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"Competition Is The Highest Form Of Consumer Protection"

Deborah Feinstein
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Re: Proposed Staples/Office Depot Merger

Merger Position: **STRONG OPPOSITION**

I am writing today with respect to the proposed multi-billion dollar merger between **Staples Office Supplies (SOS)** and **The Office Depot (TOD)**. On behalf of **America's consumers**, **The California Alliance For Consumer Protection** and **myself**, we would like to go on record as **STRONGLY OPPOSING** the merger between **SOS** and **The Office Depot**.

The specific reasons for our **OPPOSITION** to this merger are outlined in more detail below. Combined they can be summed up as follows: "Timing and repackaging are important concepts to pay attention to for any product, service, deal or mergers; but repackaging the same 'stale' product some 20 years later in the hopes that it will look 'fresh', still makes a bad consumer deal, a bad consumer deal".

As such, we support your initial 1997 ruling on the merger and ask that the **Federal Trade Commission** (**FTC**) deny the merger again. In support of our position, we hope that the **FTC** will reissue an updated and expanded ruling that mirrors its 1997 ruling that stopped the last **SOS** and **TOD** merger.

CONCEPTUAL ARGUMENTS: *Arguments in Opposition - Summary*
Our arguments against the merger fall into four basic areas and the questions that need to be answered:

1) **Competition:** Does this merger enhance or hinder market place competition?
2) **Consumers & Economic Impact**: Does this merger enhance, expand and protect consumer purchasing power or options, and/or benefit the USA and world economies?
3) **Products & Pricing**: Does this merger enhance product availability, quality and innovation?
4) **Anti-trust:** Do the possible antitrust "red flags" raised by the merger outweigh the merger's benefits?

With that in mind, and in an effort to protect the market place and consumers, we urge the **FTC** to oppose this merger. In order to do this, we support the **FTC** taking strong and swift injunctive action(s) to protect the marketplace, competition and the world's consumers by stopping this merger dead in its tracks.

Before I go on, I want to point out that our opposition arguments will be presented to you categorically (based on our Conceptual Arguments), and not in order of importance.

THOUGHTS & CONCEPTS WE HOPE WILL GUIDE YOUR DECISION MAKING:

- **What SOS & TOD Need To Show To Earn Your Approval**: The companies in this merger have to prove that they are worthy of the **FTC's** permission to merge. To do so, they have to show beyond a "shadow of a doubt" that the anticompetitive potential of the proposed acquisition is offset or reversed by the merger's efficiencies. With that in mind, we believe that the merger's negatives outweigh its positives. As such, if **SOS** can't show and prove market place positives, the merger should be denied. Overall, although the actions of **SOS** will be more efficient and increase profits for shareholders, the merger and their actions will not benefit consumers, the market place or the economy for reasons outlined in this document (below).

- **Horizontal merger**: Since the merging companies are from the same industry, are consolidating, have had contact with each other, and provide the same goods and services to the market place, we believe that the best merger evaluation formula to use is the **FTC's Horizontal Merger Criteria**. This criterion is used when large companies are merging in an attempt to create more efficient economies of scale.
- **Coordinated interaction**: This is the 2nd time that this merger has been proposed. Since the first proposal some 20 years ago, these 2 companies have not only met on the economic battlefield, but in other places where industry professionals meet – with the largest being at Analyst's Conferences. Realistically, some type of interactions/conversations/actions between the 2 companies have taken place over the years. When combined with the fact that mergers of this size 'just don't magically happen", we realize that some discussion, planning and then implementation takes place. This is especially true when the merger is not based on a hostile takeover, but rather by agreement of the two Boards of Directors. As someone who believes in the old adage that: "you keep your friends close and your enemies closer", it's not a stretch of the imagination to think that **SOS** and **TOD** have each kept track of each other's actions, interacted professionally and have taken the time to study the competition so that they could plan their corporate actions against each other. In fact, taking this just one step further, a conspiracy theorist could create a case that the 2 companies orchestrated the merger 3 years ago, and that the merger you are reviewing is a follow-up consolidation proposal, specifically designed to help them control and dominate the market place.
- **Efficiency:** In the long run, one has to ask 2 questions: 1) does this merger actually save money and 2) will the consumer benefit? The question's answer depends on which side of the coin you are on. On the corporate side, **TOD** and **SOS** must show that this merger will save <u>additional</u> operational overhead and lower their bottom line more than they are required to do by their shareholders. On the consumer side, they will initially see a flood of product on the market, temporarily lowering prices. But, as inventory contracts and dwindles, the savings will be short lived, especially as hidden operational costs are passed on to them.
- **Merger Costs Passed On To Consumers:** No matter which side of the coin you are on, this merger will add to the cost of doing business, and those costs will be passed on to consumers through higher prices. Higher prices lower consumer purchasing power and are less efficient in the market place.

COMPETITION FACTORS:

- **3 (Not 2) Of The Top 5 Companies Are Merging Into One Giant Company**: There is an old saying, "Those who do not learn from history are doomed to repeat it". Recent history shows us that less than 3 years ago, 2 of the top 5 office supply companies in the world merged with the approval of the **Federal Trade Commission.** Strangely enough, before the dust settles and we get to see the results of that merger, this merger comes before you. If allowed, that means that over a 3 year period, 3 of the top 5 office supply companies in the world will have merged into one mega corporation. As a result, when (and if) this merger is completed, the new **SOS** will control more market share than any other office supply business has before. The mere size of the new **SOS** will have a clear impact on competition, pricing and inventory control in the national and international market place(s).
- **Wal-Mart & Amazon Are NOT SOS's Competition: SOS** has been quoted in the press as saying that **Wal-Mart** and **Amazon** are their competition, and as such, the merger should be approved. This is a red hearing argument because **SOS** is an office supply store first and foremost, while **AMAZON** is a fulfillment store and **Wal-Mart** is a retail outlet. Here is a quick comparison between the companies.
    a. **SOS:** Has stores with inventory specifically dedicated to a market segment entitled office supplies. And as stated before, they are not a general retail store like a **Sears** or **Wal-Mart**. Additionally they are not a fulfillment warehouse like **Amazon** is. We do note that both **Amazon** and **Wal-Mart** carry office supplies, but don't specialize in them. Since they sell these products, they do devote a small amount of floor space to them, but not the entire store like **SOS** does. If **SOS** is allowed to use this principle in the market place, they could stretch the concept to just

about anyone and say that stores like **Sears** are their competition because they sell “back to school supplies”.

b. **Amazon:** Once you get past the products that it carries, I would like to point out that **Amazon** doesn’t have “retail outlets” like **SOS** does. In fact, with no retail space, **Amazon** acts more like a middle man or fulfillment service between the product’s seller and buyer than they do as a retailer. As such, the comparison between **SOS** and **Amazon** does not hold up.

c. **Wal-Mart**: This international business is a hybrid between the **Staples** and **Amazon**. Like **SOS**, **Wal-Mart** has retail stores that the consumer can walk into and directly purchase products. In many locations, they also have a catalog service that they can order and purchase from. Additionally, they do have some delivery services available, and the costs for those services are usually based on a variety of factors, with the location being the biggest. When asked what they are, they will tell you that they are a retail store that carries over 50,000 items, some of which are office supplies. The best way to judge the competition is to compare it financially. In a nutshell, the dollar amount of office supply products sold by “the competition”, when compared to the overall total dollar amount in by **Staples**, is minimal**.**

d. **Internet Competition**: In today’s market place, all small, medium and large companies have websites. To judge a company and its operational effectiveness on the internet, we need to understand what the purpose of their website is, especially when they are being used as examples of the “competition”. Because of a website’s importance in the business world, **Staples**, **Wal-Mart** and **Amazon** all have web sites, and they all provide different functionalities. These functionalities are based on the corporation’s needs, the time of the year and the products being sold**.** On one hand, the **SOS** website highlights advertised products that are for sale or on special, and are usually advertised in media. They also allow you to search for items by category. Additionally, they often take orders, fill them and consumers can come in and pick up their purchases. As an additional service, the products can often be sent to the customer by a delivery service for more money. The costs depend on the product and where its being sent. On the other hand, the **Amazon** web site is designed to sell product for themselves and others, and have those products delivered to the purchaser, usually free and often in one day! As a Fulfillment warehouse, they have no retail floor space and thus no foot traffic. This raises a question, namely how can **SOS** compare themselves to **Amazon**? In fact, to take the analysis just a bit further into the future, ***the 60 Minutes TV Show*** recently showed America what **Amazon’s** has planned for its delivery service in the future - to use drones. Although possible, no one else has this planned. (FYI: I was watching TV during the NBA Finals, and an **Amazon** ad came on commenting about their soon to be “use of drones”. This is a service that **SOS** doesn’t provide, and if and when they do, they will probably contract out with **Amazon** to handle it!). Is that how the competition works? This clearly shows that one company wants to bring you into the store, while the other doesn’t have a store to bring you into! As a result, their website focus is different, their markets are different, and their competition is different.

- **Product & Inventory Control**: Because of its to-be-size, the new **SOS** will have the ability to control inventory in 2 different ways. First, once this merger goes through, **SOS** will limit shelf space for old, current and future products, especially as they close stores. Less shelf space stifles the sale of old and new products. When the amount of inventory they control is factored in, the problem becomes worse. Second, **SOS** will be in indirect control of the creation, development and deployment of new products in the market place, based on two factors. First, they will slow down the purchasing of ‘new’ product until the old is sold off. Second, since they control more shelf space than anyone else in the industry, if a company or product is liked by the **SOS** Board of Directors, it will get shelf space, and if they don’t, they will get nothing. What makes this terrible is this: if the vendor is turned away, where do they go next to sell their product, especially if the market contracts and has nowhere to go because everyone has merged or has been forced out of business? Combined, these 2 actions will allow **SOS** to put a stranglehold on the supply and delivery of old and new office supply products to national or international markets. This will clearly hurt competition and consumers, and will manifest itself in market place inventory shortages and higher prices.

- **Threaten Competition**: Upon the merger's completion, the new **SOS** will control a huge market share and be so large that one of two things will happen. First, in an effort to effectively compete, others will be forced to merge even if they don't want to. Second, **SOS's** new size will scare-off those who wish to enter the market and compete. Combined, these actions will limit consumer options and raise prices, especially as stores are shuttered and jobs are eliminated.
- **Competitive Benefits**: Although **SOS** & **TOD** can point to specific competitive benefits for themselves and their shareholders, we believe that they will be hard-pressed to identify any benefits that the merger brings to the market place specifically, and consumers, generally. In all fairness to **SOS**, they are doing their job and what their shareholders expect and require of them - cutting the fat and saving money. This increases share value and profits. Unfortunately though, will the benefits **SOS** reaps be above what is expected, and are they being earned at the expense of consumer purchasing power?

CONSUMER & ECONOMIC IMPACT:

- **Inventory Control: SOS's** control over market supplies will allow them to manipulate inventory on a vast scale, creating shortages in targeted markets that will result in increased prices. What is really scary is this: because of its size and use of technology, as well as market share, **SOS** can (and will) target specific geographical markets (and businesses), and force the competition to adopt the **SOS** pricing scheme/criteria or go out of business. Some can view this as a backdoor way to fix prices. Second, we believe that fewer products will be in the market place and as such, supplies will dry up as stores are shuttered and excess inventory is sold off. Third, once stores start closing, consumers will have to drive further to get the "best price available" via competition. This will clearly cost more for everyone in the long run. For example, I live in an area that has 6 **SOS** stores and 3 **TOD** stores within a 20 mile radius. Obviously, once the merger takes place, **SOS** will close stores. The questions I have are: Which stores will be shuttered? How will the decisions be made on which stores to close? Will all stores sell the same products at the same prices once consolidation takes place? How many employees will be laid off? How far will I have to drive to purchase product and 'save money"? What impact will these negatives have on the industry? How will these store closures affect the economy?
- **Bait and Switch**: This merger allows for the expansion of **"Bait and Switch Programs"**. These programs can occur thanks to artificial product shortages or market manipulations by **SOS**. The conventional wisdom is that once in the store, the consumer will hear the following lines: "oh, I am sorry, we ran out of item "A" (or item "A" is no longer for sale), but we have item "B" in stock, and it's just as good… and it only costs a few cents more!
- **Small Business Threats**: This merger poses a significant threat and harm to currently operating small businesses because it will effectively kill market place competition, limit shelf space and impact businesses around the world. As a result of their soon-to-be size, the name **SOS** alone will strike fear into future competitors, dissuading them from entering the market place. That equates to less stores, shelf space, and competition in the market place. This leads to market domination and higher prices.
- **Future Industry Mergers**: As mentioned above, this merger will "force" others in the industry to explore and undertake mergers in an effort to simply exist or compete in the market place, whether they want to or not. It will also force businesses that have no one to merge with, to simply go out of business. And this raises both red flags and questions, with the largest being this: if no small businesses exist, and large corporations merge, how many more mergers like this will come before the **FTC**? That is followed up with this: at what point will you draw a line and say enough, is enough? Additionally, what guidelines will the industry walk away with respect to mergers and market share once you issue a ruling? Finally, right now this action is within the jurisdiction of the **FTC**, how do we keep this from ending up in court?
- **Unfair Size**: As stated above, it's well known that **TOD** recently merged with **Office Max,** creating a giant entity. At the time of the merger's approval, it was assumed that **SOS** would be its main competition. With **SOS** gobbling up the competition, the proposed merger between **SOS** and **TOD** is

downright scary. If approved in its present form, the **FTC** will have allowed 3 of the top 5 Office Supply Companies in the world to merge into 1 entity within less than 3 years.

- **The Creation & Production of Product**: As mentioned above, this merger will affect both inventory and the sale of new and used products in the stream of commerce in two ways. First, **SOS** will have the ability to control and manipulate inventory. This will help them control not just the market, but the price of products, as well as unfairly target competition. Second, as mentioned above, this merger will have a direct impact on the improvement and development of products that are produced and distributed in North America and around the world. The scariest part of this merger is this: **SOS** will be in a position to either flood or withhold products from the market place, meaning that if a company doesn't "play ball", they might lose their shelf space, market share, or simply not even get any shelf space in their stores to have a market share. In the long run, that means that fewer products will be in the stream of commerce, and this will create artificial shortages that increases prices. As a result of artificial product shortages, **SOS** will be free to charge more for product, increasing their bottom line at the consumers expense. This is great for shareholders, but not for consumer purchasing power.

PRICING & PRODUCTS:

- **Price Fixing**: This merger threatens the current low prices that competition brings consumers. Because of this merger, **SOS** will be able to control vendor product production, pricing, and thus be able to charge what they will for products based on artificial shortages that they create. Additionally, a case can be made that with only one large player in the market, this merger lays the foundation for price fixing. The definition of price fixing is: "the maintaining of prices at a certain level by agreement between competing sellers". In this instance, with the top 3 industry leaders merging, there won't really be any competition, and the new entity will be able to do what it wants because of their size, allowing them to dominate the market and establish market prices others will have to follow just to stay in business.
- **Convenience**: **SOS** states that there is competition in the market place, and that it will grow. In reality, I have shown above that **Amazon** and **Wal-Mart** are not **SOS's** competition. We have also shown that there will be fewer stores in the market place, and that equates to less competition. In fact, as they shutter stores, consumers will have to travel further to purchase product, wait in longer lines and pay more for the same product. Is this convenience? Is this saving money?
- **Product & Service Related Problems**: This merger will affect the production of products and services **SOS** currently supplies to the market place in the USA, North America and world. This will benefit **SOS** at the expense of consumers. As a direct result of this merger:
    - IT services currently provided by both companies will disappear in many areas, especially in rural or remote areas that they currently service.
    - Competitive prices for those services will disappear, allowing all existing to charge what they want in any market place they operate in.
    - A lack of shelf space will produce a lack of places to sell products. This will decrease consumer choice and purchasing power.
    - Product innovation will be stymied as shelf space dries up.
    - Consumers will pay for the merger through higher prices and less convenience.
    - Product quality will drop thanks to less product flowing in the stream of commerce as places vendors can sell their wares disappear. As such, new product producers won't be able to earn enough money to either produce the product they have, or enhance their products, so they'll start "cutting corners" on the product to simply get it on the market. In the long run, this will lower product quality and harm consumers and their purchasing power.

ANTI-TRUST: Possible "actionable" areas

- **Monopoly**: Thanks to 3 of the top 5 companies merging in the last 3 years, this merger gives **SOS** a huge market share to control, threatening competition. If the **FTC** supports this, it will ultimately be supporting the creation of a defacto monopoly because there will be no one to compete against them.

Generally speaking, there is nothing wrong with being “big”, but there is a problem with being too big. Combined, **TOD** and **Office Max** are big, but when you factor in the **TOD** and **SOS** merger, they will be GIAGANTIC.

- **Market manipulation**: Because of the size of the new company, **SOS** will be able to manipulate selected markets in their favor and at consumer’s expense (please see comments above).
- **Price Fixing**: As a result of being too big, **SOS** will be able to conduct price fixing schemes thanks to their control over inventory (please see comments above).
- **Section 7**: Antitrust laws require that as a predication of the deal, this question needs to be asked and answered: *Will this merger lead to more or less competition?* The answer is quite clear: this merger will lead to less competition in the market place.
- **Economic Harm**: This merger has both positive and negative aspects to it. On the positive side, **SOS** will make more money, especially for their shareholders. On the negative side, the merger will hurt consumer purchasing power by leaving the company free to do whatever it wants in any market that it chooses to operate in. Those actions include, but are not limited to closing stores, controlling inventory, targeting its competition, raising prices and firing employees. All this will impact not just the economy, but consumer wallets.

CONCEPTUAL ARGUMENT CONCLUSIONS:

Here are our conclusions to the above conceptual areas:

1) **Competition:** In summary, we believe that this merger does not
    a. Enhance market place competition, rather it eliminates it;
    b. Have small players, rather it has HUGE players that will exist not just today, but tomorrow;
    c. Enhance or spur competition against anyone (especially on the internet),
    d. Do anything to address the huge inventory that **SOS** will control; and
    e. Provide the market place with quality competitive benefits.
2) **Consumers & Economic Impact**: In summary, we believe that this merger
    a. Does not enhance, expand and protect consumer purchasing power or expand options;
    b. Does not benefit the USA and world economies;
    c. Has a direct impact on inventory control – it gives **SOS** a HUGE inventory to control;
    d. Fosters **Bait** and **Switch** programs;
    e. Threatens small business and future competition;
    f. Reduces overall shelf space for product sales and consumer choice;
    g. Fosters more mergers, especially amongst those who are on the verge of bankruptcy; and
    h. Gives **SOS** a huge market in which to dominate and control.
3) **Products & Pricing**: In summary, we believe that this merger
    a. Does not enhance product availability;
    b. Does not lower overall prices, especially when consumers will pay for the costs of the merger through higher prices;
    c. Fosters price fixing;
    d. Threatens consumer convenience; and
    e. Threatens quality and innovation.
4) **Anti-trust:** In summary, we believe that this merger
    a. Is filled with anti-trust pitfalls that will cost consumers money and wind up in court;
    b. Creates several residual issues that will wind up in court;
    c. Has an impact on monopoly status;
    d. Allows for market manipulation;
    e. Enhances price fixing opportunities;
    f. Doesn’t comply with Section 7 requirements; and
    g. Can have long term economic harm.

Solutions:
In our view, there are two avenues to stroll down with respect to solutions. On the easy side, the **FTC** can deny the merger using the powers Congress and courts have recognized. We believe that **Section 13(b) of the Federal Trade Commission Act** allows and empowers the **FTC** to grant and move for injunctive relief. These powers should be used to deny the merger, just like they were the first time.

But, should the **FTC** decide to stroll down the second avenue of allowing the merger, it should be done with conditions. We hope that they the following actions will be taken:

- All parties should reach a profitable agreement before any actions are approved and the merger formally takes place.
- **SOS** should be required to divest certain parts of their business to stimulate competition in various markets and give them less control over the actual market place. After reviewing various parts of their business, we would like to suggest that the following parts be divested:
    - Require that their IT section continue to service the areas that they close shops in for up to 5 years after they close shops or until the computer services center is sold.
    - Their computer service center should be spun off within 2 years.
    - Their in-store photocopying and printing business should be phased out within 6 months because there are enough places in the market place that provide these services.
    - Their "in house insurance warranty program(s)" should be spun off and be provided by a 3rd party – preferably an insurance company.
- Additionally, **Stapes** should be required to increase consumer protection(s) by:
    - Agreeing to a series of clarifying rules that cover their computer services operation(s).
    - The **FTC** should require that 20% of the chain's inventory should be new products and inventory, and that this standard should be in place for a minimum of 5 years. This will ensure that new products will be purchased, created and flow into the stream of commerce.
    - Require that 55% of all products sold in their stores be produced in the USA.
    - That a restructuring of the **SOS** board occur, and that 5 persons be added to the corporate board that are not company shareholders. These board members will represent consumers, and be called Consumer Advocates.
    - A price freeze should be established on all inventories at the time of the mergers approved.
    - Increase employee and consumer education programs.
    - Provide to-be-negotiated levels of training for all employees.

Conclusion:
As you can see from our arguments, we believe that the merger should not take place because a lot of questions are left unanswered. To us, the crazy part of this merger is that if all arrows are pointed in the right direction, it would actually put **SOS** in a position to lower prices, <u>if they wanted to</u>. And although **SOS** can use efficiencies of scale to cut prices that benefit the consumer, the real question is, will they?

With these thoughts in mind, we respectfully request that you oppose the **SOS/TOD** merger.

Sincerely;

Michael Ross
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