UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

FEDERAL TRADE COMMISSION,	)	
	)	
et al.,	)	Civil Action
	)	No. 15-2115
Plaintiff,	)	
	)	Friday, April 1, 2016
v.	)	9:15 a.m.
	)	
STAPLES INC., et al.,	)	Washington, D.C.
	)	
Defendants.	)	

DAY 8 - MORNING SESSION
TRANSCRIPT OF PRELIMINARY INJUNCTION HEARING PROCEEDINGS
(EXCLUDING SEALED PORTIONS)
BEFORE THE HONORABLE EMMET G. SULLIVAN,
UNITED STATES DISTRICT COURT JUDGE

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C O N T E N T S

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MORNING SESSION, APRIL 1, 2016

(9:20 a.m.)

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(Thereupon, the following proceedings were closed by order of the Court and are not included as part of the transcript production in this case.)

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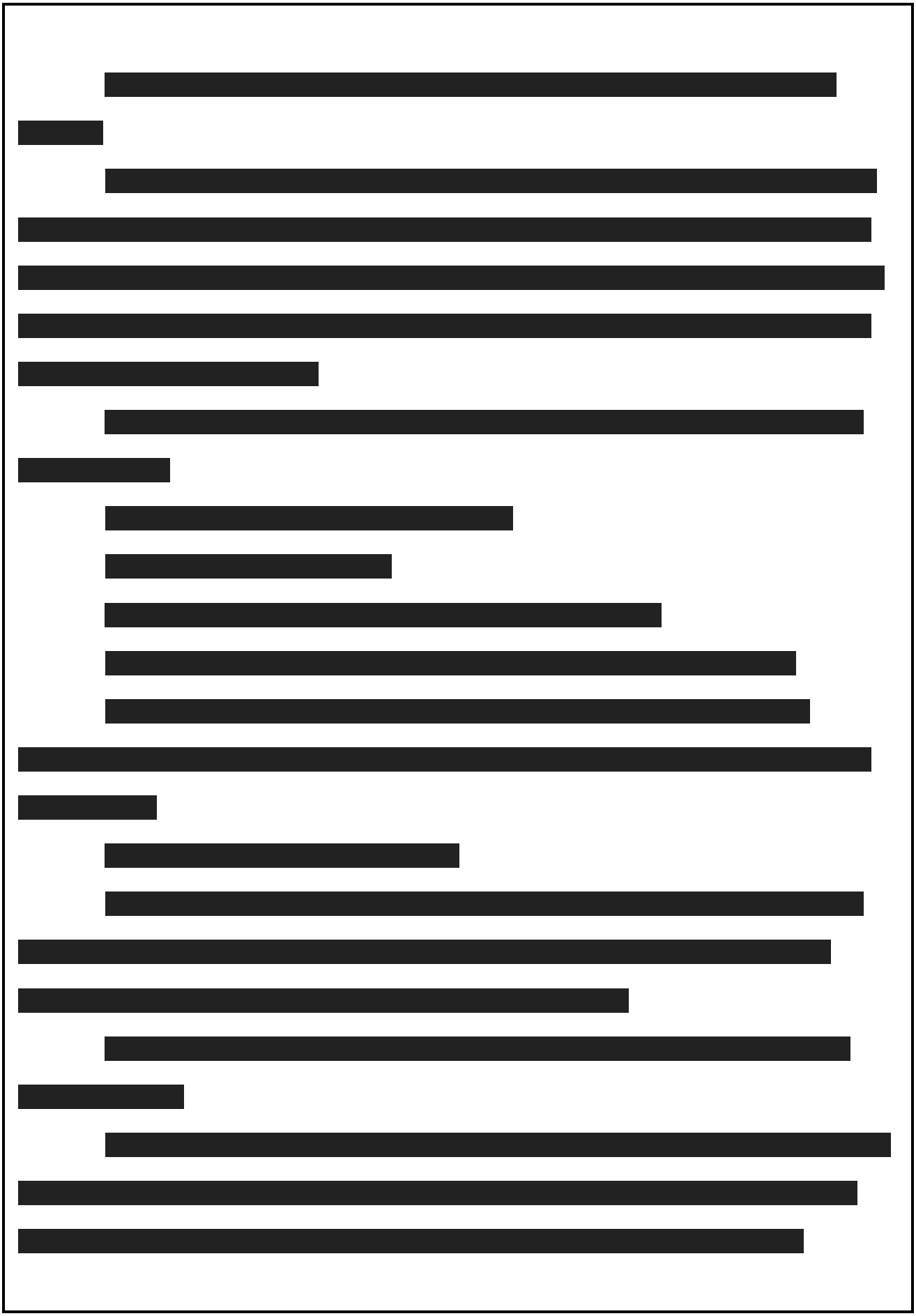





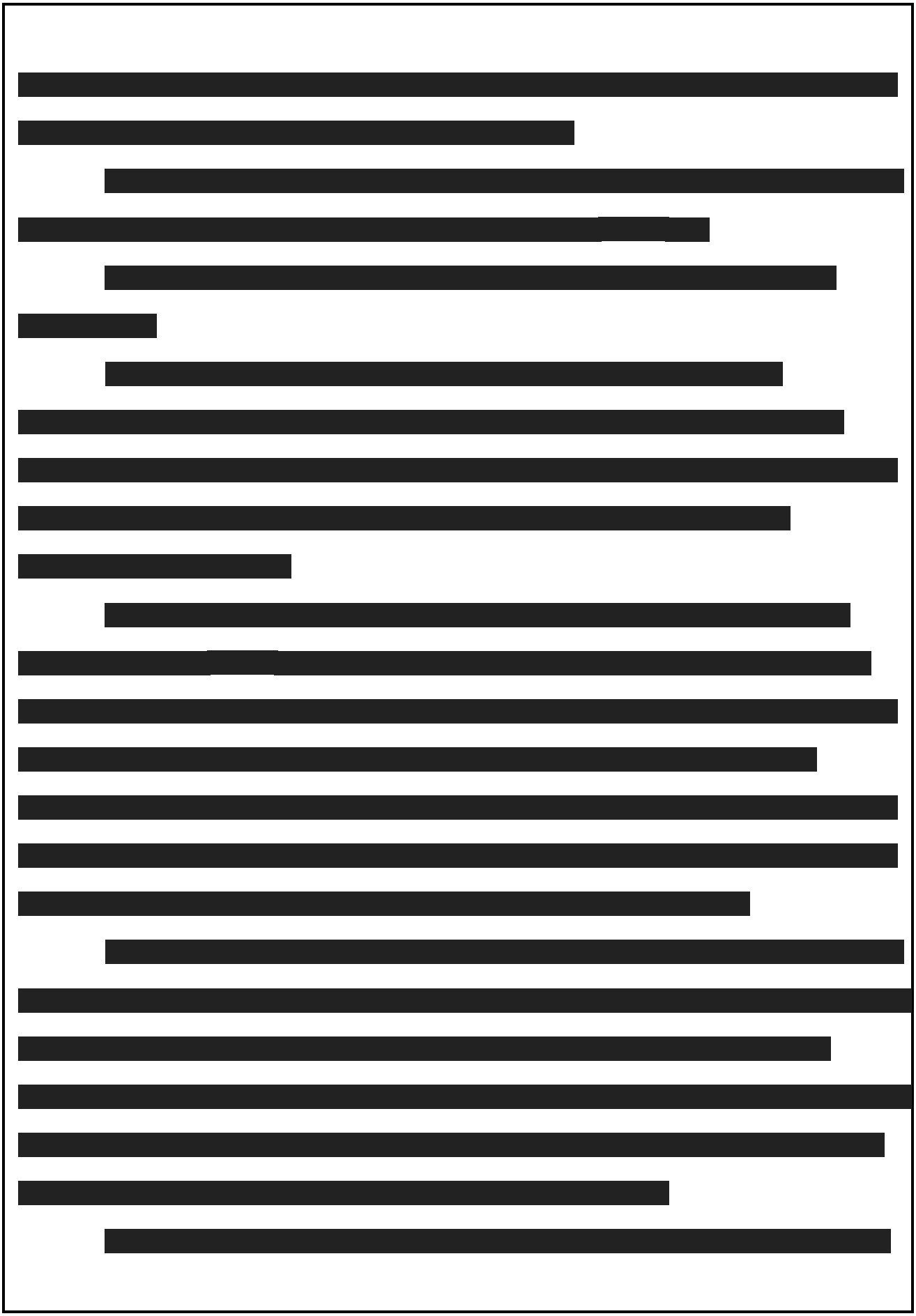



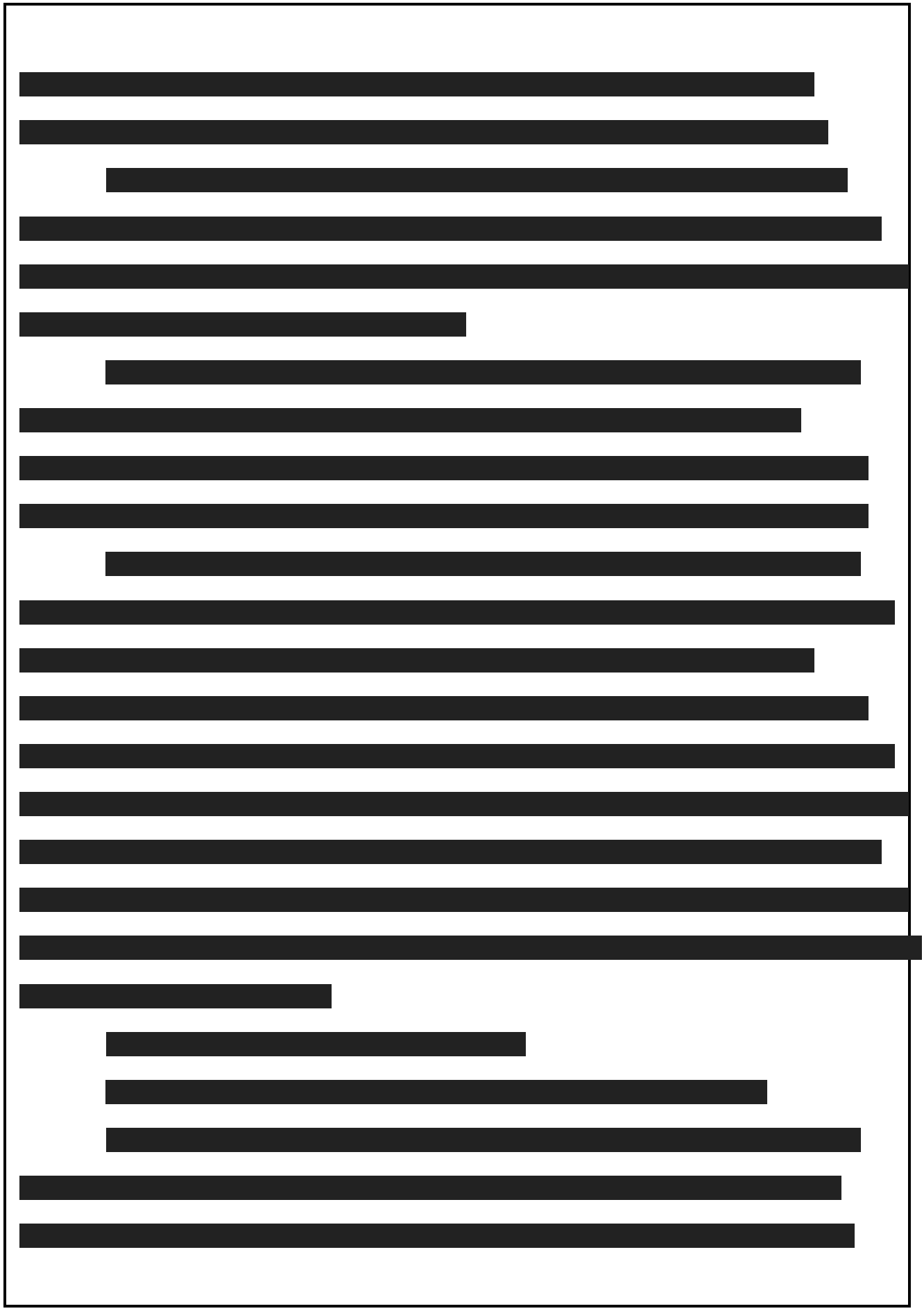











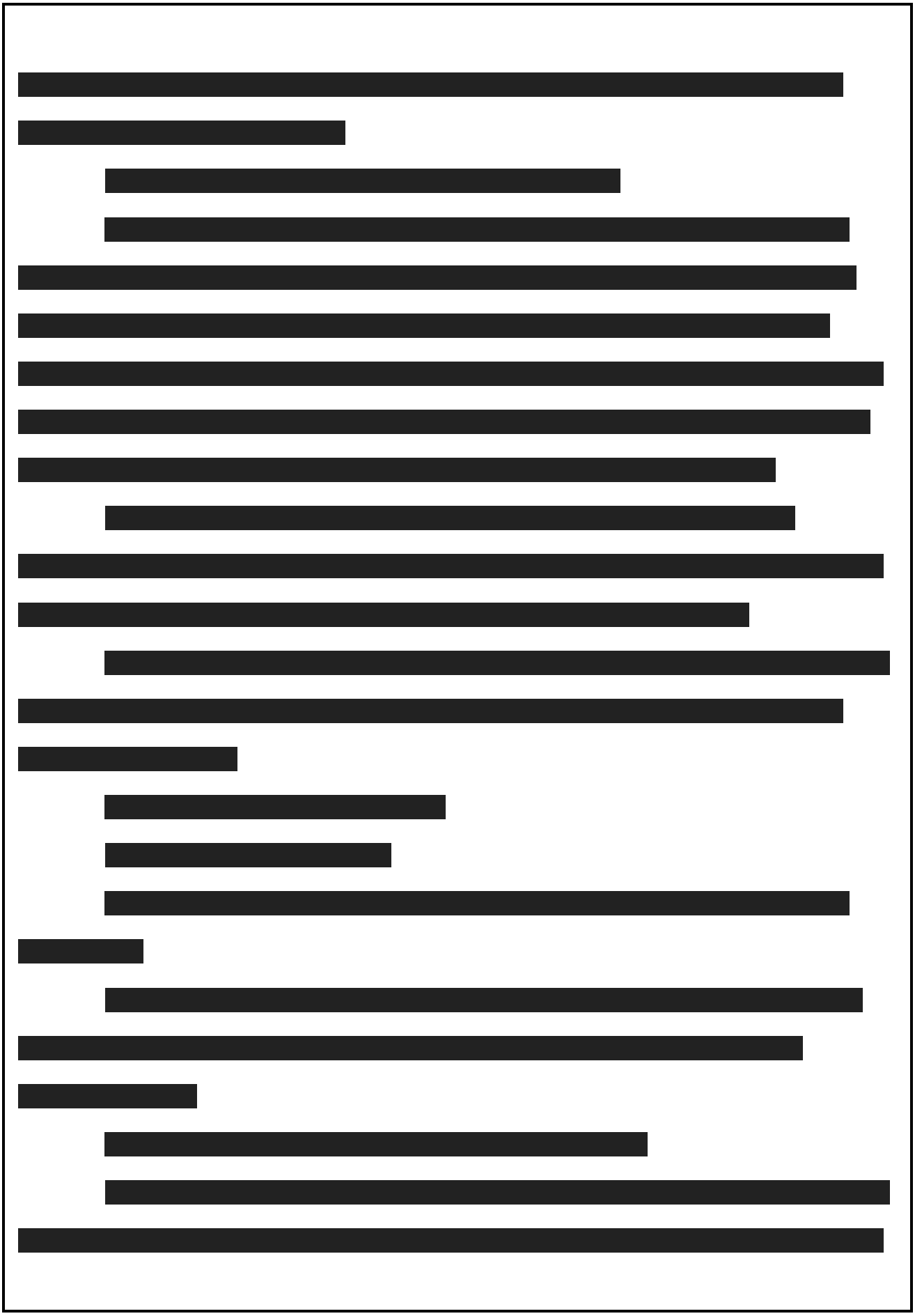











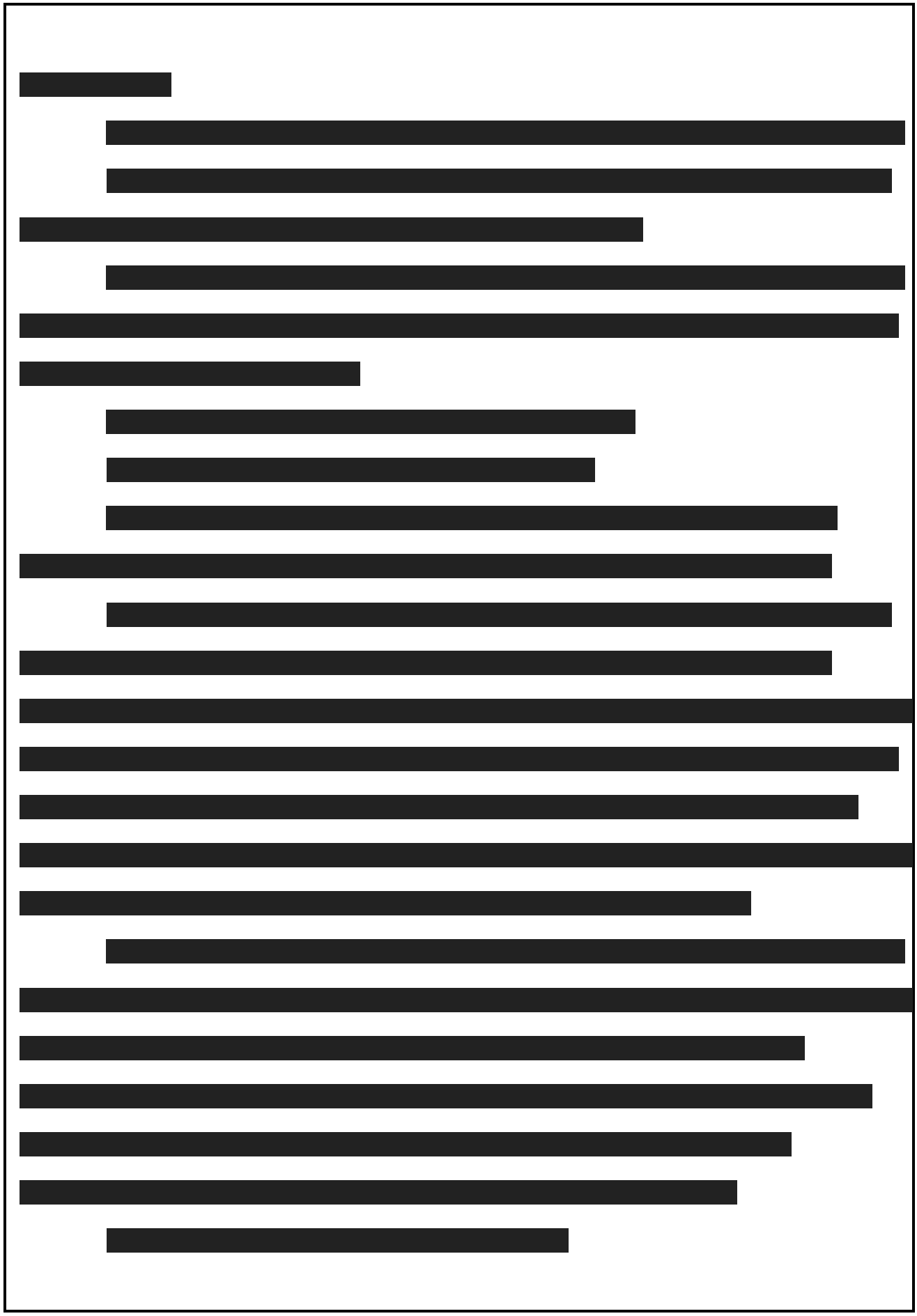





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(Previously designated closed proceedings concluded and the following further proceedings were held in open court.)

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(Thereupon, a break was had from 9:50 a.m. until 10:00 a.m.)

THE COURT: Please be seated. Good morning. How are you?

THE WITNESS: Fine, thank you.

THE COURT: Counsel, are you ready to proceed? All right.

UNIDENTIFIED SPEAKER: Your Honor, if we could have one minute.

THE COURT: Oh, okay. All right.

UNIDENTIFIED SPEAKER: Your Honor, they're on their way.

THE COURT: That's all right. Okay.

All right. Counsel, good morning.

MS. CERILLI: Good morning, Your Honor.

THE COURT: All right. Good morning, sir. How are you this morning?

THE WITNESS: Fine. Thank you.

THE COURT: Good. Go ahead, Counsel.

MS. CERILLI: Okay.

CONTINUED DIRECT EXAMINATION OF CARL SHAPIRO

BY MS. CERILLI:

Q. Professor Shapiro, yesterday you walked us through the

definition on the relevant market and your conclusion that the sale and distribution of consumable office supplies to large customers is a relevant market.

Now that you've defined the market, what is the next step in the analysis?

A. We're going to measure the market shares in that market.

Q. And what do antitrust economists learn from market shares?

A. Well, it's, again, dovetailing with the case law. We look at the --

THE COURT: You know, can I stop you? Before we get into the next category, I understand the definition of the hypothetical monopolist test. The algebraic formula, though, I need you to explain that in a little more detail.

THE WITNESS: Okay.

THE COURT: It's slide 18, I think.

THE WITNESS: All right.

THE COURT: And how do you arrive at those figures that are -- the ones that are not shaded?

THE WITNESS: Well, okay. The -- let me just first say -- so there's a standard formula. It's in appendix -- so I have a whole report here we're not going to -- that we're not -- we're not going through, but Appendix D in my initial report provides the formula in the algebra.

THE COURT: Okay.

THE WITNESS: So what we do, then, is apply that formula from the literature. And you can see here, so the main formula is this recapture rate greater than 10 percent over profit margin plus 10 percent.

THE COURT: All right.

THE WITNESS: Okay. So the two things we need to measure -- let's be clear, if that formula's satisfied, then the test is met, as it says here. Hypothetical monopolist test is satisfied if this formula -- if this inequality is satisfied. So we've got to measure the recapture rate and the profit margin, plug them in, and see what we get. So the -- so that's the main empirical exercise is to measure those two variables as best we can, and then plug them in.

So do you want me to talk about how I measured them?

THE COURT: Yes, please.

THE WITNESS: Okay. So -- all right. So, again, there's a lot more detail in the reports here.

THE COURT: I know.

THE WITNESS: So first off, the profit margin, what is this margin? There's quite different ways to talk about profits. So the profit margin is how much -- let's say Staples. We can look at both companies or Office Depot.

THE COURT: Right.

THE WITNESS: Let's say Staples, when they track the business -- the consumable office supplies business of a large

customer, what's the revenue they get from it, and then what are the costs they incur to serve that customer? Okay. So this is not just going to include, you know, overhead costs, headquarter's cost. This is what economists call the incremental cost. That's basically how much extra cost are they going to have to incur to serve that customer. And we're looking at the difference between the two.

So if they take in $100 and it cost them $80 -- they take in $100 in revenue from a customer, and it cost $80 to serve, we would say the profit margin is $20 over the 100, or 20 percent.

THE COURT: Right.

THE WITNESS: The -- one of the biggest components of the cost of the distributor is how much they have to pay to buy the office supplies from the manufacturers. So we've measured that using their own accounting data, using their own, basically, internal data from the companies. And we get a range here that's shaded, depending on exactly how we treat certain costs.

The main costs that are extra costs in serving the customer -- while they have different categories on their own accounts, but certainly the cost of goods sold -- we're going use that term a lot. So what they're paying to buy the supplies from the manufacturers usually, sometimes wholesalers, and then distribution costs, the cost of delivering, and the other services they provide to the customer.

So when we do that, we get somewhat different margins for

the two companies. We get somewhat different margins between paper and the other core supplies as well, but this is the range we get, is around -- again, it's shaded, but that's -- that's the number.

THE COURT: All right. Thank you. That's been very helpful. Thank you.

THE WITNESS: Okay. Shall we talk about the other variable, then, as well, the recapture rate?

THE COURT: Sure. Absolutely, yes.

THE WITNESS: Okay. So, first, this is a less straightforward concept than profit margin. Okay. So I first have to define it. The -- basically you have, let's call it, a mental exercise. If you imagine that Staples -- again, I'll stick with them -- raises the price to large customers, they're going to lose some business as a result; and some revenues will be lost because customers will not be happy with the prices, they'll go somewhere else.

THE COURT: Well, wait a minute. You're assuming if the merger goes through?

THE WITNESS: No.

THE COURT: All right.

THE WITNESS: Okay. In the world today, the world that we're in today, if Staples were to raise the price --

THE COURT: Right.

THE WITNESS: -- they would lose some business.

THE COURT: I agree with you.

THE WITNESS: Okay. Now, another important part of my testimony is a lot of that business we think would go to Office Depot today, and that's why we're worried about the merger, because they're two head-to-head competitors. We're coming to that. At this point we're just asking if they raised the price, they're going to lose some business. How much of that business is going to go to other people distributing office supplies? If every $100 they lose, how much -- what fraction of that's going to go to their competitors versus maybe people that just won't use office supplies so much. That would be another way that they could lose business. People would say, "Fine, I'm not going to -- I'm going to use half as many pens or, you know, conserve on Post-it notes."

So the recapture rate is if they lose some business, how much of it goes to their competitors? All of the ones we've included in the market, which is all the other forms of distribution, Office Depot, anybody else, Amazon, leakage, all those things, and that's the recapture rate, the percentage that goes to the competitors.

And if you think about it -- so I think that's very high, and that was -- we covered that quickly yesterday. I think that's very high because just from everything we know about this business. And what this formula does is we plug in that number and what -- the calculations here, if you look at the last row

here, Your Honor.

THE COURT: Right.

THE WITNESS: The blue numbers on my printout, at least, that are shaded.

THE COURT: Right.

THE WITNESS: So long as the recapture rate is at least that high, then the test is satisfied. And what I'm saying is I think all the other evidence indicates the recapture rate is well above that.

Again, if Staples raises their price, the lion's share of the lost sales would go to their competitors, and so that number is well above these shaded numbers.

Now, I have not been able to empirically estimate that using -- using data, doing some econometric -- I just -- I don't -- I would love to be able to do that. In some cases people can do that. I can't measure that, so what I'm doing here is telling you I have other evidence on that point, I believe it's well north of the numbers here, so I'm confident the test is satisfied. And that's why I said it was kind of an easy call, actually, because I don't think it's close.

THE COURT: Really? All right.

THE WITNESS: Okay.

THE COURT: Thank you.

THE WITNESS: All right.

THE COURT: Counsel.

BY MS. CERILLI:

Q. Thank you.

A. So we're back to what slide now?

Q. To market shares.

A. Okay.

Q. I think you were just introducing, you know, what is that antitrust economists learn from market shares.

A. So high market shares -- well, we mostly look at the market shares of the merging firms, and if they're very high, that is a signal that we're much more likely to have an anticompetitive concern from -- in the merger of two large firms in the market.

Q. And since market shares are based on historical data, aren't they inherently backward looking?

A. Well, yes and no in the sense that, of course, historical data, that's the real world, it's backward looking. But we can do things with the data to make -- because our whole exercise here is forward looking, so there's really two things we can do, and I will do that, and have done that in other cases.

For one thing we could do is we could look at projections. The data can include projections, and we're going to have projections, such as Amazon Business is going to be the most important element here. So we can look at projections, and more generally we can look at trends.

So in other cases, for example, let's say -- well, when I

worked on the Whirlpool/Maytag merger --

THE WITNESS: Which is related to your previous deal, Your Honor.

-- and in that case that involved washers and dryers that both Whirlpool and Maytag were selling, and LG and Samsung had at that time -- this was ten years ago, 2006, had -- were coming into the U.S. with some high-end washers and dryers.

THE COURT: Right.

THE WITNESS: And one of the questions was, "Well, their shares are growing. Are they important competitors so we don't have to worry about Whirlpool and Maytag merging?" Okay. Now, the shares were very small but they were growing. So I did a projection looking out a couple years, if their shares grew the way they had been growing, what would the concentration in the market shares look like.

So if you have reliable data for making these projections, then you should use it so we can be as forward-looking as possible with data that, again, is reliable.

And I'm going to do that here.

THE COURT: All right.

BY MS. CERILLI:

Q. And we'll obviously talk about the additional steps in the analysis, but can you just briefly reset us here?

How do market shares fit into the overall structure of the merger analysis?

A. Well, we had the very steps, market definition, market share, that then we're going to get to competitive effects.

They're an important piece of data to economists, and I note in the case law, and really -- but it's one piece of information. When I see high market shares, then you want to go to the next stage of the analysis and see, well, will there be competitive effects, am I missing something, are there other players who have small shares who are going to be a discipline entry?

So it's one step along the analysis; but it's, again, like any one piece, it doesn't give -- it doesn't dictate the result.

Q. Okay. And Professor Shapiro, what is your opinion regarding market shares in this matter?

A. I believe the combined market share of Staples and Office Depot, our best estimate is 79 percent combined. And that's the next slide, which is, I guess, not redacted? Okay.

So this is the primary historical -- I'll call it historical, this is 2014 data, market shares: 47 and 32 percent for the two companies for a combined share of 79 percent. That's my primary conclusion regarding market shares.

Q. And we're going to go through the details, but can you just briefly explain how you generated these shares and what this is showing?

A. So we are going to talk about this. So if you see on

this -- we're still at slide 20 -- it says Fortune 100 customers and then 2014.

So this -- these pie charts, these shares are generated based on I'll say extremely detailed analysis of the data and responses from the Fortune 100 companies in response to, I guess, CIDs and back and forth generally between FTC going to all of these hundred companies and trying to get information about their purchases -- excuse me -- of consumable office supplies.

So that's the basis for these numbers.

Q. Okay. And did you look at other data sources to confirm these findings from the Fortune 100?

A. So yes, I have another measure, which I call primary vendor shares, which is based on data from the suppliers.

So the Fortune 100 data, that's customers, a particular set of customers, and then we have another data set from the suppliers which has some advantages and disadvantages. All in all for the purposes of measuring market shares, these are the better data, in my opinion, the ones here with the Fortune 100, but they're very much corroborated by the other data set from the suppliers. And we have many other pieces of evidence that line up with this, the bidding data that we've talked about and will return to, for example.

Q. Okay. So let's first take a more in-depth look at the Fortune 100 market shares, which you said is your best estimate

of market shares here.

How did you calculate market shares using the Fortune 100 data?

A. So I already made -- said that was a pretty extensive bit of work.

So each Fortune 100 company was asked by the FTC -- and there were multiple rounds of going back for more information -- about their purchases. And so all that information came in. This is over a period of months. And my staff was participating in that exercise, and looking at the information, and asking more questions, and so forth.

And then when we did that, the -- the tricky part really was to do two things: Break out consumable office supplies from other purchases that these companies made, to the best we could, and then to allocate -- figure out which vendors, which suppliers they bought from so we could attribute shares. Okay.

And each of these is quite a -- I'll say messy. It is messy, you know, because each company has a different accounting system and different records, and they responded in terms -- rather incompletely and we couldn't use them; others more completely. So it's very much a hand-crafted work, okay.

When I say that -- well, I don't know. I guess I'm very thankful to my staff. Okay. So you know it's not cookie-cutter stuff. Okay.

THE WITNESS: And, again, you can see that, Your Honor,

it's a plus or minus; and, you know, I'm happy to go into any level of detail about how we did it. We'll talk a little bit about how we, in my view, when we -- when things were ambiguous, we attributed more sales to the smaller competitors -- the smaller firms so that our share -- if anything, we've juiced up their shares, if you will, by just -- because of ambiguities in the data.

If I can direct your attention -- Your Honor, I think you have the binder with my reports in it as well.

THE COURT: I'm sure I do.

THE WITNESS: Okay. So --

THE COURT: In fact, I do.

THE WITNESS: Yeah. So I'm not necessarily encouraging you to turn to it right now, but there's a -- there are a good number of exhibits on market shares there that have a lot more detail than we're displaying for you here in court.

Then there are appendices. So in the first report, there's an appendix on how we process the customer data from the Fortune 100. There's another appendix, G, on how we -- the first one is E. And Appendix G, on how we process the data from the competitors. And then in the appendix responding to certain criticisms, there's another appendix, Appendix C, on how we -- we're essentially defending our approach to processing the Fortune 100 data.

So there's a lot of detail there in terms of exhibits and

text about what we did.

But the main thing is, basically, our best efforts to figure out which purchases were involved, consumable office supplies, and from whom, so we could calculate these numbers.

BY MS. CERILLI:

Q. Okay. Dr. Shapiro, did you receive data from all of the Fortune 100?

A. Well, not usable data, okay. So we ended up determining that 81 of the hundred companies we felt that was accurate enough and detailed enough the way we could break things out. So some companies, large companies, only gave us a part of their company information. Others didn't disaggregate things at all.

THE COURT: What about Amazon?

THE WITNESS: Amazon is one of the ones we could not use. I know they -- either the -- their primary vendor is either Staples or Office Depot, I can't remember which one; they buy a lot. We have an exhibit on that. They buy -- I don't know the number, but a large volume of office supplies from one of the two companies.

They did not provide data about their own -- other purchases from other sources. Again, this is their own purchases, right, we're talking about as a customer.

THE COURT: Right, right.

THE WITNESS: Okay. We'll get to them as a supplier before. They are in the Fortune 100 so we asked them.

THE COURT: Right.

THE WITNESS: They are one of the 19 that we couldn't use, but we did -- I know, and we have -- I won't turn to it now.

THE COURT: You can if you want to.

THE WITNESS: Okay. Give me one moment then.

(Brief pause in proceedings.)

THE WITNESS: I will find it, I promise.

THE COURT: Take your time.

BY MS. CERILLI:

Q. I believe it's R1A.

A. Which one?

Q. R1A.

A. No, no. That's not it. There's an exhibit -- okay. I'm still looking for it. I'm going to find it. We have an exhibit of all the companies whose data we couldn't use, the 19. And it shows how much they buy from Office Depot and Staples; and that's the one I'm having trouble with.

THE COURT: Take your time.

BY MS. CERILLI:

Q. I'm sorry, it's slide 30.

A. We have it as a slide?

Q. Yes.

A. Uh, even better.

Q. And I'm sorry, we just have to be a little careful because the names of these are confidential.

A. Okay. Thank you.

All right.

THE WITNESS: So do you have slide 30 for -- okay.

And you see the -- so these are the names -- you see the redacted part of the 19 names. You'll see down there, fourth one lists -- I shouldn't say -- okay. One of the ones list -- I already said it.

So Amazon is listed there with a corresponding number, okay. So what we did -- so in one of my appendices, Your Honor, it describes for each of the 19 companies why we felt that company's response was not detailed enough to use for the data set. So there's that.

And then what we figure, well, let's go back, because I was criticized by Mr. Orszag, these 19, you know, that was biased and, you know, maybe we -- they should have been included or it's a problem.

So one thing we were able to do is go back for each of those companies, and Amazon is one of those, and see how much did they buy from Staples and Office Depot; because we have the Staples and Office Depot data on their sales that we can find it. And you see the number here, and let's just say that's a big number.

THE COURT: Right.

THE WITNESS: Even for Amazon. So -- in general among the large customers, that's a big number. So that gave me some

comfort that it wasn't as though we were, you know, excluding companies. The companies that didn't give us sufficient responses, they're also shown here, large customers, Amazon and a number of others.

THE COURT: Thank you.

THE WITNESS: Okay.

BY MS. CERILLI:

Q. Okay. And Professor Shapiro, you alluded to the fact that these were a hundred data sets that took months to process, and I think we -- we'd probably be here until May 10th if we were to go through all of the nuances in them, so I appreciate that you referred the Court to some of the detailed backup. And I'd like to still go through kind of some of the conceptual issues for the Court's understanding.

So what is it, just getting us started, that you and your team did when you received these data sets?

A. Okay. Well, can we -- we just tried to segregate out -- first, was the response sufficient to work with and disaggregate; and then break out basically product, the consumable office supplies; and then vendors. The whole point of this is it's not going to be useful unless we can figure out who the supplier is and attribute shares to that.

So that's the basic step.

Also -- but for Staples and for Office Depot, we have their data on what they're selling to each of these Fortune 100

companies. So we used Staples and Office Depot data to measure their sales to the Fortune 100; and then we used the customers' responses to measure sales for everybody else, all the other suppliers.

Now you might think, wait a moment that's kind of mixing two sources, is that okay? And it is. Because what we've done for all the other suppliers is overestimate their sales because we don't have as accurate detailed information.

So when it was ambiguous, what -- let's say, W.B. Mason sold -- let's take W.B. Mason. We show them selling to some of these large customers. The customer might say, "I bought a lot of stuff from W.B. Mason, it -- and they lumped together ink and toner and other stuff. So we would just take that number and say we'll include it. So we've actually included W.B. Mason's ink and toner sales in here, which is more than they've sold of the products we're measuring for Staples and Office Depot, because we're not including Staples' and Office Depot's ink and toner.

Another company, Veritiv, shows up here as a paper manu- -- as a paper vendor, a large one. They have a bunch of sales to one very large customer -- I won't name them -- that involve a lot of other shipping supplies and things, other sort of packaging and shipping, that they -- that this customer, this Fortune 100 customer, reported here's what we bought in this area from Veritiv. We didn't get a breakout from cut sheet

paper and all sorts of other packaging materials, so we took the whole number and just treated that as though it was paper. So we overstated their Veritiv sales to this customer.

That's happening a lot, and so all I can say is the -- in the end, the sales of the other firms are overstated so the shares of Staples and Office Depot are understated. Even so, we're getting shares of 47 and 32 percent here.

Q. And now, you assembled data for the Fortune 100.

Why didn't you measure market shares for all large customers?

A. Well, it wouldn't be practical to go to 1,000 or so customers and do this, so we picked the Fortune 100 as a, you know, well-defined set of companies, as our sample, our proxy for the overall set of customers. You could not do this for 1,000 customers and have a hearing in this decade.

Q. Okay. And why did you pick the Fortune 100 as the companies to use as a proxy?

A. Well, it's a set of companies that I didn't pick. If I pick companies, then how am I going to pick them, which was I going to pick? So it's a preset sample, if you will, so that's -- and it's kind of a lot. Actually, 100 was a lot to work with, so we did that. So it's a pre-given set of companies, is the main point.

Q. Okay. And is using a proxy group a common way to measure market shares in merger cases?

A. Often. It depends on, you know, what the data availability is here. The big issue is: Is it representative? You know, that's going to be the big issue: Is it biased in some way or another? So I think, you know, it's highly informative, and we -- we need to consider whether it somehow overstates or understates the company's share because it's not the whole set of customers.

Q. Okay. And why do you think that the Fortune 100 are a good proxy for all large customers?

A. Okay.

THE WITNESS: So first I would emphasize, Your Honor, that while these are the -- first of all, what is a Fortune 100? It's measurement of companies by their revenues. Okay. These are the largest companies in America by their revenues, but they're not the largest companies in terms of their purchases of consumable office supplies. Okay. So they're not actually the largest customers in our market. They tend to be larger than average, but they're not the very largest.

So we -- you know, if we think in terms of -- remember, large customers in our market are the ones who buy at least 500,000.

THE COURT: Right.

THE WITNESS: So we've -- in fact, not every single Fortune 100 company buys more than 500,000. A couple of them fall below that threshold. I could have taken them out. I

decided to just include them all. It wouldn't matter very much because their sales aren't -- their purchases aren't very much.

But we've got a good range of sizes, and we're going to see that up ahead -- maybe -- well, anyhow, we'll show you that, I think. So that's -- that's useful, I think, in terms of there's some distribution.

The other thing we did was a standard method, which is we said, well, let's -- let's split the sample into half -- we had 81 to work with, so we split it basically top 40, bottom 40 -- and see what the shares look like for Staples and Office Depot. Now, I mean, the ones who buy the most office supplies and then the second half. And to see -- I thought that Staples' and Office Depot's market share would drop off in the second half because they're a bit smaller. You know, I still have in mind this continuum from very large enterprise, you know, down to small business. In fact, it didn't drop off at all.

I think I'm probably out of order here, in terms of the slides, Your Honor, so maybe we'll come back to that, but -- so that's a good check that we're not getting some, you know, distorted figure here, that this is a good proxy. So we've done a number of things that give me confidence.

BY MS. CERILLI:

Q. Okay. And I notice looking at the shares here that there are a number of smaller distributors that don't appear at all. Why is that?

A. Well, back to slide 20, Your Honor, I actually had W.B. Mason displayed here. They come in at 0.2 percent, you know, which is small, right? The other larger companies are showing up are all paper manufacturers or paper vendors.

So the reason the other -- some of the smaller companies you've heard about, HiTouch or Guernsey, are not here, they're just so small they're lumped together in the all other suppliers category. Otherwise we'd have too many slivers in this pie. But they were counted, and a number of them did appear, but very small quantities.

Q. Okay. And I believe you referenced that you were using 2014 data here.

Why did you not use a more recent time period?

A. So, again, this is practical. The CIDs went out, I think, in the summer of last year, middle, maybe into the fall. The process certainly continued in the fall. So this collection effort is going on for a period of months, and so it's natural to ask companies to give us your most recent years' worth of data, which was 2014, so that's what we have.

Q. Okay. And are you concerned that the data is out of date?

A. Well, no. It's reliable data for 2014. The question is: Are things very different for 2016 or '17? So I thought about that. Okay. And we do have a way to project. So you ask yourself: What's significantly changing in this space from one

year to the next? And the only big thing that's happening or even potentially big thing, is Amazon Business that we've heard about. Okay.

And now you've heard, Your Honor, from, you know, W.B. Mason who's the next largest here and others. It's not like they're expanding. There's no big thing happening, other than Amazon that we've heard about. So I'm not concerned that the data's out of date, but I want to do a projection if I can to account for this -- the one element that is potentially a big changer, and that's Amazon Business.

BY MS. CERILLI:

Q. Okay. And did you do adjustments for Amazon Business?

A. So yes, that's our --

Q. And I think --

A. That's our next slide.

Q. Okay.

A. Okay.

MS. CERILLI: Now, this slide will have to be confidential because it involves Amazon Business confidential information.

BY MS. CERILLI:

Q. But certainly if the -- you can describe it in general terms, and the Court will be able to see.

A. Right, okay.

THE WITNESS: So -- and, Your Honor, given what I've seen in the trial transcript, I think this is, you know, pretty

important and responsive to some of your questions, so I certainly attempted to do that.

MS. SULLIVAN: Your Honor, I'm just going to object because this analysis and slide are not in his report at all. This expert witness's analysis was undisclosed to us in this case.

THE COURT: This particular slide?

MS. SULLIVAN: And this whole analysis about Amazon and the future is not in his report.

MS. CERILLI: Absolutely not. I mean, he's a professor -- Mr. Orszag argued in his report that Professor Shapiro did not account for future competitive significance of Amazon Business. Professor Shapiro responded in his reply that nothing about Amazon Business' projections unsettled his results. It was an opinion directly expressed in Professor Shapiro's reply report. This is a visual representation of that opinion. It's not new.

THE COURT: Well, it wasn't disclosed in the expert's report, though, so it is -- it is new. I mean, I query whether it'd be appropriate for rebuttal, I guess, to rebut any evidence that the defendants' expert produces is query.

MS. SULLIVAN: Even rebuttal, Your Honor, should have been disclosed.

THE COURT: Well, I'm not so sure rebuttal has to be disclosed. I'm not sure.

MS. SULLIVAN: It's no secret that Amazon was going to be

a huge part of this case, where Amazon was going to be in two to three years; so he's got one line in his report, and now they want to enter his whole analysis. He was deposed, and this did not come up in his deposition. And, Your Honor, I would object to it.

THE COURT: Ms. Reinhart.

MS. REINHART: Yes, Your Honor. He did address the criticism by Mr. Orszag in his rebuttal report. He addressed it. If it didn't come up in his deposition, it's because they didn't ask about it.

THE COURT: All right. So it is in the rebuttal report; is that correct?

MS. SULLIVAN: No, no.

THE COURT: It's not?

MS. SULLIVAN: There's a line in his rebuttal report that says that Amazon's not going to be here in two or three years, but there's no analysis. This whole analysis was not disclosed. He had a reply report. They could have put the analysis in if they wanted to talk about it at trial. They did not do it, and now it's -- so here's a new analysis that --

THE COURT: Is this disclosed anywhere, this slide, in the analysis of Amazon?

MS. REINHART: It's just a depiction, Your Honor. It's a depiction that did not include --

THE COURT: Is the analysis, though -- is the analysis set

forth anywhere?

MS. SULLIVAN: No, it's not.

THE COURT: It either is or it's not. I mean, if it's not, then, I think this is new. And I'm going to sustain the objection.

MS. CERILLI: I would say it's not a new analysis, though, is what we're saying.

THE COURT: But it was not disclosed at all, is it? Is it disclosed? And let me make it easy: Where is it disclosed?

MS. CERILLI: In his rebuttal report he describes how the Amazon Business projections do not unsettle --

THE COURT: Show me the chapter and verse there. I mean, it's either there or it's not there.

MS. SULLIVAN: Your Honor, I have the final report. There's one line about it, one sentence, page 26.

MS. CERILLI: Well, I don't know if some of this is confidential. It's page 26 of his reply report.

THE COURT: Is the analysis of Amazon disclosed? It either is or it's not, Counsel.

MS. CERILLI: This representation of the shares are not in there.

MS. SULLIVAN: It's at the top of the page, Your Honor. One sentence, there's no analysis, no discussion.

MS. REINHART: Could you direct the judge to the appropriate paragraphs to look at?

MS. SULLIVAN: Yes.

MS. CERILLI: Yeah. It starts at the top of the page.

THE COURT: What page, Counsel?

MS. CERILLI: Page 26, basically the first three paragraphs.

THE COURT: Is that where you're reading from?

MS. CERILLI: Yes, the first three paragraphs.

MS. SULLIVAN: Yes, Your Honor, the discussion for purposes of Amazon in the future, there's one line on top: "I concluded it was unlikely that Amazon Business would replace Office Depot as a strong competitor to Staples in the relevant market in the foreseeable future, by which I mean the next two to three years."

The analysis they're about to discuss is not in his report at all.

THE COURT: Right.

MS. SULLIVAN: It is not attached.

THE COURT: There's a difference between citing a conclusion and an analysis leading up to the conclusion. The conclusion's there, but the question is whether or not the analysis was set forth anywhere.

MS. CERILLI: Yeah. And I guess we would just say we did not think of this as new analysis, it's just a --

THE COURT: Well, it's new if it's not set forth anywhere. I mean, you have to give their experts a chance to take a look at

what was analyzed. I'm going to sustain the objection.

MS. SULLIVAN: Thank you, Your Honor.

THE COURT: Let's move on.

(Brief pause in proceedings.)

MS. SULLIVAN: And, Your Honor, I'm going to move to strike. There are apparently a bunch of slides in this deck.

THE COURT: Yeah. I mean, look, it's nonjury. I'm not going to give -- I'm not going to give any consideration to them. So you're referring to slide 21?

MS. SULLIVAN: Yeah. There's a couple, Your Honor. We can put it up right here.

THE COURT: All right. Just give me the number. I know 21 is among them. All right.

MS. REINHART: Just generally, Your Honor, this witness is testifying and is giving opinions about -- you know, about Amazon, and what they are and where they're going.

THE COURT: Right, but the point that counsel's raising, though, is that the analysis that supports the conclusion was not set forth in the report -- and it doesn't appear that it was -- so, therefore, I query whether it's fair to allow examination in open court now on an analysis that's not previously been shared with defendants; and I don't think it is.

MS. REINHART: Your Honor, I -- as Your Honor said, this is a bench trial.

THE COURT: Right.

MS. REINHART: We want to have as full a record as possible. There are other opportunities we could have to do this, give them an opportunity to respond to it, and then he could --

THE COURT: Well, why should he respond to something that was not previously disclosed in discovery?

MS. REINHART: Well, and one of the issues we have here, Your Honor, is there was recently produced new data from Amazon. And I think perhaps some of the slides that counsel's referencing later in his report relate to that new data. Your Honor understands that just came in after you requested it. There are plenty of opportunities for the parties to --

THE COURT: Yeah, but there would have been a motion filed to supplement the expert's report, a fair opportunity to depose the expert, a lot of other things. Counsel's just claiming -- you know, she's claiming fundamental unfairness, and I'm inclined to agree with her.

I think that -- I mean, if the government is going to rely upon this analysis that supports the conclusion, the conclusion is in the rebuttal report, but the analysis leading up to it is not; and I don't think that's fair.

So I'll sustain the objection.

MS. CERILLI: Okay.

THE COURT: It would have been very helpful, very interesting.

MS. CERILLI: Your Honor, we would request then to be able to disclose it today. We're happy to provide the backup data and reserve the right to call Professor Shapiro as a rebuttal.

THE COURT: How would you feel if someone sprung that on you at trial? You know, seriously. I think it's fundamentally -- you know, as I've said time and time again, there's wealth of talent in the well of the court, and I think it's just fundamentally unfair, and we're in trial now. You know, there was extensive discovery. There was discovery disputes. I know it firsthand. And the parties fought very fairly but vigorously about, you know, trying to obtain all the discoverable information they can.

This is a big issue here, the analysis leading up to conclusions that address the impact of projected market shares for Amazon. It's a huge issue.

MS. SULLIVAN: And what makes it doubly-unfair, Your Honor, is that the FTC purposely didn't seek this data themselves as part of their investigation. We had to make motions, and Your Honor was good enough as part of the fairness to let us see this data, and now data they could have had for a year they want to all of a sudden do a magical analysis in the middle of trial without disclosure.

It's unfair, Your Honor.

THE COURT: And I've sustained the objection. Your objection is noted, and I've sustained it.

MS. REINHART: And, Your Honor, we take exception to that characterization. We collected data from Amazon during the investigation. And we don't need to get into a dispute right now about what we asked for and what we didn't ask for. I'm only saying --

THE COURT: No, I'm not assigning any sinister motive to anyone. I just think that it's just fundamentally unfair to allow testimony about an analysis that has not been previously shared with defendants.

MS. REINHART: Your Honor, we, of course, are happy to give the other side whatever time they need. It is not unusual for experts in these situations to supplement their responses, to bring things to their --

THE COURT: I agree.

MS. REINHART: -- to their testimony even if they are in the courtroom.

THE COURT: When did you learn about this?

MS. REINHART: When did we learn about the...

THE COURT: Yeah, the slide and the analysis, right. Before trial?

MS. REINHART: Before trial? I'm not quite sure how to answer Your Honor's question based on the --

THE COURT: Well, truthfully would help.

FROM THE FLOOR: (Laughter.)

MS. REINHART: Your Honor, of course. Your Honor, of

course --

THE COURT: Yeah, I just want --

MS. REINHART: -- we're answering truthfully.

THE COURT: No, seriously though. If you learned about this before trial, you could have filed a motion to supplement, then I would have given them time to take a deposition. Well, I probably would have granted that. I probably would have granted it had I known about it. And then I probably would have told defendants, I would have said, "Look, fair is fair. If you want to take his deposition at the government's expense, bring the expert here, and we'll do it that way."

I probably would have -- because, you know -- I mean, the trial lawyer in me would have allowed -- would have suggested to me to do that, but -- but no motion was made.

MS. REINHART: In response to your question, Your Honor, Mr. Wilson from Amazon gave testimony in this trial. Professor Shapiro has been accumulating knowledge based on testimony; including that testimony, has been continuing to do analyses. There's no effort to keep anything from the other side. Perhaps we could have done it a day sooner or something like that but --

THE COURT: Well, let me ask you this, let me ask you this: When did the government learn about the analytical underpinnings that support this conclusion?

MS. CERILLI: Okay.

THE COURT: All right. I have to rely on the expert? I

mean, I can.

MS. CERILLI: No, no.

THE COURT: Is that your answer, to ask the witness?

MS. CERILLI: It was informed by Mr. Wilson's testimony about Amazon's projected sales.

THE COURT: What's your answer? I'm just -- I don't want to put you on the spot. I'm asking the attorney. I mean -- they're looking at you for the answer, so I'll ask you.

When did you give the government your analysis that supports that conclusion?

THE WITNESS: So all I was going to say, and I realize this is a delicate situation --

THE COURT: Yeah, I'm not trying to put you on the spot.

THE WITNESS: No, and I raised my hand. So -- there's two sources of --

THE COURT: But the government should answer this. It's a question directed to the government. I don't want to put you on the --

THE WITNESS: Okay, I'm sorry. I apologize then.

THE COURT: No, no, I just -- I'm just shielding you. I don't -- I think I should get an answer from the government, from the attorneys.

MS. SULLIVAN: And, Your Honor, at least the slides --

THE COURT: No one is suggesting you've done anything wrong. But, you know, I'm just asking the government: When did

you learn of it? I'm just trying to figure out what could have been done.

MS. SULLIVAN: Your Honor, looking at their dec, the projection cites to Mr. Wilson's deposition, which was many months ago.

MS. REINHART: It's to an exhibit from the deposition, Your Honor, which he then, again, described here in his testimony.

THE COURT: So is that actually an exhibit that was used during the deposition?

MS. SULLIVAN: Yes, Your Honor.

MS. REINHART: It's an exhibit that was used in the deposition as well as in his testimony here.

THE COURT: So he was deposed about this area then.

MS. SULLIVAN: No, Your Honor. They're taking a deposition exhibit and doing a whole new analysis based on it. So the point is that they had --

THE COURT: Oh. Well, let me ask you this: So he was not deposed -- the expert was not deposed about this exhibit during his deposition?

MS. SULLIVAN: No, no -- yeah, Your Honor. Just so it's clear, the data -- this analysis is taken -- they took a deposition of Mr. Wilson many months ago, that's the vice president of Amazon who testified here, and what it looks like Dr. Shapiro has done is taken an exhibit from that deposition

and --

THE COURT: Oh, I see.

MS. SULLIVAN: -- and did a whole new analysis.

THE COURT: I'm sorry, I see. I thought you were referring to your deposition of this expert; you're referring to the deposition of Mr. Wilson.

MS. SULLIVAN: And so it's clear, that the government had the basis for this analysis many months ago. There are -- and, Your Honor, there are rules for a reason, and basic fairness is one of them, and unfair surprise in the middle of a hearing is significantly prejudicial. They had the -- if they wanted to do this analysis, they had the deposition many months ago.

MS. CERILLI: And, again, as you can see, this slide is actually citing Professor Shapiro's reply report; and, again, it was our perspective that --

THE COURT: That's the conclusion, though. I mean, that -- the analysis is not in the reply report. I didn't see it there. I didn't see the analysis.

All right. I've sustained the objection.

BY MS. CERILLI:

Q. Okay. So, Dr. Shapiro, putting aside the specific data or any specific calculations, as you articulated in your reply report, you were aware that Amazon Business had certain projections concerning their sale of consumable office supplies, correct?

A. Yes.

Q. And as expressed in your reply report, do those future projections of Amazon Business unsettle your conclusions that Staples and Office Depot have a substantial share --

MS. SULLIVAN: Objection, Your Honor, it's the same issue.

THE COURT: Well, the conclusion is there, but it's not supported by any underpinnings. So I'll take it and give it whatever weight, if any, it's entitled to.

THE WITNESS: Um, that was based on -- my conclusion was based on the data I had available at the time of the reply report, which was from Mr. -- which we've been talking about here, the projections that were in the exhibit to Mr. Wilson's deposition, which I should say was not available to me in time to include in my initial report.

BY MS. CERILLI:

Q. Okay. So going back to the initial market share chart --

THE COURT: What slide, Counsel?

MS. CERILLI: Slide 20.

THE COURT: All right.

BY MS. CERILLI:

Q. -- I noticed that the -- some of the next largest suppliers here are focused on paper. Did you break out market shares for paper as distinct from other types of consumable office supplies?

A. Yes, I did.

Q. Okay. And what did you find?

THE WITNESS: So this would now be slide 23, Your Honor. Isn't that right? I think so.

So as we would have expected -- so first off, we did the same thing with the Fortune 100 companies; we just had to try to pry apart the paper and the other, what's called core office supplies, which is an imperfect exercise again.

We know as a matter of arithmetic that when we break it out, one side's going to end up with higher shares for the merging companies; the other side's share -- piece is going to be lower.

THE COURT: Right.

THE WITNESS: We're pretty sure going in, the core office supplies is going to be higher, and the paper is lower because we see these paper manufacturers. And that's what this chart shows you.

I would emphasize the bottom row, that the core would get a share of about 87 percent combined between the two companies. It is lower in paper, 71; and then the 79 over there on the left, that's the number we had before, when we -- before we broke them out.

So actually the total amount of money for the two companies, it's a little bit more than half its core and a little bit less than half its paper; I think 46 percent is paper. So that's all adding up.

So this is one of the reasons, by the way, originally -- so I did this in my prior -- my rebuttal report, or prior report. I had looked at this originally and not done the break out; Mr. Orszag criticized that, and we did some extra work. There's some additional, you know, like I said, allocations or attributes that have to be made.

And this is the result, so we've done that now.

BY MS. CERILLI:

Q. Okay. And so is your takeaway from this is that even if you had not included paper in your cluster and you separately defined a paper market, you still would have found substantial shares for the parties in paper?

A. Well, I think -- so I think this is actually instructive regarding how cluster markets work. So if you look at the 79 percent for the core and the paper together, you say, "Well, I'm not sure they're exactly the same. Let's try to break them out." It's hard to do, you break them out, you start with 79, you get one number that's higher, the other number that's lower.

It is worth checking that the 71 percent -- well, okay, that's still pretty high. If that number were 20 percent, then I go like, wait a moment. Something else is going on in paper. Maybe there's not a problem in paper. And then the clustering would be dubious.

THE WITNESS: We could have put ink and toner as another column here, Your Honor, and, again, it would take a lot more

work to measure. But if you put ink and toner in, we have every reason to believe that we would end up with a considerably lower share; and that's why we haven't done it. Okay. But the same sort of arithmetic would apply. We stuck here.

So I think the main message here is the paper shares are still very high. I guess if you look at 46 and 25, for the two companies, and that is what it is in terms of concentration --

THE COURT: If you put ink and toner in, you would come up with lower share such as, what, I mean, what percentage?

THE WITNESS: Well, we don't know. You see, the trouble -- and the trouble is a lot of these -- again, we're talking about Fortune 100 customer responses. So I mentioned W.B. Mason, they didn't break out -- many large customers would say, "Here's what we bought from W.B. Mason in the office supplies category generally."

THE COURT: And everyone interprets it differently; do they? Is that --

THE WITNESS: There's some of that, yes. But then the FTC went back and said, "Well, what do you include in this?" And some companies had more detail, other companies didn't. But a lot of those times after that back and forth, the company would say, "Look, this is what our records show. We buy from W.B. Mason" --

THE COURT: You figured it out, right?

THE WITNESS: Yeah, "We don't know how to break it out."

THE COURT: More often than not, though, would it be fair to say that most companies include ink and toner as an office -- under the category of office supplies/office products?

THE WITNESS: I'd have to double-check the underlying records. I wouldn't be surprised. But I'm not, as a factual matter, sure, if we went through those, you know, 81 responses we worked with.

There's a lot of, you know, variety here; everybody has their own accounting system and so forth. But -- and, again, the dis- --

THE COURT: But you wouldn't be surprised if that were the case.

THE WITNESS: Sorry, I didn't answer clearly.

I wouldn't be surprised if a number of the large Fortune 100 companies had a category --

THE COURT: Or the majority.

THE WITNESS: Or the majority. No, I wouldn't be surprised at all.

THE COURT: So you think ink and toner is office supplies/office products?

THE WITNESS: Yes, and the -- and that's why in many -- if we kept it in the market shares, that goes back to my example with W.B. Mason. So we would say, "All right, you're not breaking it out" --

THE COURT: Yeah.

THE WITNESS: -- "we'll just include the whole number," even though they've told us it includes some ink and toner.

THE COURT: Right, right.

THE WITNESS: So my purposes, that inflates W.B. Mason's share here because we've -- because I'm trying to measure core and paper.

THE COURT: Right.

THE WITNESS: But I understand, I think, where you're coming from: Well, don't people think of it together in a group?

THE COURT: Exactly, right.

THE WITNESS: And I there's some -- look, I think that's pretty common. I can't give you numbers. I'm not -- I'm not quibbling about --

THE COURT: It is usual for a Fortune 100 not to include ink and toner under the category of office supplies/office products, and -- well, do you have an expert opinion about that?

THE WITNESS: Well, it -- I don't want to say right now. I could ask one of staff members, you know, Matt Johnson, who looked at this very carefully and knows all the details. I do not know, sitting here, how many. And, again they're all different so it's idiosyncratic. I just don't know as a factual matter, Your Honor.

BY MS. CERILLI:

Q. But does the fact that a particular customer buys products together mean that they belong in the same cluster?

A. No, no, not at all. I mean, if you go back to my example with the cardiac surgery and the knee surgery, same insurance companies contracting with the hospital for a range of things, that doesn't mean you lump it together.

THE COURT: Right.

BY MS. CERILLI:

Q. And, again, Professor Shapiro, I believe when we were looking at the original market share graph, it included some manufacturing of paper; is that correct?

A. Yes, that's right.

Q. So did your -- do your market shares include sales of manufacturers to the Fortune 100?

A. Yes, absolutely. If any Fortune 100 company is buying paper directly from the manufacturer, I would include that. We see some of that in the data. In fact, is it shown here? Yeah, Georgia-Pacific is showing up as one of the paper manufacturers. That actually -- all of that is a very large order by one very large company of paper that that company reported to us, one of the Fortune 100 companies, so it's included here. And this is part of the method of asking them: Tell us wherever you got your office supplies from, manufacturer, distributor, somebody going to the store to buy it; tell us wherever they came from.

And so the manufacturers are included. Georgia-Pacific shows up here and Domtar.

Q. And what about manufacturers of office supplies other

than paper?

A. Well, they're also included. It's minuscule in the overall scheme of things. That's just not something these companies want to be doing, ordering those smaller items directly from manufacturers; very, very tiny shares.

Q. Okay. And what conclusions did you draw from these market share figures?

A. I'm sorry, I spaced out. What did I conclude? Okay.

Q. Sort of what is your assessment of the market concentration in light of these shares?

A. So, look, that is highly-concentrated market, 47 plus 32 are very large shares in a merger context. I would call this market a duopoly with a fringe, just in terms of the way the literature would describe this. And the fringe is not a derogatory term. It just means a lot of smaller players, which there are a large number here. And, of course, the merger would then turn it into what we would call a dominant firm plus a fringe, rather than duopoly. So highly-concentrated with a, you know, dramatic increase in concentration that would result from the merger.

Q. Okay. And can you show us your formal assessment of the market concentration figures?

A. So that's slide 24.

THE WITNESS: I think Your Honor has already heard about the Herfindahl index, the HHI, the sum of the squared shares, so

I'm going to skip through that, I think. It's purely an arithmetic calculation, but a standard one. And you can see here the post of the -- the HHI in the upper half, the 3,274, that's the concentration today, as best we measure it using these data. And then after the merger, combining the two firms, it would go up again from 3,200-something to 6,200-some. So I've highlighted the increase, which is what I give a lot of weight to, the increase in the Herfindahl, because that's what's really changing. And that's 3,000. It happens to be a round number. That's a -- that's what the, you know, Herfindahl concentration arithmetic tells us here.

Q. Okay. And does this increase in market concentration have implications for the likelihood of anticompetitive conditions?

A. Well, yes. I mean, following the normal methods of what we do with the Herfindahl index, this is well into the zone. For example, under the merger guidelines, it's, you know, well above the zone where there would be -- whatever the guidelines' language is actually something to the effect -- the presumption of significant harm to competition, which is, you know, in the case law type of language.

Q. Okay. And you understand that the defendants claim that the HHI comparisons and Office Depot/OfficeMax would have also been above the threshold.

Does that weaken your confidence in -- of the

significance of the high concentration here?

A. No, not here. I mean, I don't view this as the end of the analysis anyhow. It's informative. So one thing, we need to go on to look at competitive facts.

The other thing is, in shorthand, if that merger was 3 to 2, this is 2 to 1, again with the fringe. So that's just a whole different matter. And there's reason to believe that the 3 to 2 -- if I can use that language again -- didn't have, as far as we can discern, anticompetitive effects, because after that merger Office Depot and Staples have been competing very vigorously since then.

So two -- two strong players looks like it was a -- very valuable for customers. The drop from 3 to 2, I can't find any big effect that occurred from that. So the Herfindahl is one piece of that, but we're going to look at the bidding analysis; and that's going to be, in a way, more informative to me about tracing through the actual effects.

Q. Okay. And we'll skip the next slide in light of the objection that the Court sustained, but consistent with your opinion --

THE COURT: Which one is that, 25?

MS. CERILLI: Yes.

THE COURT: All right.

BY MS. CERILLI:

Q. But consistent with the opinion you expressed in your

reply report, does your understanding of Amazon Business' projections unsettle your conclusion that this merger would result in a highly-concentrated market?

MS. SULLIVAN: Objection, Your Honor, again, undisclosed expert opinion.

THE COURT: I'll sustain that.

BY MS. CERILLI:

Q. So, Professor Shapiro, you mentioned that you sought to corroborate the conclusions in the Fortune 100 shares in other ways, and I believe one of the other ways you mentioned was the primary vendor relationship shares.

So can you explain what those are and elaborate on how you think it corroborates the F100 shares?

A. Yes. So we might as well look at slide 26 to do this. So this is the other main data set and data analysis I did for market shares, for measuring shares. So the main starting point here is, first off, the data. It's a completely different set of data. These are data coming from suppliers. Okay. The other was customers, Fortune 100. These are the suppliers. And I think it's mostly redacted, but you can see the long list -- well, the list of suppliers here, there's about 35 of them I think, that provided information.

THE COURT: All right.

THE WITNESS: They were contacted and provided information. And then what did we do with each of those

suppliers? Again, this is the same process: The FTC seeking information, back and forth, my staff involved, period of months, detailed analysis. It's all similar in that sense, but it's a different set of sources of data.

So the -- we tried to determine -- first off, let me define a primary vendor relationship. Okay. We asked -- tried to find out -- asked these companies: "Can you identify -- can you identify customers to whom you sell at least $500,000 of consumable office supplies during a given year?" And, again, they would have mostly be talking about 2014, the previous year. So that's what we're trying to measure.

The idea is to measure how are these -- how's everybody -- all these large -- all these distributors, how are they doing -- how successful are they in establishing a primary vendor relationship and selling office supplies in that relationship. And that's what we're trying to do here, and -- actually, if we could jump to the next slide.

We'll go back and forth between 27 and 26. 27 shows a little more detail that I think is instructive in terms of what we get from these data. So, for example, the first two are Office Depot and Staples, and you can see their sales. That's not redacted, right? So between the two of them, each have around 900 million of sales to these -- in -- to customers in this category. And you can see they each have 500-some customers that they sell at least $500,000 worth of consumable office

supplies. So that we're getting, of course, right from their own data, Staples and Office Depot.

Everybody else, the data is from these other suppliers, and their names have been blocked out for the open court. And so a number of things here are relevant, and they're also reflected in the previous bar chart. So, actually, if you flip back to 26, you can see the sales have been turned into percentage terms. Office Depot and Staples have 45 and 43 percent of all these sales go to them. And then the next couple of companies are at the, you know, 3 or 2 or 3 percent range. And you can see, Your Honor, on slide 27 -- although it's redacted -- who they are, and then on down the line. Okay.

So we've got -- that's -- so this is the main additional measure of shares. I want to be very careful. I'm not -- I don't want to call these market shares, okay, and we can talk about exactly why. I want to call the Fortune 100 data market shares. I'm calling these primary vendor relationship shares because they're measuring something different but something very valuable for the merger analysis, in my view.

BY MS. CERILLI:

Q. Okay. And did you have data also on how important the primary vendor is to large customers?

A. Yes. So we do know that -- so from the Fortune 100 data, we know that on average -- if I remember this right -- 78 percent of the purchases are from their number one vendor.

Okay. See, those customers we can ask them -- we know, who did they buy from? We could say the top dog in terms of who they buy from was 78 percent on average. And so that's consistent with other evidence that this -- the primary vendor's playing a big role. It's not the only role. It's not 100 percent, but it's a big role. So that strengthens the informative value of these primary relationship shares that we're looking at here.

Q. Okay. And I understand that these shares are based on collection of data from several dozen different distributors of office supplies, and similar to the Fortune 100, we won't have time to go through all of the detailed analysis that you did to assemble and process that data.

Can you refer the Court to where that is in your report in the event that he -- the Court has specific detailed information -- more detailed information he's interested in?

A. Yes, I can. So Appendix G to my first report is called, "Competitor Data Compilation and Processing," and that goes through in, you know, a fair bit of detail how this was done, including how the firms were selected to be contacted.

And I believe in the end we got -- we, the FTC, got something like 35 usable responses out of 39 companies that were contacted, something like that.

Q. Okay. And similar to the F100 shares, when you were processing the data that you got from competitors, did the

method that you took, was it over conclusive or under inclusive with respect to counting shares to the competitors?

A. So, again, there's a lot of -- so, for example, Fastenal is an adjacent supplier. Okay. So we might get data that they sold -- actually, I'm not sure that they apply here. I should back off on that.

Let me make the general point: We often had trouble breaking out whether this company that supported the data, between their sales of consumable office supplies and other items, including our favorite ink and toner in some cases. So what we did is, if the -- we basically said, look, if they can't break it out between the products we're trying to count and other products, we'll just include -- we'll include the sales that are ambiguous as well. So we're overstating their sales.

And I think -- again, I'm not certain of this one, I'm sorry. But I think with Fastenal, you know, they sell a lot of other stuff; so we would, I think in some cases at least, include some of their sales. I'm sorry, I shouldn't have said that. I -- the general principle -- I apologize.

So we're overinclusive where we can't break things out. I'd have to go back and check for particular examples, but that's what's going on. Grainger, that's going to happen for. Grainger is in here. I won't say where, but they're on the list, listed on slide 26.

Q. Okay. And did you also consider breaking out paper as

well from other consumable office supplies in relation to when you were looking at the primary vendor relationships?

A. So yes, we did the same breakout, same type of breakout -- that is now going to be slide 28 here -- as best we could again, doing the split. And we get, as you can see there -- well, the share we were -- we started with for the two combined categories was 88 percent, 87.6 shown here, and that broke out into 94 and 81.

Again, the key question, I think, in doing this is: Is paper still -- share high enough that you would still, you know, have some strong concern about paper?

And here we say yes, because it's 42 plus 39.

Q. Okay. And we're seeing here that Staples and Office Depot have a very, very large share, a primary vendor share, using what I believe you're using here, the $500,000 spend cutoff.

Did you test the sensitivity of going down to a lower spend threshold to see if their share -- their shares drop at all?

A. Yes, we did. So I -- that's the next slide. That'll be slide 29. Fortunately, because of the information that was obtained by the FTC here, we were able to look at a broader set of customers with the $250,000 threshold.

THE WITNESS: And, actually, it's shown there on the slide, Your Honor. There were 1,249 primary vendor relationships

at the 500,000 cutoff. By lowering the cutoff to 250,000, we roughly doubled the number of data points here to 2,490.

And I -- again, I thought the shares, Staples' and Office Depot's shares, would fall a little bit or maybe a moderate amount. I wasn't sure. I think more or less by coincidence they're almost exactly the same. They didn't fall at all. Which, you know, looking at this alone, actually made me worry about somewhat low -- the next range of customers and harm to them. Now, they're not included in the relevant market; but it gives me, you know, that much more confidence that by using the 500,000 threshold we're not, you know, missing something important, some other supplier's a big deal who's serving smaller customers. That's not the case.

Q. Okay. And, generally, just to sort of sum up, what significance do you draw from seeing such large primary vendor shares for Staples and Office Depot?

A. Well, I think these shares -- and look, these are higher than the market shares. And the reason they're higher is because we're not including leakage and a bunch of other things. This is just establishing a primary vendor relationship often by winning an RFP, you know, or getting a renewal on a major contract. These are the basic, I'll say, relationships that large companies want to have with their vendors here, and so this is a measure of success. And it's going to dovetail with the bidding data we look at, too.

So this may -- this, I guess, further increases my concern about the deal at the stage where we're still measuring shares before we get to bidding analysis as such.

Q. Okay. And Professor, I'd like to turn now to address some of the criticisms that defendants have made against your market shares based on the Fortune 100 data.

So you testified that the shares are not based on the full Fortune 100 but instead that you only had usable data for 81 of the companies.

Do you believe that leads to bias in your results?

A. No, I don't. We talked about that before. I maybe got ahead of myself on that. And we had this Exhibit 30 that we had already covered.

So it doesn't -- it doesn't lead to bias, in my view. This particular exhibit was showing that the 19 companies that we couldn't -- that didn't have enough -- good enough data from, are, you know, generally very large, also using Staples and Office Depot as their primary vendors; they're certainly large customers of Staples and Office Depot.

But more generally, I have no reason to think this sample is biased, and I've done a number of things to check it. And it fits with all the other evidence, so I'm not concerned about that, no.

Q. Okay. And you did also touch on this next question before, but just to sum up: You know, the Fortune 100 are the

largest companies in America. Why are you comfortable using that as far as a larger or different set of companies?

A. Well, again, they are not the largest customers of consumable office supplies. We actually -- you know, I'm going to take this opportunity.

THE WITNESS: Judge, if you could look -- turn to in my reply report, Exhibit R1A. Do you mind?

THE COURT: I'm not sure I have that, but I'll make a note of that.

Go ahead.

THE WITNESS: Okay.

THE COURT: What's the exhibit number? R1A?

THE WITNESS: It's R1A in the reply report.

So this lists -- this lists the 81 companies we've been talking about, how much they buy in consumable office supplies, and it's listed out between by Staples and Office Depot.

So, you know, you want to see who are these companies, how much are they actually buying, and it lists their total purchases. So -- and I guess the individual items.

But you can see that when we get down to the lower part of this list, the last -- the lower half, say -- and we saw this on the other exhibit, too -- they're buying -- they're buying one or two million of consumable office supplies. And that's, you know, in the range of other -- of many other large customers, okay.

So there's nothing -- you know, I don't think this is some

distorted or -- sample that's not reliable.
BY MS. CERILLI:
Q. Okay. Now, did the Fortune 100 shares you calculated -- I believe you said it included sales not only on contract -- through a contract but also any purchases that the companies were making off-contract; is that correct?
A. Correct.
Q. Okay. And how specifically did you account for any off-contract spend?
A. So at the risk of repetition, these Fortune 100 responses from the customers, we asked them -- again, "we" being FTC with all of the intermediaries, between me and them -- "Please tell us all the ways in which you get your consumable office supplies." Okay. "Not just your primary vendor, other off-contract spend, how you get your paper," and we asked them about what you've heard about already, leakage, okay, which there are different definitions of the term, but we just said, "Include it all, everything."

And so the shared numbers do include that.

There were -- of course, a number of companies said, "Well, here's everything we track, but there's some stuff we can't track, we don't track." So, you know, we could -- I tend to call that discretionary leakage or unreported leakage.

THE WITNESS: And if you see in slide 31, let's say, that's about where we are now, Your Honor, there's an unreported

leakage adjustment, I don't -- that's not redacted.

So we took information about what -- a number of companies responded and said, "Well, look, there's a bunch of stuff we can't track. Leakage, we're not sure how big it is, but it's small," and we used that.

And slide 32 lists all the companies that gave specific answer about that in this back and forth with the FTC. So, you know, a number of them said de minimis when asked about, you know, everything -- "Everything you told us and specified, is there some stuff you're missing?" And they'd say, "De minimis," or "Less than 3 percent," whatever.

So we took all those numbers, we -- I made the decision to count de minimis as 1 percent, then I added it all up and then that's what leads to this 2.2 percent unreported leakage adjustment.

So it's my best shot at using the data I have to include leakage and, therefore, all sources by which companies get their office supplies in my market share table.

So that's the goal, and I think we've done a good job of it, is to be inclusive.

BY MS. CERILLI:

Q. Okay. And do you have other data analysis that you used that added confidence to your belief that these estimates were reliable?

A. Well -- so just in terms of these data, I'm still

thinking -- I had seen a lot of -- as part of this process again, over a period of months, the Staples and Office Depot were saying, "There's a lot of leakage, there's a great deal of leakage as a form of competition that we have to worry about." And so -- and some of the leakage would be people going and buying at retail or online.

So I said, "Well, okay, how can we study that?" And so we looked at the price difference between what the big customers pay on their contract and what they have to pay if they would go online. We know they're getting a good deal, but how good is it?

So we looked at that price gap. The idea is, look, if when you go online, if you have to pay 50 percent more, that's not going to be very attractive. If it's the same price, that's more interesting where I'd have to worry about leakage more.

So we measured this price gap between the contract price and the online or in-store prices.

Q. And did you also see evidence from the customers themselves that they prefer that customers -- prefer that their employees purchase on contract?

A. Well, yes, and I think you've heard testimony about that from some of the procurement officers. Look, it makes sense: They get a really good deal from Office Depot or Staples. It's -- well, we're going to show the numbers here. It's a lot better than if people just go buy on their own. And, of course,

they want to save money. They want to control that rogue spend or discretionary spend. They want to control it.

And, of course, it's an interesting situation: If Staples is the primary vendor, they and the customer, they both want to control that spend. So they're really teaming up to do this.

And we see that the in the RFPs, we see that in other materials that it's a combined effort. It makes perfect sense to me. So that also -- and customers talk about how they're, you know, controlling leakage and generally successful at it, I would say, although it's an ongoing issue.

MS. CERILLI: Okay. Before we turn to the next slide, Your Honor, I just wanted to address what the next slide is showing.

So Your Honor recalled that you requested that Amazon produce data from Amazon.com. That data was produced basically midnight last Friday. We assumed Your Honor would have questions on it and whether unsettled Professor Shapiro's analysis. And so in the next slide he seeks to just explain that it does not.

We are happy to proceed however you'd like. We would be happy to produce the backup of that today so that their expert can address it. We would even go so far as to make him available --

THE COURT: Just so the record is clear, what slide are

you referring to?

MS. CERILLI: We are referring to slide 34.

THE WITNESS: Thirty-four.

MS. CERILLI: And, obviously, there is no attempt at holding anything back, it's just that this data did not come in until midnight last Friday, and we were literally processing it within the last 48 hours.

MS. SULLIVAN: And, Your Honor, two things: One, again, we object to an undisclosed expert analysis and expert report; and two, it didn't come in until last night because we pressed for this, Your Honor, and Your Honor granted our request. The FTC could have gotten this data a year ago. They purposely put blinders on when it came to Amazon. So it's doubly unfair: One, undisclosed expert testimony; and two, data that they purposely didn't pursue in this case because they didn't want anybody to know what was going on in terms of sales from Amazon.

MS. CERILLI: Let me clarify. We had data from the Fortune 100. The Fortune 100 were asked to report all of their purchases, as Professor Shapiro has been explaining, including from Amazon -- and you can see on slide 34 this is not new data. This is directly from the Fortune 100 market shares. This is the reported data directly from the customers. So we're not putting blinders on; we are going directly to the customers and asking them to produce their Amazon.com spend.

THE COURT: So wait a minute. So you did not get this

information until when? Last Friday?

MS. CERILLI: Yes. And so from the customer side, we have --

THE COURT: Did you share it with defendants then?

MS. CERILLI: So what came in last Friday was Your Honor had asked Amazon.com to produce data.

MS. SULLIVAN: At our request.

MS. CERILLI: That was what was produced last Friday.

We did not pursue that data because we were pursuing it from the customers. And as you can see here, you can see Amazon.com's share in our F100 shares. We just thought that Your Honor might have the natural question of whether the data coming from the other side, from Amazon.com, was inconsistent with the data that we had from the customer side.

Professor Shapiro analyzed it and concluded it did not. That's all we're seeking to show here. But we're happy to do it to alleviate any concern; we will produce the backup to this. We -- their expert will have a chance to --

THE COURT: I'm sorry, I'm sorry. So you have the backup, you have the analysis --

MS. CERILLI: We have the backup to the Amazon.com data that came in last --

THE COURT: How long have you had that?

MS. CERILLI: Within the last 48 hours, because the data itself only came in at midnight last Friday.

MS. SULLIVAN: And here's the problem, Your Honor. They only pursued for their market share analysis data from Staples and Office Depot. They purposely didn't look for the Amazon.com data. It was only at our request, Your Honor, that it was produced. And they've had a year to put this case together, they purposely didn't receive this data. They never disclosed any opinions from this expert about this data. It's an unfair surprise at this point, Your Honor.

MS. REINHART: Your Honor, regarding Amazon data, there was data that we collected during the investigation. And that data was used as the basis for the numbers, the projections that were in the declaration. Mr. Wilson testified about that methodology in his deposition.

There never was another request from the other side forthcoming for any additional data.

He then testified again here in this courtroom and had a slightly different spin on things. That caused Your Honor to make the request for the data.

We're very comfortable with the data as it was, but it was given to us, and now this supplemental data has just put a slight twist on things. And that's what -- that's what --

THE COURT: That's what I want to know, though, that the defendants' experts have not had an opportunity to consider, right?

MS. REINHART: We just -- Judge --

THE COURT: I understand that, but you -- all right. And I accept what you're saying, but you received it two days ago. Why didn't you let me know two days ago? Maybe I could have done something then. I don't know.

MS. REINHART: So the data came in that Your Honor had requested them to produce. We received it, transmitted it to our expert, they began working with it. They just finished their work on it, the backup has just been created. We're happy to give it to the other side.

THE COURT: And what are they supposed to do with it now?

MS. REINHART: Well, their expert will be testifying sometime next week. They have plenty of time to work with it.

THE COURT: Okay. I'm not going to allow it. The objection's sustained.

BY MS. CERILLI:

Q. Professor, I think we --

THE COURT: Let me ask a question: Could not that data have been obtained by the government at any time during the last year?

MS. REINHART: It could have, Your Honor, and I think -- I think the only reason it wasn't is that we were comfortable with the data we received, the forecasting information that they gave us and the description that came with it. And, again, Mr. Wilson testified about all of that in his deposition. We were comfortable with that testimony. Apparently the other side was

too because they did not ask him for anything additional. It was only when he testified here last week that there was a request.

MS. SULLIVAN: Your Honor, they purposely sought data only from Amazon Business, not from Amazon.com.

THE COURT: All right. I sustained the objection.

MS. SULLIVAN: Thank you.

BY MS. CERILLI:

Q. Mr. Shapiro, I still would like to address the top half of this slide, which is data from --

THE COURT: Which one are you referring to now?

MS. CERILLI: To slide 34.

THE COURT: All right.

BY MS. CERILLI:

Q. We've heard -- defendants have been making arguments that off-contract spend goes to Amazon.com. Did you assess purchases by the Fortune 100 on Amazon.com in your shares?

A. Yes, I did. And that's what's shown on the top of the slide here.

Q. And can you explain what the top half of the slide is showing?

A. Certainly.

THE WITNESS: So let me go back again, Your Honor. The -- so all the Fortune 100 companies, we get their information --

MS. SULLIVAN: Your Honor, I'm sorry. This was -- if we

could take this down. This is what was just objected to and sustained, and now they put the slide back up.

MS. CERILLI: Well, the top half of the slide is the analysis from his report. That's all I'm asking him to address.

MS. SULLIVAN: You just published it.

THE WITNESS: Slide 34, slide 34.

THE COURT: That's not the one I have here, slide 34.

THE WITNESS: It's titled --

THE COURT: I see it. Right. All right.

THE WITNESS: Are we okay now?

THE COURT: Counsel, what's your objection?

MS. SULLIVAN: Your Honor, I have no problem with the top half.

THE COURT: Right.

MS. SULLIVAN: It's the bottom half that --

THE COURT: All right. That's what I thought.

All right. You can proceed, Counsel.

THE WITNESS: Okay. So the highlighted parts there in the circle, that's directly from probably -- let me actually look at it and make sure I'm right here -- R1D as indicated.

Okay. So that's from the exhibit in my reply report where I broke out the sales to the Fortune 100 companies. And one of the suppliers, not surprising, is Amazon. And you can see their purchases shown there. That is the Fortune 100 purchases from Amazon. Whatever they said, where they mention Amazon, which

would include Amazon.com, that's there.

There were a couple of other places where Amazon -- important places where Amazon, I'm sure, are appearing in those data but not by name. Those are the next two rows, which are, you know, between them, nearly 20 million, $19 million, which is -- and you can see in terms of the shares of the overall -- about 4-1/2 percent. And if you went back to the pie chart you'd see those. They're there, too. Okay.

So what are those? So that is two things: Other supplier not specified -- so a lot of times the Fortune 100 company says, "I don't know who this is bought from," so it's not specified. I assume some of that's Amazon.com. I don't know how much, but they're going to be in there to some degree.

And then we have this unreported leakage adjustment that I talked about before, so this is, again, where the corporate procurement officers are not -- they're not tracking it. And I assume some of that, maybe a lot of that is Amazon.com.

So there's about, if you look at it together, you know, about 20 million here. And this is what the slide is showing, in this -- which is about 4-1/2 percent of total purchases in this universe here from Fortune 100 companies that is either specified as Amazon or could well be Amazon without their name attached to it.

So that's my -- that's how I've measured and tracked Fortune 100 company purchases from Amazon.com using the data from

the customers. Okay. And -- okay. So that -- that's what's shown here.

BY MS. CERILLI:

Q. Okay. And Professor Shapiro, defendants have asserted that many other suppliers will enter the market and expand if Staples raises prices after the merger.

How do your market shares account for entering and expansion?

A. So the market shares -- the historical market shares do not account for entry and expansion that would arise as a result of the merger. Okay. That is going to come in a subsequent analysis. We're trying to measure, as best we can, what are people actually buying and selling right now.

This question about the future and what might happen, we're not including that, so that's coming.

Q. Okay. And you understand that some large customers negotiate pricing of paper directly with manufacturers; and you, I understand, attributed those sales to Staples.

Why is that appropriate?

A. In my market share calculations, when Staples sells and distributes paper to a customer, I attribute that, those sales, to Staples. In some cases, such as -- well, maybe -- I'm not sure what I'm supposed to say, so I'll just leave it at that.

The customer may talk directly with the paper manufacturer, such as Domar [sic] -- Domtar, excuse me, and get

a -- get a lower price. And I am -- but Staples is still actually making the sale at that price; and, more importantly, doing the distribution services, and booking the sale, and so forth.

I'm attributing those sales to Staples. That's something that the defendants have objected to or criticized, their expert. I stand by it. I think it's the right way to do it; and it's the normal way to do these things; because we're really looking at who's providing the distribution services, and it's not the paper manufacturer.

In cases where the paper manufacturer directly sells and delivers the paper to the customer, then I attribute the sales to the paper manufacturer.

THE COURT: Let's do this, Counsel, I'm going -- let's take a ten-minute recess and I think we'll keep it at ten minutes, and we'll start back at 20 to the hour.

MS. CERILLI: Sure.

THE COURT: You can step down.

(Thereupon, a break was had from 11:28 a.m. until 11:44 a.m.)

THE COURT: Let me ask a question about -- I want to separate out the Amazon supplemental material received pretrial and the Amazon supplemental material received after trial commenced.

Let me ask defense counsel: Does your expert intend to

factor that newly-produced information into his opinion?

MS. SULLIVAN: Your Honor, it's pretty self-evident so we're happy to put it in the proposed Findings of Fact. The number is absolutely clear, and so I don't think it needs expert opinion. I mean, it is what it is in terms of their forecast and the fact that they're grown by 50 percent every year. I mean, it's incredible.

MS. CERILLI: We disagree. I mean, I think -- the data that was produced was not specific to large customers; it was not specific to consumable office supplies. If Your Honor is interested in the implications of that data --

THE COURT: No, I was just concerned as to whether or not -- I was just interested in whether or not, since it was produced after the trial started and produced to both sides, whether or not the defendants plan to factor that information --

MS. REINHART: Your Honor, might I make --

THE COURT: -- into its position.

MS. REINHART: Might I make a suggestion based on Ms. Sullivan's colloquy just here, is that we step back and talk a little bit afterward and decide whether it's actually going to be used. It may be useful to the Court to see some --

THE COURT: That's my whole point. I don't want to spite myself, you know.

MS. REINHART: Exactly.

THE COURT: I mean, this is a nonjury, and I can let it in

and if there are objections --

MS. SULLIVAN: So --

MS. REINHART: If might suggest, Your Honor, if we can consult with the other side and decide if it's worth arguing about and perhaps making a proffer.

THE COURT: That's fine.

MS. SULLIVAN: That's fine, Your Honor.

THE COURT: You can do that over lunch.

MS. SULLIVAN: We will, Your Honor.

THE COURT: Because I was concerned -- yeah. And why am I doing this to myself, because it could be extremely helpful information to inform the Court's decision, so --

MS. SULLIVAN: And part of the issue, Your Honor, is if the government for their own reasons made a conscious decision not to get vendor data from Amazon.com or we wouldn't be here. It's been a year and they made a decision: We don't want to look at that.

THE COURT: Right. And now, I had anticipated one of two answers. One answer would be, "We have the information, and no, Judge, you know, our expert did not plan to opine on it," and then that informs the Court's decision to leave it out.

But if you're going to use it, then query whether or not the expert should be allowed --

MS. SULLIVAN: Well, we'll take a look at that, Your Honor, and decide.

THE COURT: All right.

MS. SULLIVAN: Well, we hadn't intended to use it with our expert. The numbers are what they are. And whether or not it's significant enough to put in our findings of fact, we can do that.

THE COURT: All right. Fair enough. All right.

BY MS. CERILLI:

Q. Okay. Professor Shapiro, I believe we left off and you were addressing how you accounted for sales by paper manufacturers.

I noticed also in your Fortune 100 shares that you did not generally have shares for diversity suppliers. Why is that?

A. So when a diversity supplier works with, let's say, Office Depot and serves a large customer, I've attributed those revenues to Staples in that -- excuse me, Office Depot in that case, rather than the diversity supplier as such. I think that's the right approach under the competition normal methods.

The point really is, if you think about what the shares are trying to do, you're trying to measure how significant are different firms as competitors. And, you know, Mr. Morrison from P.D. Morrison made it clear, he couldn't serve these customers alone, no way. He's a valuable partner with Office Depot, and it seems like they have a very good relationship. But if I were to attribute those sales that Office Depot makes to his company, it would make it look like he's a big competitor

independent of them. And that would not be -- that would be a misleading approach in terms of shares.

There is a slightly -- one could say, well, his -- the diversity suppliers do get a small piece -- you know, they get a small piece of the revenue, a few percentage. He mentioned single digits; you know, it's small.

THE COURT: Right.

THE WITNESS: One could attribute a little bit of it to him and his -- and the other Tier 1 suppliers. It wouldn't matter in the numbers. I'm not doing that. I'm really trying to measure who's providing the basic services, who's capable of doing it independently, and that's Staples and Office Depot. And not Mr. Morrison, as valuable as he is in the relationship with Office Depot.

THE COURT: I understand.

THE WITNESS: Okay.

BY MS. CERILLI:

Q. And, Professor Shapiro, I would just like to wrap up on market shares, and I do want to actually return to the topic of ink and toner and whether the -- the question of whether ink and toner is or is not out unsettled anything that we just talked about.

So I understand from our discussion yesterday you did not include ink and toner in your cluster, correct?

A. Correct.

Q. Did you calculate shares for ink and toner?

A. So no, and I think we had a little bit of back and forth with the Court about why it would be quite hard to do that with my data from the Fortune 100 companies, to break it out; that is, from the core and paper.

Q. Okay. And does the absence of ink and toner bias your market share results that you're showing here?

A. Well, no. These are the correct measures for the relevant market that we've defined, let's call it core and paper, because we've kept out ink and toner. So no, it doesn't bias these results; it's just we're looking at a narrower cluster.

Q. Okay. And I understand that you did not include ink and toner in the cluster because you felt that there was significant sales coming from MPS providers.

What if you're wrong about that and, in fact, MPS sale of ink and toner is fairly small?

A. Right. So if MPS sales are small, then the competitive conditions for ink and toner might look a lot like paper and core.

THE COURT: Do you have -- did you factor in reliable data about MPS sales from the Fortune 100 companies?

THE WITNESS: Right. So we have some data from them, and the trouble is the data -- let's take Xerox or Lexmark. They're going to -- a customer will say, "I bought all this stuff from

Xerox. It's a lot of printers. It's maintenance on the printers and ink and toner." So you get a big number. But the customer is not able to break out how much of that was ink and toner.

THE COURT: Right.

THE WITNESS: So I don't have reliable data on ink and toner apart from the bundle of services that they purchase it with, which is the --

THE COURT: But somebody can break it out, couldn't you?

THE WITNESS: Well -- okay. So the Fortune 100 is based on the customers.

THE COURT: Right, right.

THE WITNESS: So that's, you know, one of my two main data sets so I can't do it there.

THE COURT: Right.

THE WITNESS: Sellers -- so then you would have to -- then you would have to go to a whole collection of who are the MPS providers and the printers and you could --

THE COURT: Right. It's a big factor, though, because you're excluding ink and toner based on an understanding, a factor that the print services overly compensates for ink and toner --

THE WITNESS: -- okay --

THE COURT: -- or adequately compensates for ink and toner. I mean, that's why you're not including ink and toner. It's covered by the managed print services.

Does that sound right?

THE WITNESS: Yes, but let me back up.

THE COURT: It seems to me you would have to have reliable data about the service contracts separate and apart from computers and maintenance, right?

THE WITNESS: That's what we could not break out with the Fortune 100 companies; that's exactly right, for Fortune 100.

But let me back up a half step, Your Honor. I hope this is helpful, which is, look, I have evidence that --

THE COURT: Let me back up a second. Let me just explain to you.

THE WITNESS: I was backing up first.

FROM THE FLOOR: (Laughter.)

THE COURT: All right. Your objection is sustained.

FROM THE FLOOR: (Laughter.)

THE COURT: Go ahead. Go ahead.

THE WITNESS: No, really. All right. I had my backup lights on, I think.

So, I have evidence that the ink and toners often sold as package with the other stuff.

THE COURT: Right, right, right.

THE WITNESS: And I think there's quite a bit of that. There's evidence that's growing, and I think Staples and Office Depot would agree. Okay. So if that's right -- if I'm right, if that's correct, then it really is a different competitive

situation over there. And, you know, I shouldn't put that in the same cluster. It just doesn't look the same. Like I said, ink and toner is a consumable office supply by a reasonable -- you know, just common sense, common usage; but the competitive conditions are different. So if I'm right about that, it really shouldn't be in the cluster, any more than furniture should be.

THE COURT: Or jan/san.

THE WITNESS: Yeah, or jan/san, exactly. What if I'm wrong about it? Okay. What if I'm wrong and actually those MPS guys, you know, they don't sell very much of ink and toner.

THE COURT: Right.

THE WITNESS: Okay. It's kind of small. Then maybe it would be similar competitive conditions. Okay.

THE COURT: Right. And then it should be in the category of office products and supplies.

THE WITNESS: Okay. So then if we included it -- let's trace that through, though. Okay. So then I should have included it. Okay. If I should have included it -- because actually that's telling me Staples and Office Depot shares of ink and toner are probably going to be -- I have every reason to think they'll be just like similar to what they are in core and paper. Similar, that's why we put it in the same cluster. So they're going to be 80 percent.

So if I'm wrong about the MPS guys, and they're small, then I make made a mistake and this case should be broader. We

should be worried about harm in ink and toner. We'd have a bigger case. Ink and toner is, you know, a significant additional bunch of money. So the mistake would be -- whether you attribute it to the FTC or me -- bringing a case to you that was too narrow and didn't include some more products. I don't think we've made that mistake, I've made that mistake, because I think the MPS guys are big; but that's the nature of the possible error. It's not that we fabricated a problem in core and paper or fabri- --

THE COURT: No, I'm not saying that, right.

THE WITNESS: You know, it's not that we've given you inflated shares in core and paper that makes it look like there's a problem when there's not. It's we might have left out another problem area. Okay.

THE COURT: All right.

THE WITNESS: I don't think we're doing that. But even if we are, it doesn't change the fact we've got the problem in the area we're focusing on. That's where we've shined the spotlight. There's some stuff around the edges. I don't think we need to look at that.

So -- so that's why I'm highly confident that these shares -- and we can see bidding data in this core and paper area is, you know, a legitimate problem. And I think -- I don't think we've -- you know, I think -- I think ink and toner is different. It is different than MPS, but whatever we -- even if we're wrong

about that, it doesn't undermine what we're presenting to you.

THE COURT: All right. Thank you.

THE WITNESS: Okay.

MS. CERILLI: Thank you.

BY MS. CERILLI:

Q. So just to sum up, we covered a lot of data, Professor Shapiro.

Can you just sum up your opinions about the market shares and what the significance is to you?

A. Okay. So once we have the market defined -- obviously we're going to have arguments about that -- then we measure the shares. I think it's crystal clear that the shares of the two merging firms are very large. Okay. I've got 79 percent, 47 and 32. We've got some different measures. It's very large. It's a little bit lower for paper. So just that piece of the analysis, I think, is clearly raising a flag. And we can do the Herfindahl on the shares.

Now, I don't stop there, but we -- it means we need to keep going onto the next step, which is to try to trace through the effects.

Q. Okay. Great. So, Professor Shapiro, you mentioned that the next element is competitive effects.

What are the ways in which a merger can result in a loss of competition?

A. Well, the normal analysis -- and this is in the merger

guidelines -- talks about two general categories of competitive effects. They're called coordinated effects and unilateral effects. And to put it simply, coordinated effects is the fear that the merger will make it easier for the merged firm and its competitors to coordinate, collude, in an extreme sense, after the merger. You know, more concentrated market, more of a danger of collusion, section 1 type of stuff; or just tacit coordination that wouldn't be a section 1 violation.

The unilateral effects is quite different -- and that's what we're going to talk about here -- which is simply the merged firm by no one having to compete -- the two firms by no longer having to compete, the merged firm will have more market power on its own, no coordination with anybody else, just on its own, and that's why it's unilateral. On their own they're going to have more power and raise price, and that's what we're talking about in this case.

Q. Okay. So let's consider unilateral effects in more depth.

Can you provide a further explanation of what a unilateral effect is?

A. So really it's anything that's going to -- where the merged firm -- because it no longer faces the company it just acquired as a competitor -- will harm consumers -- where customers will be harmed as a result. Typically a higher price, but it could be, you know, not being pushed to innovate quickly.

Okay. In the tech industry that's often the concern, rather than prices.

Here we're going to focus on prices as an effect, as unilateral -- so I might use the word "unilateral price effects."

Q. Okay. How does the analysis of unilateral effects relate to the market shares we just reviewed?

A. Well, it's -- it smoothly is the next step, which is if you have high market shares, that's certainly an indication that you're likely to have these unilateral effects. That is to say, if the firms are competing directly against each other a lot, then that's when you're going to be worried. So the market shares are one -- actually one simple way of getting an estimate of how often are the firms really going head to head? How often do they compete against each other? The market shares are an indication of that.

But we want to go beyond that and look in more detail at how they actually do compete, and that's what's going to bring us to the bidding data.

Q. And you're starting along those lines, but how do economists determine whether an adverse unilateral effect may occur?

A. Well, the -- the first thing we're looking for is diversion between the two companies. Okay. That word comes up a lot. Or head-to-head competition and looking for the

frequency of that.

And then we're also going to be looking to see if these two companies stop competing -- as they will if they merge -- are there other companies that can just step right in and will be just about as good? So there's really two elements to this analysis, the economics: One is diversion, how often are they going head to head; and I'll call it gap, I'll just use the word "gap," which is how far behind is the next guy.

You know, in this case, you know, whether it's W.B. Mason, or HiTouch, or whoever -- maybe it'll be Amazon, you know, in another year or two -- how far behind in terms of their ability to compete effectively? And if that gap is large, that's when you're worried. If you have high diversion and a high gap, that's -- those are -- that's -- that's the most worrisome situation.

Q. Okay. And so what types of evidence do economists draw on to measure diversion and the gap issue that you've flagged?

A. Well, we love to look at the bidding data, as you already heard. But, you know, I'm looking at what the customers say about their choices -- you know, sort of stuff you've heard about from McDonald's and so forth -- and, of course, what the suppliers themselves say about who are we going up against, who are we bidding against, and how good are they.

You know, and we're going to get into competitive advantage and disadvantage, you know, so we can talk about this

gap. So any information that I find that speaks to the strength or the competitive advantage or disadvantage of the different firms, that's going to start to come in here in this phase of the analysis that wouldn't necessarily get picked up just with measuring market shares.

Q. Okay. And that was -- you mentioned bidding already a lot. So how does the fact that that is a market that involves bidding play into assessing unilateral effects?

A. Well, the way -- I think the way I like to think about it is, in the real world, what's going to -- we see Office Depot and Staples bidding directly against each other. You know, I think the only -- the AEP example is a very good one, not the only one -- and the benefits, we talked about that yesterday afternoon.

And so we want to see how the customers benefit from the bidding, and that's -- and then see who's going to be -- who else is going to be able to bid in terms of come in, who does bid, do they win very often. So that's the real, you know, here and now, if you will, of how competition takes place. You know, it's not an abstract concept. Okay. To Mr. O'Neill it's not an abstract concept. It's having these guys sweat it out a little bit about who's going to win his business and get something out of them as a result.

Q. Okay. And now, do all customers in the market have to view the merging parties as their two best options for there to

be unilateral anticompetitive effects?

A. No. I mean, of course not. The -- there are going to be some customers who don't pick Staples or Office Depot. This is -- anything short of a total merger and monopoly, you're going to always have that. There are other suppliers. The fact that there are some other suppliers does not -- does not mean a deal is okay. I mean, that's -- that makes -- doesn't make sense in terms of economics. So that's why we'll look -- we've looked at the shares of those suppliers, and we're going to look at their presence in the bidding data, and their competitive disadvantages.

So, no, the fact that there are other firms who serve large customers -- you know, W.B. Mason absolutely does sell, particularly in his region -- that does not somehow give a -- give a free pass, if you will, or -- to the deal or imply that there's no unilateral effects, not at all.

Q. Okay. And so let's turn to your analysis effects and your conclusions here.

What are your conclusions concerning the likely competitive effects of the merger on large customers?

THE WITNESS: So this is really some of what you've already heard, Your Honor, which I think the -- there will be a significant reduction in bidding competition for the large customers, as a result of the merger. And the other suppliers -- and right now we're talking about the suppliers who are in the

market now. We're going to get -- when we get to entry and expansion, we'll talk about who might come in more. Okay.

But the suppliers who we see now, they're just not enough strong ones who are comparable to replace Office Depot.

THE COURT: How strong would Mason have to be, hypothetically, to be a competitor?

THE WITNESS: Right. So I would think of that in three differently ways. One is, what's the market share? Okay. So it's pretty -- it's very small, actually, and --

THE COURT: They'd have to increase its market share by a significant percentage, right?

THE WITNESS: Well, we would -- I mean, we had 0.2 percent in there in the Fortune 100 numbers.

THE COURT: Right.

THE WITNESS: Even if we underestimated a little bit, give them five times that much, 1 percent, you know, this is the -- Office Depot, the smaller of the two firms in the market share, 32 percent. So it would be a huge chasm for them to clear to get to be anywhere near that big, just in terms of size.

THE COURT: What if they increased the market share to, say, 25 percent?

THE WITNESS: What would it take for them?

THE COURT: Yeah.

THE WITNESS: Okay. So let me come around to that. So first off, there's a big gap. It would take -- they'd have to

expand enormously, okay, in this market.

THE COURT: Right. And they can do that by acquisition of business, right?

THE WITNESS: Okay. Right. So, look, the reality is they couldn't -- just to -- even to start doing that, they'd have to build out nationally.

THE COURT: Right.

THE WITNESS: Okay. And I know you've thought about this.

THE COURT: They couldn't stay in Masonville?

THE WITNESS: Well, they could -- look, they could grow a fair bit in Masonville.

THE COURT: Right.

THE WITNESS: Okay. But not so much with these customers because most of these large customers, we have data on -- they're national -- they don't want to pick somebody for this contract -- main contract who can only serve part of their needs.

THE COURT: Right.

THE WITNESS: It's awkward. You know, it's not really what they want in a distributor. So -- and I think he -- I think Mr. Meehan said as much. Okay.

So -- so first of all, they've got a huge gap in terms what -- the way I -- I think -- quantitatively I think, okay, you've got a 47 and a 32 percent.

THE COURT: Right.

THE WITNESS: If you had somebody who was 10 percent, you

might say, well, maybe they could double and that would do a lot to fill the gap. We don't have anybody like that here, so it makes me more worried.

So we're looking at W.B. Mason because they're the next one down. The paper guys we could talk about, too, but they're not coming in on this core -- these core supplies, okay, core office supplies.

So -- and then I look at bidding data. Who else -- is there somebody else who's bidding a lot and, like, seems like they're putting competitive pressure on? Maybe they could turn up the dial. And we're not seeing -- you already saw the preview on the bidding data. We're not seeing anybody close. Okay. So we've got a big gap there.

So then you're into building out significant expansion, and that's going to be in the -- well, at least -- I'll do whatever you want, but in my way of thinking, that's entry and expansion. That's not -- unilateral effects we're looking at what's going on with the bidding? What are people's capabilities now? Okay. And they're -- look, you'll see -- I mean, they're definitely number three here in terms of the core office supplies, but they're way behind Staples and Office Depot. So -- so they would have to build out nationally. And we could talk about -- let's talk about that, if you don't mind, when we get to entry and expansion.

THE COURT: Sure.

BY MS. CERILLI:

Q. Okay. Professor Shapiro, you mentioned that your views on your -- your conclusions about competitive effects were informed by the bid data as well as other evidence in the record, including documentary evidence and testimonial evidence.

Obviously, I want to go through the bid data in detail, but before we do that, can you talk us through the other evidence you saw on the record that informed your conclusions about unilateral effects?

A. Okay. So we can ask -- we can see what customers think. We can see what the suppliers think. We have a slide here next, that'd be slide 36.

Q. And we'll have the -- these are documents from customer files, and so we've redacted the names of the customers.

A. So these are from -- so these are customers' statements about -- and you heard it directly from Mr. O'Neill, you know, in court here and others who -- some of the, not all of them, say, "These are the only two guys who really can serve my needs right now." Okay. That's a pretty strong statement.

THE WITNESS: Just so you understand, Your Honor, the -- so what happens -- during the whole process, the FTC gathers, as you well know -- I guess, gets declarations and other information. That comes to me -- I basically have a standing request: I want to know what the customers think; I want to know what the suppliers think. You know, some broad categories,

and I have my staff working with the FTC. So in my report, it's sprinkled with various cites to declarations; you know, all the material that one could have at that time from discovery.

So here are a few, okay. And I should say, you know, I don't -- this isn't the basis of my opinion because I'm sure there are other customers that say the opposite. I get that. But in this area I think generally there's a good number who feel this way and, you know, it fits with the other things we see. Either these are the only two companies that can serve their needs or -- or something close to that. This is the customer side.

Q. And did you also see documentary evidence from Staples and Office Depot's own files?

A. So yes, that's the next slide we have for you. Again, I -- you'll get this directly from other sources, I imagine, but it's consistent.

You know, they recognize each other as, you know, critical direct competitors. Look, they also identify other competitors. I'm not saying they don't. Okay. They're looking broadly. Some of what they're doing, of course, is trying to expand into other product areas, so they're seeing competitors there. That's not as directly relevant for our case here. Okay. But, you know, there's certainly some indications that they, you know, see this as now a duopoly that has gone from three to two.

Q. And, of course, Professor Shapiro, did you also perform an empirical analysis in order to assess unilateral effects?

A. I thought you'd never get to the bid data. Here we are.

Q. Okay. So let's turn to your bid data analysis then. Before we dive into the results, can you explain why bid data is relevant in the case?

A. Well, I think we did that in intro. It's really the best way to measure the head-to-head competition that's going on.

Again, with the firms, what we've actually seen historically, you know, as close as we can get to it today, and that's, you know, that's the reality of competition, for -- again, the focus here is on large customers, and these contracts they sign and the primary vendor relationships. That's the heart of what we're looking at here now, and that's what the bid data is going to speak to.

Q. Okay. And if we can move to slide 38, can you provide an overview of what type of analysis you attempted to -- you performed with respect to the bid data?

A. Okay.

THE WITNESS: So we're just laying out for you, Your Honor, types of analysis, and these are all pretty standard.

Frequencies, basically, who do we see bidding and appearing as a bidder; who, the different competitors; how often is W.B. Mason in the bid, you know, and so forth. And then who wins in the bidding. That's the first part.

And then the other thing we can look at is when customers switch from one supplier to another, what's going on? And in particular when Staples loses a customer, who are they losing it to and vice versa, and where do their big wins come from.

And so we can do both of those types of analysis here.

Q. Okay. And what data did you have available to you to conduct that analysis?

A. So we had -- the first two -- I'm on slide 39 now, we had the win-loss data from the companies that we already talked about in the intro section of the testimony. That's the first two.

Then we have data they provided, both of the companies, that is, on their top wins and losses in response to the FTC's request for information. So this would be top wins and losses based on sales of consumable office supplies.

And then we have data from the Fortune 100 companies. Part of the back and forth with those companies was, have you done a bidding, who bid, who won, what can you tell us about your RFPs.

So that's our fifth data set.

Q. Okay. And can you just explain a little bit further, what is the top wins-losses data set?

A. So these are basically when -- let's take losses. Okay. So Office Depot would say, when we've lost a customer in terms of how much revenue we lost, that customer was spending with us

and we lost in consumable office supplies, who is that customer? And then we can try to find out where they went. Okay. That's what we're measuring there and then likewise for wins.

Q. Okay. And then, obviously, we talked about the Fortune 100 market share data. So as -- but is what you're saying that the Fortune 100 also submitted their bid files as well?

A. Yes, about half of them had responsive information on that, not all of them.

Q. Okay. Let's turn to the results of your analysis.

I think -- why don't we start out with customer switching. Did you analyze how frequently large customers switched between office supply vendors?

A. So yes, I did. And that's going to be on slide 40.

So one of the features of this market is that the large customers very typically year to year stay with the same vendor, and you can see all these numbers are very high in this table. And Staples and Office Depot have documents that indicate the same thing, that their customers tend to be sticky.

THE COURT: That's because of the evergreen contracts, I assume?

THE WITNESS: I don't think about it as an evergreen contract so much. So I think there are two things going on: One is, if you sign a three-year contract, yeah, people could terminate it but why did you sign a three-year contract? You know, stick around for a few years. They don't want to do it

every year. So that would --

But more importantly from my analysis, even when a company has decided, all right, the contract's term is ending, should we renew it or should we go somewhere else, they want to renegotiate. That's when the competition is going to happen, okay, usually. I mean, people don't do it every month for fun, right?

So at this point -- and whether they do it through a formal RFP or just, you know, turn to their incumbent supplier and say, "Look, you want to just give us a good deal and we won't bother with that," we find that these very high retention rates, part -- I think there's an advantage for the incumbent, basically. They have a business relationship, of course, and their switching costs, okay. So -- and we've seen some evidence on that; that you have to integrate with the new vendor with your systems and so forth.

So it's a combination of customers don't want to have think about this every year, sign a multi-year contract, but also there's -- they have switching costs.

The main point here, we're going to come back to this later, actually, but the main point here simply is when we look at the data on switching. The numbers are going to be much smaller, on the small side, because there aren't that many switches. You can see, you know, what small percentage of customers are actually switching. And that's -- this is kind of

a prelude to the switching data to indicate to you why the numbers are on the small side.

BY MS. CERILLI:

Q. Okay.

Now, Professor Shapiro, you said you did analysis of bid frequencies. Can you explain what that is and why that's important?

A. So bid frequencies basically measure how often do different bidders show up in our data, and that's an indication of their competitive significance. In the end I'll probably go more with who wins, but showing up in bidding is worth tracking so we track both.

Q. Okay. And can you explain for the Court the results that you saw with respect to bid frequency and all of the different data sets that you had access to and analyzed?

A. Okay. So slide 41 shows the Fortune 100 data, so you can see it's RFP data appearances. So when the companies reported they had an RFP, then they indicated who bid. And you see -- oh, this is not redacted, okay. So there are 52 responses.

As it turned out, Staples was in there on every one as one of the bidders and Office Depot on almost all of them. And then we see a number of other -- the other suppliers who appeared at least twice.

It's noted at the bottom in the smaller print, 45 suppliers are mentioned. So if you look at all this data,

you're going to see a bunch of other companies, but they're hardly ever -- but they're bidding rarely. Okay.

The other thing I have to say is, some of these other companies -- I mean, Fastenal here is a good example. Sometimes we have a bid that includes consumable office supplies but it includes a lot of other stuff, and they would appear but they're not winning -- we're going to see that on the next chart or some other chart -- they're not going to win the consumable office supplies' bid but they're appearing.

So some of these appearances are actually people who are bidding on other things, so -- but, anyhow, Staples and Office Depot, you know, obviously dominate the appearances --

Q. Okay.

A. -- in bidding Fortune 100.

Q. Okay. And so slide 41 is the Fortune 100 bid data.

A. Yep.

Q. In how many of the Fortune 100 bid data files that you looked at were Staples and Office Depot actually the only bidders?

A. Right. So about 30 of those 50 or 60 percent. The only Fortune 100 company reported there were two bidders, Staples and Office Depot. That's who we -- so Mr. O'Neill's testimony is not unusual, that they were the two who could serve APD's needs in his case.

Q. And did you also examine the bid frequencies using the

Office Depot bid data?

A. Yes, so that's slide 42, which is I think the very first slide we showed you at the beginning of my testimony. So as the title said, "Staples dominates in appearances in the Office Depot data with 833 appearances," you know, far more than anybody else.

Q. And did you examine bid frequencies using the Staples data?

A. So that's the next slide, 43, which we also presented in the opening part, same pattern.

Q. Okay.

A. With Office Depot appearing in the Staples data.

Q. Okay. And what do you conclude from this bid frequency analysis seeing Staples and Office Depot so prominent and their smaller rivals --

A. Well --

Q. -- small?

A. -- and we're looking to the extent of head-to-head competition and gap with somebody else. We got a lot of head-to-head competition and a big gap. So that's what we're seeing.

Q. All right. I want to turn now to your analysis of who wins in bidding situations. And we can turn to 544. I believe this is based on the Fortune 100 RFP data.

Can you explain the results of that analysis?

A. Yes.

So I already mentioned that there were 52 Fortune 100 responses involving these bids, so now we can see who won. Okay. So, you know, almost all of them were Staples and Office Depot. Runco I happened -- they showed me a bid. I happen to know they got part of that contract in one case, and so they're showing up here.

And Veritiv is a paper, a paper merchant, and they're showing up here.

Q. And did you examine win frequencies using the Office Depot data?

A. Yes.

So now we're back to the slide 45 which we showed Your Honor at the beginning, and I do put more weight on the wins than the appearances because I think they're both informative. So we've got Staples dominating in who wins from the data we got from Office Depot.

Q. Okay. And did you examine win frequencies using the Staples data?

A. So that's slide 46; same idea. Office Depot dominating in what we see in the Staples data.

THE WITNESS: We also showed that to you, Your Honor, yesterday.

BY MS. CERILLI:

Q. Okay. And what do you conclude from this analysis of who

wins in these bidding situations?

A. So it's -- it's a pretty dominant picture for the two merging firms.

Q. Okay. And I want to turn now to your analysis of who wins when Staples and Office Depot loses a large customer. Why is looking at Staples and Office Depot's losses of large customers important?

A. I'm sorry, I was having a drink of water.

Could you say that again?

Q. I want to turn to your analysis of who actually picks up the customer in the event that a Staples or Office Depot loses a large customer.

A. Okay.

Q. So just to introduce that analysis, why is it important to look at who's winning in occasions when Staples and Office -- or Office Depot loses a large customer?

A. Well, in a sense it's a particular direct way of measuring the companies competing. You know, in business, people come in and say, "They stole my customer," you know. And so this is what we're talking about when the customers actually switch.

The earlier discussion was to alert you that this is a small number here because customers don't switch very much. But it's one of the most direct and tangible ways of seeing head-to-head competition between the two firms.

So we're on slide 47 now, I think.

Q. And does that switching, does that link back to the diversion term that you referred to earlier?

A. Yes. So that would be -- when the customer doesn't get a good enough deal from one company, from, let's say, Office Depot, who's an incumbent, where do they go? We're seeing here that in the seven cases where -- excuse me.

Let me start with the upper -- take somebody who's incumbent is Office Depot, that's the upper row. There are seven cases where Office Depot lost to a competitor and all seven of these those happen to be to Staples.

Oh, I should say, this is Fortune 100 data. Okay. We've -- previously we were talking about the company's data, this is -- so it's a relatively small sample, but you've got only 50 or so companies and they don't move all the time. So -- but, you know, it's meaningful to me. So every single one that Office Depot lost in this group was to Staples, seven out of seven.

The second row shows that almost all of the losses that Staples had were to Office Depot. It may look odd that we have a half there, but that was a customer. Staples only lost half of the business, so it's a half a loss to another supplier.

But, again, the -- overwhelmingly when they lose a large customer here in the Fortune 100, it's to Office Depot, the other --

Q. And just to be sure it's clear on the record, you are describing slide 47, which is showing in the Fortune 100 bid data who wins in instances when Staples and Office Depot loses; is that correct?

A. Yes, I hope that's there. Yes.

Q. Okay. And who wins in the bid lost by Office Depot in the Office Depot data?

A. So this is slide 48, and so you see here there's -- at the bottom actually seven- -- and equals 78, so there were 78 instances where Staples lost -- excuse me, back up -- where Office Depot lost, and about three-quarters of those were to Staples.

Notice, this number 78. It's on the small side compared to the other data sets because they don't lose that much. They tend to keep their customers. But when they do -- when Office Depot loses in their own data, about three-quarters of the time it's to Staples.

Q. Okay. And then moving to 549, what about the Staples data?

A. Exact same thing going in the other direction. When Staples loses, it's showing 80 percent of the time it's to Office Depot.

Q. Okay. And then you mentioned early that you had analysis specifically about the top 50 losses that Staples and Office Depot had in the last several years.

Can you describe how you used that data and what the results were?

A. Right. So now we're into slide 50. So this is just another -- again, one of the other data sets that I have because of response to FTC's request for information.

And top losses, so the left side here is Staples' top 50 losses that they report, 80 percent went to Office Depot. The other direction, almost as high. It's the same pattern. You know, we're seeing the same thing.

And let's just flip to 51. Those are the wins. When they get their big wins, most of the time it's from the other company. Okay.

So this is, you know, I don't know, very -- I guess I'll say nicely consistent from my point of view as an data analysis. I'm not seeing anomalies here. I'm not seeing anything coming up. Look, what I really am -- I'm looking for how they're competing, and is there somebody else -- I'm -- had the high market shares. So I'm like, well, it sure looks like there's a problem based on that, but maybe I'm missing something. How -- you know, what's going on?

I'm looking. Is there some other player who's -- maybe their market share was small, but they're in here bidding a lot, they're winning some of these, you know, and I'm not seeing that. I don't think -- I think that would be a phantom. Basically that firm does not exist. That's what I'm getting

from these data.

Q. Okay. So obviously we passed through a lot of detailed data. Just taking a step back, what are the implications of this data to your conclusion about unilateral effects?

A. Okay. So -- so what we're looking for here in, unilateral effects of bidding, is extensive bidding against each other, head-to-head competition, especially winning, stealing customers from each other, if I can use that term. And these are very high numbers. Okay. This -- I'm not shocked, given the market shares, but just -- it's all consistent. And so, it leaves me, you know, no doubt that this is a very big red flag.

I still want to check, are these other smaller firms, why are they not winning more? You know, it suggests to me they're at some significant disadvantage. So I want to check that that's true, that's part of the -- you know, what the disadvantage is. But at this point, you know, they're not bidding that much, they're not winning that much, these smaller players, and this is making me pretty concerned.

Q. Okay. And that's definitely something I want to talk about in depth.

Before we leave the data, in particular, do you have any concerns about the reliability of this data?

A. Well, generally the bid data -- so there's -- I've done a fair number of cases with bid data. I did just good a big one with GE, for General Electric buying Alstom, where they're

bidding to sell huge turbines to electric power plants.

And I like working with bid data a lot. There's always imperfections. So, for example, the suppliers -- when Office Depot and Staples provide the bid data, they write down who they know about who's bidding, but they may not know -- they may not be right. They may not be exactly accurate. There may be a bidder they didn't hear about. Okay. They may think somebody's bidding and they're not. Okay. So it's basically what any company knows. That's all they can do. I'm not worried about that here. I don't see any reason that creates a bias in what I've got.

The other thing is, they don't necessarily report every single bid. You know, this is coming -- in Office Depot's case, this is coming from their normal course of business. They keep track of these things. So you're always worried, you now, is there something wrong with this sample? I looked as best I can. I don't see a problem. And the numbers are so overwhelming and consistent with everything else, that I'm okay on that. Basically I think -- I think we're safe.

The Fortune 100 company data, that's the other -- the data source that doesn't come from the merging companies here. That, in some ways, I like that better because, look, the customer knows who's bidding. You know, they're going to be the most accurate on that. And they will even know -- you know, they could even say things like, "Only these two guys really do

what this third guy bid, but he wasn't, like, get out of here," right? So you get -- the customer's view is very important, and it's quite consistent here.

But this is a smaller data set, so I don't want to just look at that one. But altogether it's so consistent and so unambiguous that -- that I'm, you know, very comfortable recognizing the data's imperfect.

Q. Okay. And in your bid analysis, you would acknowledge that often the bids cover items other than consumable office supplies, correct?

A. Very often, and Mr. Orszag has made that point effectively, I think, in his report.

Q. Okay. And does that bias your results?

A. Well, no, but let clarify. Some of the bids we see -- I mentioned Fastenal in there -- are bids -- so what we counted here are bids that include consumable office supplies. Sometimes people are bidding, and they're going to end up -- the bidding for or winning another part of the business. I'm including all those, wherever they appear. I'm not ruling them out.

Okay. I happen to know Fastenal, a very tiny share of their business is in consumable office supplies. You know, very tiny. I'm not sure if I'm allowed to say it not, but tiny. Okay. So when I look at the bidding here, like, probably they're not bidding for this part of the business, but I'm going

to include them because I don't know for sure, and I just -- so by including those other suppliers, I have decreased the dominance of Staples and Office Depot because I'm showing other people bidding. So this complication that the RFPs often include other products does not bias my results, although it may -- may lead me to understate the importance of Staples and Office Depot when it comes to bidding for the products that we're actually worried about here.

Q. Okay. And so we've seen a bunch of data indicating that Staples and Office Depot are prominent winners and prominent in bidding for large customers.

What's the next step that you would look at to assess the unilateral effects?

A. Well, so then we want to look at the gap. As I said, you've got a lot of head-to-head competition. What about the gap versus the other players? And the larger that gap is the more worried we are.

Q. Okay. And how did you pursue that inquiry?

A. Well, I guess we get into starting to look at these other players -- you know, W.B. Mason stands out, actually -- and there's a number of elements to it. What -- what are their competitive -- do they have significant competitive disadvantages relative to Staples and Office Depot and what are they? I'm pretty sure they do have significant competitive disadvantages. That's why they're not getting the

market-to-market share. That's why they're not winning very much. But I'd like to understand what they are, and if we possibly can, to quantify that, which is hard.

So that's where I'm going next. Competitive advantages that Staples and Office Depot have, or same thing, competitive disadvantages the other guys have who are much smaller.

Q. Okay. And based on your assessment of the record, what competitive advantage do you find that Staples and Office Depot have over these other firms?

A. Well, two of them stand out, and we're going to come back to this when we get to entry expansion. The same question's going to be very relevant there, too.

But at this point I would just say, two, which is the smaller firms such as W.B. Mason or even much smaller ones like Guernsey, they have a much smaller -- they have a higher cost of goods sold. They basically are purchasing at a much smaller volume, and through wholesalers much more, rather than directly from manufacturers, and it's a disadvantage for them, and it's a significant one.

The other is geographic scope. And you heard this from Mr. Meehan very clearly. They're, you know, either really not able to bid or have a huge disadvantage with a company -- with a customer who wants nationwide, you know, scope, delivery from a single vendor. So those are the two: Cost of goods sold; and geographic scope, which I think are pretty compelling in -- at

this part of the analysis, as explaining what the smaller players are not -- not really in -- not in this game very effectively. Again, W.B. Mason appears, but much smaller.

Q. Okay. And as you mentioned, we are going to discuss some of this in the entry and expansion section, but I would like to just briefly have you explain the purchasing scale issue and the distribution disadvantage issue here.

So let's start with purchasing scale. What evidence have you seen in the record explaining that scale gap, and what is it and why does it exist?

A. So first off, if you start to think about -- let's use W.B. Mason as our example because they're the next guy. What is the purchasing scale that we're going to look at? We're thinking if they're going to a manufacturer to buy a bunch of pens or Post-its, whatever, so we want to look at how much are they buying in total? Okay. So now for this purpose we've got to look at their total purchases, not -- we can't just look at large customers anymore, because they're buying for all their customers. So it's total purchases. So that's the thing we want to measure. And we can measure that, basically see how big they are compared to Staples and Office Depot.

Now, we're not going to measure their purchases of all this stuff. We're going to measure how much they sell in all channels because, of course, they have to buy all that stuff in order to sell it. So we're now going to measure their total

sales in all channels, retail, small business, everything, and compare that to Staples and Office Depot, all channels. Okay.

So this is perfectly consistent with the relevant market we've got in the case, Your Honor, because we're still just concerned about harm to large customers. But for assessing this competitive disadvantage, it's driven by sales more broadly, so we're looking at a broader measure of sales, and that's what we're going to do on slide 52.

Q. Turn to slide 52, yeah.

A. Yeah.

Q. And unfortunately we have to keep the numbers confidential, but obviously you and the Court can see them.

A. Okay. So here the -- as it says, Exhibit R9, it's a reply report, so there's, you know, more detail there on what was done, but this is based on the suppliers' responses themselves.

One of the things it was pretty easy to get from all the suppliers is, how much do you sell in consumable office supplies? You know, what's your revenues? So you can see here -- and, you know, I think it's good to focus on W.B. Mason because they're actually -- you know, they're clearly number three in this sense, and -- I guess I shouldn't say the number, but there's a very large multiple between their size or scale, let's call it, and either of the merging parties, and that will predictively put them at a significant disadvantage when it

comes to cost to goods sold.

Now, that's one metric I can present to you, but we also have two other things that come up here: One is -- well, Mr. Meehan himself described this is a problem for him in going up against the big guys; and second, we have other evidence that a distributor who has to purchase more of their products from a wholesaler, rather than directly from the manufacturer, is at a cost disadvantage as well. And I think we're going to come back to that in entry, so I'll -- I won't say more now.

Q. Okay. And, basically, the reason for looking at this is because the more a distributor buys, they're able to obtain, in general, lower product costs from manufacturers?

A. Yes. I -- I hope that was implicit. Basically, the more you buy from a manufacturer or a wholesaler, as a distributor, the lower the cost you will get on average.

Q. And then you also mentioned a distribution network advantage that Staples and Office Depot have. And, again, we'll cover it in more depth in the next section, but can you briefly describe what you were referring to here?

A. So basically nobody else is national like they are, none of these other players, and -- but then, of course, the next question is, well, W.B. Mason, can't they deliver to customers outside of Masonville? You know, can't very handle that? And we've learned pretty clearly from them that they do that some -- not much, actually, a very tiny amount. But one reason they

don't do it much is it's a lot more costly.

So this is -- and, I mean, now I'm talking about cost of the distribution function, not the buying of the goods. So that's another significant disadvantage that the regional players would have in trying to go after a big customer who had a lot of locations outside their -- their home zone.

Q. Okay. And why is having higher product costs or higher distribution costs competitively significant?

A. Well, we're all talking -- we're talking about this gap. Okay. How strong are the other guys, can they fill the gap and replace the competition that's lost after the merger.

To the extent they have -- again, W.B. Mason or others have significant cost disadvantages; it's going to be much harder for them to do that and ultimately to apply competitive pressure to Staples, which is what, of course, the customers want.

Q. Okay. And have you been able to measure the gap or the magnitude of the unilateral -- the likely unilateral effects?

A. So I have one measurement that we've got here on slide 53, which we have estimates -- so we have to ask ourselves: How much does scale matter in terms of purchasing costs? Getting bigger, how much better deal do you get? And then, what's the scale gap?

So the first question, if you double in size, if we look at what Office Depot is saying from its merger with OfficeMax,

they roughly doubled in size, and then we can see here what they have, I guess, experienced, or claimed, or asserted regarding their cost of goods sold; how much that's gone down because of the doubling in size, and that's the number that's redacted.

You're on slide 53, I hope.

So a doubling -- if we take that number, a doubling leads to that amount of a cost reduction, a cost of goods sold.

And then we look at W.B. Mason and they would have to more than double; they'd have to double some number of times to get to be the size of Office Depot. So if we apply the same number, we get a cost of goods sold gap between W.B. Mason and Office Depot.

So that's one measurement of the gap.

Q. And, actually, I should say here, you can say that the total gap from your analysis is 6 percent. We will -- that is public. And we will unredact it from this slide, just the total number. Some of the other numbers that --

A. The 6 percent.

I want to say two things about that. So I stand by that analysis. I think it's sound.

But I want to say two things: First, the testimony of Mr. Meehan, actually, and Mr. Morrison as well, both point to a significantly large number in terms of the cost disadvantage they face. I don't have a way to quantify that; I couldn't do that, but that is what they have said. Okay. That's one.

The other thing is, this is simply -- we're measuring one aspect of the disadvantage that W.B. Mason faces, cost of goods sold. But the distribution network is probably, you know, at least as important in terms of national scope, which is actually being able to bid today for a national customer, you know, a geographically disbursed customer.

So this gap, as it exists today, is quite large, and that -- you know, the 6 percent number is surely too low but it's the piece I can quantify in this way. We can put in a significantly higher number based on their testimony, but I don't know how general that is. I mean, W.B. Mason, that's pretty important to me what he said.

This is the part I'm able to quantify with -- with as shown. As shown, yeah.

Q. And so is the 6 percent figure your estimate of a post-merger price increase?

A. So no, I think the number I used in my report was, as I said, it could be a guide. And I've explained now to the Court how it's -- I think of it as a lower bound because it's only measuring one aspect of the disadvantage, and because we have some other evidence that the actual cost gap -- COGS gap alone is bigger than this estimate.

Q. Okay. And have you considered how Staples could profitably raise prices following the merger?

A. So yes. I think I have, and this is an important part of

unilateral effects analysis, yes.

Q. Okay. And what different ways could Staples utilize to raise prices after the merger?

A. So here's how we do this: What I do is I look at how Staples actually prices to the large customers. Okay. And it's a bit complicated --

THE WITNESS: But you've seen it already, Your Honor. So I would flag -- first they have a list of core items that are high-volume items the customer wants a particularly good discount on; we talked about this a little bit. Then they've got noncore items that they get another discount on.

And then the part I actually want to highlight at this moment, they have sign-on bonuses and then they have rebates based on volume purchasing, so they have some other elements where they -- of pricing to try to win these large customers.

Now, the sign-on bonuses, on average, those are about 5 percent of the total that they're getting. So that's a significant number. And one of the most -- again, with my methodology, assuming the company threw out the profit maximized, if they want to raise price, they can, but of course they don't want to lose business when they do so. It's quite natural, I'm thinking, first, that they would trim or eliminate these sign-up bonuses, okay. And like I said, there's quite a bit of money there.

Now, why don't they do that now? Why do they offer these

sign-up bonuses? Well, you've heard about it: They do it in order not to lose the business to the other guy, okay.

THE COURT: Right.

THE WITNESS: And, of course, the customers are savvy, and they're trying to play that as best they can.

So this is the motive analysis and they say -- well, take a customer six months from now if the merger goes through, they're negotiating, that pressure to do the sign-up bonus is really not there. Who else is the customer going to turn to? Are they really going to credibly turn to, you know -- name that -- we don't have -- we've got a gap.

So it's -- the advantage for Staples after the merger of using this tactic is they're not raising the price -- this element alone -- they're not raising the price of any of their core items. Okay. They're not encouraging any leakage. You know, the only way a customer -- what's a customer going to do? Okay.

So they haven't -- so that's the first step, is they could eliminate or significantly reduce these sign-up bonuses. And because those are large, I see that as really the low-hanging fruit for them after the merger because the customers won't have the same leverage.

So that's a natural mechanism, and that fits with what we see in the bidding data. This is one of the key ways in which they compete.

And then we've got volume discounts and other elements, too. I'm not saying they won't change those prices. But the starting point, I would think, would be, I'm not giving you as much of sign-up bonus; why should I?

BY MS. CERILLI:

Q. Okay. And are there any other ways in which it would be advantageous for Staples to implement the price increase?

A. Well, they could increase any of the elements we talked about. The one other way that might not be obvious, I guess, or it's a little tricky, would be they could raise the price of, let's say the core items, and then also raise the volume discounts so that there wouldn't be any -- so they would discourage leakage and still get an average price that's higher. Okay. Basically they can say, "Look, you're going to have to pay this amount to do business with us, but if you grow your business a little bit more, we'll give you a good deal on the extra stuff; but not a good deal on the first million or two that you're buying because we know you don't really have a good choice for that." Okay. "The extra stuff, we'll" -- they're sort of competing for that leakage or extra sales.

So they have a price structure they can twist, I don't mean that in a bad way, they can adjust as well.

The key point -- this is --

THE WITNESS: I know this may seem a little intricate, maybe, Your Honor, but I'm not adding any bells and whistles to

the pricing structure they already have; I'm just looking at it. And it's not just a flat price. It's got these elements. And there's some ways that would be more or less profitable for them to take advantage of their enhanced market power after the merger, and I've identified a couple where I think it would be most advantageous.

BY MS. CERILLI:

Q. Okay. Now, you've talked about ways in which customers can be harmed. I do want to ask you about whether you think there are ways that customers can protect themselves.

First, you'd acknowledge that there are large customers that don't even use Staples or Office Depot today. So if they can get by without Staples and Office Depot today, why is there any reasons for concerns here?

A. Well, there are other competitors. The fact that this is not a total monopoly situation doesn't mean that there's no problem. This is why we look at market shares, and frequencies of bidding, and winning.

So I'm not saying every single customer in the relevant market will be harmed. Some of them are not using these companies and have their reasons for that. But we're talking about a predominant situation.

Q. Okay. And why can't large customers protect themselves by buying at retail?

A. Um, well, we talked before about how --

THE WITNESS: I think we showed you the data there, Your Honor, how the retail -- I'm not allowed to say that.

How the retail prices are far, far above the contract prices, so that's just not an attractive option. There's a little bit of it that takes place. We've measured that. But that's not what any of these big companies want to do to shift to more retail purchases. That would totally go against their attempts at cost control.

Q. Okay. But -- and then defendants say they're concerned about off-contract spend. So will that concern about off-contract spend constrain a likely price increase?

A. Well, we've measured that; it's small. And I don't see any reason to think it would grow dramatically, particularly with the type of pricing structure changes I described a moment ago.

Q. Okay. But you've heard defendants argue that leakage is significant. Have you seen any evidence in the record of that?

A. Well -- so we have quite a bit of evidence about the leakage or the absence of it. So first off, I've measured that in my market shares. We talked about that before. And we have customers testifying about how they want to control it and do control it; and, of course, their primary vendor helps them do that, and that will be true after the merger as well.

Q. I believe defendants' expert put forth some analysis of potential leakage. Does that unsettle your conclusions at all?

A. No. I responded to that in my reply report. It does not, and so it's not been part of my affirmative presentation here.

Q. Okay. Now, you said a moment ago that retail prices are generally higher than the prices that large customers pay.

But doesn't that show that large customers are getting a better deal anyway; so what's the concern here, even if they face a price increase?

A. Large customers are getting very good deals here. And the issue is whether that will, to some degree, go away. That's the concern. That's the customer harm from a loss of competition. That's what I'm focusing on.

I don't know what else to say. That's a real antitrust harm. I mean, I don't mean that as a legal thing. It's just as an economist, I'm concerned about that. Even though they're big customers and even though they'll still -- look, given the gaps, even if the price went up 10 or 20 percent, they'd still be getting better than retail; but it would be a big hit.

Q. Okay. But you've acknowledged that Staples and Office Depot often sell more than just consumable office supplies to large customers: Ink and toner, maybe some of the BOSS products.

So can a large customer simply threaten to take those BOSS products away from Staples and Office Depot in order to, you know, forestall a price increase on the consumable office

supplies after the merger?

A. Well, I -- large customers are going to use whatever bargaining tools they have at their disposal, which could include that tactic, to threaten, you know, I won't buy furniture or whatever. They're doing that today; they're going to do that after the merger, I assume. That's not changing. They're losing leverage, fundamental leverage, because of the deal. The fact that they have some leverage in some areas is not relevant because it's unchanging.

Q. Okay. Can you give us an example, kind of a practical example, to help understand that?

THE WITNESS: Well, I made this up, Your Honor. We'll see if it helps you or not.

I'm a big national parks buff and I go to the Grand Canyon sometimes. I was down in Utah recently.

So imagine there's two hotels at the Grand Canyon, two lodges to stay; there's only two, and I really want to go there. And maybe it's off season and they have some extra space; they've got some discounts.

They offer a package with air and ground transportation, too, and I'm buying the package. Okay. Some people buy the package, some people don't.

Now they merge. There's only one company that controls both lodges, the Grand Canyon.

They know there's a lot of people who really want to come

to the Grand Canyon. Let's imagine they -- you know, it would be tempting to raise the price. I'm a customer. I say, "Gee, I really don't like that." I say, "You know, if you raise the price, I'm not going to take your airfare and ground transportation package."

Is that going to protect me from the monopoly, it's not. Okay. I'm already getting -- whatever they're charging for that piece of it, the air and the ground, they've got to compete with other people already. That's true now; that's going to be true after they merge. Now they've got control over the lodges. I'm going in a weak position.

So it's just -- it's a bogus economic argument that that somehow gives customers leverage to offset what the merger's causing.

I don't doubt for a moment a lot of customers will use that leverage as part of a negotiation and they get volume discounts over broad -- all that's true, okay, and Staples and Office Depot have emphasized that. I'm not disputing that. I'm just saying the effect of the merger is, I only got one place I can go to the Grand Canyon, and no matter what's going on with air and ground transportation, that's market power.

BY MS. CERILLI:

Q. Okay. But we've also heard throughout the hearing that these are large, sophisticated companies. A lot of them have procurement staff. A lot of them bring in consultants

specifically to help them negotiate. Why won't there -- all of those tools and sophistication help them in preventing a price increase?

A. It comes back to the fundamental economics. These customers -- as I said, they're not particularly lovable. They're large. They're powerful. Done. But they are losing leverage, and they can be a sophisticated -- they are sophisticated. They can bring all the consultants they want. If they don't have good choices, they're going to pay more.

Q. Okay. And defendants have also argued that the -- that the consumable office supplies are a commodity product.

Does that mean there won't be harm here?

A. Well, I think that strikes me as a somewhat confusing statement to talk about the commodities product.

What the companies offer are sales and distribution service, and I've called them kind of high-end sophisticated distribution services. What they offer is not a commodity product, right? It's the IT system, it's the integration, it's the nationwide delivery, it's desktop, it's all these other things. That's what they offer.

I'm assuming that any distributor can get the same pens, can get the same Post-its, those items -- okay, now they may have to pay more, but -- no. What the issue in the case is what the companies' services are, and that is by no means commodity. Okay. That's -- that's just -- it's a red herring, really.

Q. Okay. And we've also heard that large customers often have contracts that run for several years.

Won't the length of the contract prevent these customers from harm?

A. Well, I think this came up a bit yesterday in terms of the contracts, so let me try to be very precise here.

The -- a customer who has a contract now -- first off, they may have -- typically, say, for the first year -- the core prices locked in. Okay. So that's some protection. Other prices typically wouldn't be locked in, and after the first year they can float anyhow. So I think there's some short-term protection for some customers, and it's going to depend customer by customer.

The -- and then, of course, renewals are coming in all the time. So, I guess, I'll just say as a general matter, I think it's a really bad idea to allow mergers to go through that are anticompetitive because some customers are protected for some period of time. Because you're basically -- I don't mean you, but one is then allowing a market structure to be put into place that is less competitive, and even if the harm's a bit delayed, that still should be worrisome. Okay.

Now, in a balancing, it's a fair question, some customers are protected. But, you know, it -- and it depends customer by customer. It's not that long, and it's not on all the items for sure; so I don't view that as, you know, something that

alleviates my concerns, the presence of the contracts.

MS. CERILLI: Okay. And, Your Honor, I want to just note, we have about five minutes more material on this section. I'll follow your lead, but I'm happy to finish this section and then maybe a time for a break for lunch?

THE COURT: Sure.

MS. CERILLI: Okay.

BY MS. CERILLI:

Q. Now, Professor Shapiro, have you evaluated whether there were any anticompetitive effects from the Office Depot/OfficeMax merger?

A. I did look that, yes. It's a natural thing to look at.

Q. Okay. And what did you find?

A. As best I can discern with the data I have available, I have not found any such effects.

Q. Okay. And in that case, why would you expect harm here?

A. Well, the -- first off, I'd say it -- it's irresistible to look at this recent merger and see what it's effects were, so I did that. The -- so I would think of it, there's a three -- think of that as, again, in the shorthand. That was the three to two, and now we've got a two to one, you know, in the shorthand language we sometimes use. So it's a whole different creature, you know, from a customer whose choices have been -- gone from three to two versus now down to one. So it's really -- we're in a different range here, substantially

different range in terms of market shares, bidding, competitive effects. So this is very different than what we saw before, and I think that's why we're here.

Q. Okay. And did you evaluate bid data in the Office Depot/OfficeMax merger?

A. Well, no, I was not involved in that merger. But I did have available the data that Office Depot presented to the FTC at the time -- so this would be 2013 -- where they did a bid analysis very similar to the sort of thing I presented here for this merger. And I -- I -- so I'm aware of that. We have -- we have access to that. We have slides on that.

Q. Okay. And so what did the data that Office Depot and OfficeMax presented to the commission in 2013 show?

A. So we'll have three slides in four minutes, I hope.

Basically, as I -- I was not present at these meetings. But as I read these charts, they're showing -- they were basically going in -- I'll characterize it, but I think it's right -- going in to say, "Don't worry about our merger because Staples is a big guy, we have to compete against them." Okay.

So the data here shows, they -- these data -- that were presented to the FTC, is showing in each of these bid charts, Staples is a bigger factor than here Office Depot. So this first chart on slide 55, OfficeMax's losses. So when they lost -- same sort of thing we did here, right? They're showing when OfficeMax lost, who did they lose to. And they're showing,

gee, most of the time they lost to Staples, not so much to Office Depot, would be their point here. The left-hand side is somewhat smaller accounts, over 150,000; the right-hand side is the larger accounts, over a million. And I'm pretty sure that's all office supplies, so -- or maybe all sales, so I would look at the right-hand side as for most relevant for our customer set here if you wanted to compare.

Okay. So they're finding when OfficeMax loses, a lot of it's to Staples. And then if we flip ahead -- I'm trying to get us to lunch here -- the first one was when OfficeMax loses. The second one is when Office Depot loses. Okay. And they've got a couple of different data sets and different sizes of customers. The reds are Staples again, appearing a lot, same point.

And then they have runner-up data on slide 57, which I generally haven't had here, but that's something we often look at, who won, who was the runner up, okay, who's applying the pressure. And they're showing Staples as the runner-up two-thirds of the time in the largest customer set here. That's slide 57.

So it's really very similar type of bidding analysis that I'm doing. And they were arguing that Staples was a huge factor, and that's why the Depot/Max merger should be allowed, and it was.

Q. And so, is this -- given the prominence of Staples in this data, is this data suggesting that Office Depot and

OfficeMax were not each other's closest competitors?

A. Well, as measured by these frequencies, Staples was a bigger, you know, more -- a bigger competitor, if you will, to either of them than they were to each other.

THE COURT: Were the products in the office supply category defined the same way as they are now by the FTC?

THE WITNESS: No, I'm pretty sure they -- no. They included ink and toner.

THE COURT: All right.

THE WITNESS: They certainly did in --

THE COURT: Is that significant, then?

THE WITNESS: Um, well, maybe -- I'm not sure what significant -- in term of interpreting the data?

THE COURT: Yeah. Well, we're making comparisons and judgments --

THE WITNESS: Right.

THE COURT: -- but it's apples and oranges, though, right?

THE WITNESS: No, I wouldn't --

THE COURT: The categories were not defined the same way.

THE WITNESS: Fair point, but --

THE COURT: I mean, it's getting back to the cardiac surgery or the knee surgery, isn't it?

THE WITNESS: Well, my knee's hurting when you say that. The -- it's a fair point. I don't think it's so different that we can't make the comparison. Okay. So they're including -- so

let's think it through. They've included ink and toner here.

THE COURT: Right.

THE WITNESS: So they may have some --

THE COURT: When you say "here," you mean 2013?

THE WITNESS: Well, yeah, in their category -- yeah, the slides we just looked at. Okay. So I don't know all the details about their data there, but the concern that you're raising, I think, would be -- right, they've got a bunch of bids. They include ink and toner, so some of these bids might be ink -- might be MPS bids.

THE COURT: Right.

THE WITNESS: Okay. I don't know how much that's true in their data; but if it's true, then if you took out ink and toner, Staples would look even bigger.

THE COURT: Right, right.

THE WITNESS: Okay. Which would reinforce the point they were making then and that I'm making now.

THE COURT: Right.

BY MS. CERILLI:

Q. Okay. And so --

THE COURT: Do you have an opinion as to why the government defined the product category differently in 2013 as opposed to now?

THE WITNESS: Um, I don't know why they did it. What -- I don't know -- have insight to what they did exactly then, but I

can tell you now that -- I said I started by including ink and toner.

THE COURT: Right.

THE WITNESS: I assume some of the people at FTC did, too, probably some of the same people who did this a few years ago. And, again, speaking for myself, as I learned about MPS, I carved it out for the reasons we've talked about. I -- so that -- fine. That's my guess.

THE COURT: Did the government say, "Exclude ink and toner from your calculations"?

THE WITNESS: No, no. They didn't tell me what to do, if that's what you mean. There's a dialogue, you know, working together, for sure. It was more, "We learned about ink and toner. My staff tells me, you know, these MPS are showing up, they're selling a lot of stuff. It looks different."

THE COURT: Right.

THE WITNESS: I'm like, "Well, gee, if it's really different, we should carve it out. Can we do that with the data? Is it practicable?"

And we found a way to do it. So -- and at the same time the FTC's saying the same thing, so we're -- you know, we're in a conversation together, and that's how it happened.

MS. CERILLI: And certainly, Your Honor, we'd be happy to address that question in our summation as well.

THE COURT: All right. Sure.

MS. CERILLI: Okay.

BY MS. CERILLI:

Q. So if we're looking at -- what we're looking at here in the Office Depot/OfficeMax merger, who was the next option available to customers, large customers?

A. Well, it was clearly Staples, as the obvious option, to go against the now-merged firm, Office Depot after they acquire OfficeMax. That's what they were projecting, and that's what happened.

Q. And I take it, you had no reason to believe that Staples is at any competitive disadvantage in the way that we're seeing the remaining firms here?

A. Right. So if you go back to what I was saying about bidding analysis, you look at the gap. So in the previous merger there was no gap. Okay. Once they merged they had this other guy just as big to go against, so the gap was tiny. And in the end that's what -- that's my view of what happened, is we went from three to two. Staples was plenty powerful enough to go head -- toe to toe, against Office Depot. They compete quite aggressively against each other, and prices didn't go up. That's what I think happened.

Q. Okay. And just to sum up for us -- we've covered a lot of evidence related to competitive effects -- taking that all into account, what is your opinion concerning the likely competitive effects of the merger on large customers?

A. So now we've got -- it's clear from the bidding data; it's all lining up. This just reinforces what we have from the market shares stage. You know, two critical competitors going up against each other all the time. The others -- compet- -- the other bidders or competitors are significantly weaker or smaller. So, you know, we get to this point, like, okay, I've got some serious concerns here. And then we're going to ask: Is entry going to save the day?

MS. CERILLI: It sounds like a good time for lunch.

THE WITNESS: Wait, we don't get to do it now? It's so exciting.

FROM THE FLOOR: (Laughter.)

THE COURT: Objection overruled.

FROM THE FLOOR: (Laughter.)

THE COURT: We'll break until 2:15. Enjoy your lunch.

THE WITNESS: You, too.

(Thereupon, a luncheon recess was had beginning at 1:05 p.m.)

C E R T I F I C A T E

I, Scott L. Wallace, RDR-CRR, certify that the foregoing is a correct transcript from the record of proceedings in the above-entitled matter.

/s/ Scott L. Wallace — 4/1/16

Scott L. Wallace, RDR, CRR
Official Court Reporter

Date

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