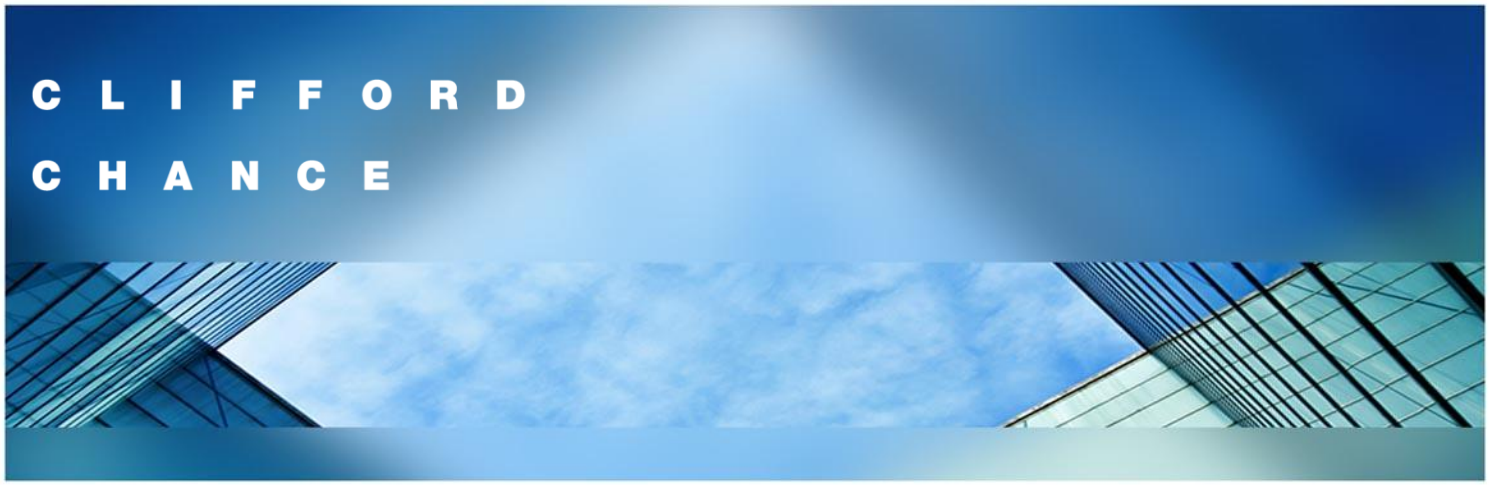

ONE-STOP SHOPS STOPPED: TWO JUDGES BLOCK KROGER-ALBERTSONS TRANSACTION

On December 10, 2024, a federal judge granted a motion by the Federal Trade Commission and nine state attorneys general[1] to preliminarily enjoin Kroger's proposed acquisition of Albertsons.[2] Later that day, a Washington state judge permanently enjoined the deal under the state's Consumer Protection Act.[3] The two judges ruled on similar grounds, holding that the merger would harm supermarket competition by eliminating head-to-head competition between the companies. The judges also found that neither the merging parties' proposed divestiture nor their proffered efficiencies would prevent the transaction from harming consumers. Together, these decisions provide several important considerations for parties considering a merger or an acquisition.

KEY TAKEAWAYS

First, both courts referred to both the 2010 Merger Guidelines and 2023 Merger Guidelines in evaluating market concentration. The current leadership at the federal antitrust agencies are likely to view this as a victory and further evidence that courts are adopting the 2023 Merger Guidelines. On the other hand, merging parties and critics of the 2023 Merger Guidelines can point to the courts' opinions as evidence that the 2010 Merger Guidelines still have some influence and have not been completely replaced.

Second, the federal court's opinion may have opened the door to the FTC or the US Department of Justice bringing a standalone challenge to a merger on a labor-based theory of harm. In such a future case, the government might refer to the court's statement that "[t]here is no apparent exemption or prohibition against considering the labor theory and plaintiffs present a compelling and logical case for applying traditional antitrust analysis to labor markets."

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[1] The nine attorneys general represented Arizona, California, Illinois, Maryland, Nevada, New Mexico, Oregon, Wyoming, and Washington, DC.
[2] See Opinion & Order in Fed. Trade Comm'n v. Kroger Co., No. 3:24-cv-00347 (D. Or.) (Dec. 10, 2024).
[3] See Findings of Fact and Conclusions of Law in State of Wash. v. Kroger Co., No. 24-2-00977-9 SEA (Wash. Sup. Ct.) (Dec. 10, 2024).

Third, both decisions amplify the importance for companies to ensure that their ordinary course documents and internal communications support their arguments and advocacy in favor of a transaction or other conduct. While the merging parties argued that they competed with additional supermarkets and non-supermarket stores to a significant extent, the plaintiffs were able to point to internal documents from each merging party that suggested that it viewed the other as its most or second-most significant competitor, including documents in which the merging parties "price checked" or benchmarked against one another and discussed how labor union issues affecting one company would benefit the other.

Further discussion of the two decisions is below.

PROCEDURAL HISTORY

On October 14, 2022, Kroger and Albertsons announced that Kroger had agreed to acquire Albertsons for $24.6 billion.[4] Kroger operates over twenty distinct "banners," or store brands, with approximately 2,700 stores located across thirty-five states and Washington, DC. Albertsons, through its approximately twenty "banners," has 2,269 stores across thirty-four states and Washington, DC.

As part of the proposed transaction, the companies attempted to address antitrust authorities' concerns through a divestiture package whereby C&S Wholesale Grocers, LLC would acquire 579 Kroger and Albertsons stores across approximately thirty states and Washington, DC. C&S is a privately held wholesaler that provides grocery products to retail grocery stores. The $2.9 billion divestiture package also included distribution centers, ownership and licensing rights for certain private label brands and store brands, and the right to use certain services, technology, and data during a transitional period.

On February 26, 2024, the FTC initiated an administrative proceeding to block the transaction and filed a complaint in the United States District Court for the District of Oregon to enjoin the merger pending the outcome of the administrative proceeding. The merging parties stipulated to a temporary restraining order where they would not consummate the merger until five days after the federal district court's ruling. Leading up to the FTC's action, the states of Colorado and Washington filed their own lawsuits in their respective state courts seeking to block the deal from going forward.[5]

Following the rulings on December 10, 2024, Albertsons announced on December 11 that it had exercised its right to terminate the deal and had filed suit against Kroger in the Delaware Court of Chancery. Albertsons contends that Kroger "willfully breached" the companies' merger agreement, "including by repeatedly refusing to divest assets necessary for antitrust approval, ignoring regulators' feedback, rejecting stronger divestiture buyers and failing to cooperate with

[4] See "Kroger and Albertsons Companies Announce Definitive Merger Agreement" (Oct. 14, 2022), available at https://www.albertsonscompanies.com/newsroom/press-releases/news-details/2022/Kroger-and-Albertsons-Companies-Announce-Definitive-Merger-Agreement/default.aspx.

[5] See "AG Ferguson files lawsuit to block Kroger-Albertsons merger" (Jan. 15, 2024), available at https://www.atg.wa.gov/news/news-releases/ag-ferguson-files-lawsuit-block-kroger-albertsons-merger; "Colorado Attorney General Phil Weiser files lawsuit to block proposed Kroger/Albertsons merger" (Feb. 14, 2024), available at https://coag.gov/2024/colorado-attorney-general-phil-weiser-files-lawsuit-to-block-proposed-kroger-albertsons-merger. As of December 11, trial had concluded in the Colorado case and a decision by the court was pending.

Albertsons" and thus failing to "exercise 'best efforts'" and "take 'any and all actions' to secure regulatory approval."[6]

GOVERNMENT-FRIENDLY STANDARD FOR MERGER CHALLENGES

District Judge Adrienne Nelson's opinion was a significant policy win for the FTC. The opinion upheld the standard for preliminary injunctions under Section 13(b) of the Federal Trade Commission Act,[7] relied (at least in part) on the 2023 Merger Guidelines' lower thresholds for finding a presumption of competitive harm, considered divestitures in the rebuttal stage as opposed to placing the burden on the plaintiffs in making their prima facie case, and opened the door for standalone labor market challenges under Section 7 of the Clayton Act.[8]

Section 13(b) authorizes a federal district court, upon a finding that the FTC has reason to believe that an entity is about to violate any provision of law enforced by the FTC and an injunction would be in the public's interest, to preliminarily enjoin a merger or acquisition pending the FTC's administrative adjudication process. To prevail, the FTC must show that, "weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest." The merging parties argued that the court should instead use a four-part test commonly used for preliminary injunctions in non-antitrust contexts, which imposes a higher burden on a plaintiff by requiring a showing of irreparable harm in the absence of a preliminary injunction. The court rejected this argument as inconsistent with both the plain text of Section 13(b) and the framework that courts have applied consistently in cases involving Section 13(b).

NARROWLY DEFINED MARKET FOR SUPERMARKETS

The plaintiffs argued that the primary relevant product market in which the effects on competition for groceries should be analyzed was the market for "traditional supermarkets and supercenters," which they referred to collectively as "supermarkets." Supermarkets, as described by the plaintiffs, have distinct characteristics, uses, customers, and other attributes that distinguish them from other retail businesses. The merging parties argued that this definition did not properly account for premium, natural, and organic stores (such as Whole Foods), club stores (such as Costco), and limited assortment stores (such as Aldi and Lidl), amongst others. The merging parties also argued that they and other traditional supermarkets primarily compete with Walmart rather than each other. The merging parties further argued that customers no longer engage in "one-stop shopping" and instead shop for the types of goods offered by Kroger and Albertsons across a broad variety of store formats.

The court adopted the plaintiffs' proffered product market, stating that supermarkets formed a relevant antitrust "submarket" within a larger market based on their broad product selection and customer service focus as well as industry

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6 "Albertsons Files Lawsuit Against Kroger for Breach of Merger Agreement" (Dec. 11, 2024), available at https://www.albertsonscompanies.com/newsroom/press-releases/news-details/2024/Albertsons-Files-Lawsuit-Against-Kroger-for-Breach-of-Merger-Agreement/default.aspx.

7 15 U.S.C. § 53(b).

8 15 U.S.C. § 18.

recognition. With regard to geographic markets, the court adopted the plaintiffs' proposed markets of small, local areas proximate to the merging parties' stores.

USE OF 2010 AND 2023 MERGER GUIDELINES

Judge Nelson's decision is among the first merger decisions to be issued following the release of the 2023 Merger Guidelines, promulgated jointly by the FTC and DOJ in December 2023 to replace the agencies' 2010 Horizontal Merger Guidelines. Among other changes, the 2023 Merger Guidelines lowered the thresholds for the level of increase in concentration pursuant to which the agencies deem a transaction to harm competition. Although the Merger Guidelines do not have the force of law, the DOJ and FTC have often relied on them for advocacy when challenging a merger, and courts have in turn looked to the guidelines for guidance.

In her opinion, Judge Nelson stated that "multiple courts have cited [the 2023 Merger Guidelines] as persuasive authority without weighing their relative merits vis-à-vis the 2010 Merger Guidelines," and "encouraged by the fact that other courts have found the presumptions to be useful, persuasive authority when considering market concentration, the Court s[aw] no reason to reject the 2023 Merger Guidelines in favor of a previous edition." Nonetheless, each side's experts presented, and the judge reviewed, the estimated changes in market concentration under the thresholds of both the 2010 Merger Guidelines and the 2023 Merger Guidelines. In fact, the judge implied that the choice of Merger Guidelines was not material to the decision, stating that based on the analysis of one of the merging parties' experts, "there are numerous presumptively unlawful markets under either the 2010 or 2023 thresholds, suggesting that the proposed merger is likely to substantially lessen competition under either set of guidelines."

AFFIRMATION OF HARM TO LABOR AS A VIABLE MERGER CHALLENGE THEORY

While Judge Nelson grounded the decision to issue a preliminary injunction entirely on the potential for harm to competition for supermarkets, Judge Nelson also addressed the additional theory of harm raised by the plaintiffs of the potential for harm to competition for the labor of union grocery workers. The court held that the plaintiffs had "not presented sufficient evidence to establish a prima facie case that the proposed merger will substantially lessen competition for union grocery labor." The court's opinion nonetheless discussed the labor-harm theory and provided some validation for its use in merger cases, stating that "[t]here is no apparent exemption or prohibition against considering the labor theory and plaintiffs present a compelling and logical case for applying traditional antitrust analysis to labor markets."

The court also found that the plaintiffs had established a "plausible, relevant market for antitrust purposes" for union grocery labor, that Kroger and Albertsons "engage in head-to-head competition when hiring union grocery workers and negotiating [collective bargaining agreements]," and that the merger would "increase the market concentration of union grocery workers" in multiple regions. Nonetheless, in this case, the court said that it lacked the necessary means to determine whether the merger would result in "undue market concentration" for

union grocery labor as well as “economic analysis of whether the merged firm will have an incentive to reduce wages and benefits.”

REJECTION OF MERGING PARTIES’ REBUTTAL ARGUMENTS

The merging parties offered three rebuttal arguments in response to the plaintiffs’ prima facie case: (1) other competitors would aggressively expand, constraining the merged firm’s market power; (2) efficiencies generated from the merger would mitigate the proposed merger’s anticompetitive effects; and (3) the proposed divestiture would mitigate the proposed merger’s anticompetitive effects.

The court found that any entry by new competitors would not be timely, likely, or sufficient to mitigate the anticompetitive effects of the merger, given the time and resources required to build or expand a supermarket (significant lead time for building and making operational, costs of construction, etc.), and the lack of evidence of aggressive expansion plans by other supermarkets. Although the court “remain[ed] skeptical about the efficiencies defense,” the court considered the merging parties’ efficiencies arguments but found that the purported efficiencies were not merger-specific, verifiable, or guaranteed.

Addressing the proposed divestiture package, the court cited previous merger cases to hold that any remedy must “replace the competitive intensity lost as a result of the merger,” rejecting the merging parties’ contention that the plaintiffs bore the burden in their prima facie case to show that the competition would be harmed even with the divestiture. The court then assessed the remaining overlaps, the divested assets, and C&S as a divestiture buyer, and found that the merging parties had failed to rebut the plaintiffs’ prima facie case given these issues.

First, the court found that even a “perfectly successful divestiture in which no sales are lost or stores closed as a result of the change” would not sufficiently resolve the competitive issues from the transaction, noting that the merging parties’ economist conceded that such a divestiture would still result in twenty-two presumptively unlawful markets under the 2010 Merger Guidelines or 231 presumptively unlawful markets under the 2023 Merger Guidelines. Second, the court was concerned about C&S’s ability to meaningfully compete without further assistance from Kroger and Albertsons; even with a complex transition plan, the court was not convinced that “rebannering” half the stores and introducing new private label items would be sufficient to compete against all of the familiar banners and products available at Kroger and Albertsons stores. Finally, the court was concerned about C&S’s track record as a purchaser of retail grocery stores, finding that its “past divestiture purchases have not been successful” and that its “current stores are performing below expectations.”

PARALLEL STATE OPINION GRANTING PERMANENT INJUNCTION

Judge Marshall Ferguson’s opinion granting the State of Washington’s request for an injunction paralleled Judge Nelson’s opinion in several ways. Like Judge Nelson, Judge Ferguson found that the State had established a relevant product market for supermarkets that excluded “other retail formats, including club stores, dollar stores, and specialty and natural grocers, and mass merchandisers.” Judge

Ferguson found that the merger would “produce 57 highly concentrated supermarket city area markets” in the state of Washington and would be “likely to cause anticompetitive effects in Washington, in the form of both higher prices or lower quality.” Judge Ferguson rejected the merging parties’ rebuttal arguments on similar grounds as Judge Nelson, describing C&S as “inexperienced and ill-equipped,” stating that the proposed divestiture package would put C&S at a “competitive disadvantage,” and finding that C&S would have both the ability and “strong incentives” to close or sell off the divested stores it would acquire.

The court granted the State’s requested relief of an injunction barring Kroger and Albertsons from consummating the merger. The court stated that “[t]he fact that enjoining the transaction will have effects beyond Washington also does not alter the propriety of an injunction.” The court noted that some appellate courts had criticized the use of so-called “nationwide injunctions” by lower courts, but disclaimed the application of that label given that “[t]he injunction restrains the conduct only of Defendants, who do significant business in Washington, and only as to this specific merger, which has anticompetitive effects in Washington.”

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