



Date and Time: Sunday, October 22, 2023 1:20:00 PM CST

Job Number: 208634710

## Documents (100)

### 1. [Merkle v. Aetna Health, Inc., 2005 U.S. Dist. LEXIS 47586](#)

**Client/Matter:** -None-

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### 2. [Riley v. R.I. Dep't of Envtl. Mgmt., 2005 R.I. Super. LEXIS 62](#)

**Client/Matter:** -None-

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### 3. [Genesee Vending, Inc. v. R.J. Reynolds Tobacco Co., 2005 U.S. Dist. LEXIS 17442](#)

**Client/Matter:** -None-

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### 4. [In re Monosodium Glutamate Antitrust Litig., 2005 U.S. Dist. LEXIS 8424](#)

**Client/Matter:** -None-

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### 5. [Bassett v. NCAA, 2005 U.S. Dist. LEXIS 17570](#)

**Client/Matter:** -None-

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**Search Type:** Natural Language

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6. [Brennan v. Concord EFS, Inc., 369 F. Supp. 2d 1127](#)

**Client/Matter:** -None-

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**Search Type:** Natural Language

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7. [Am. Needle, Inc. v. New Orleans La. Saints, 385 F. Supp. 2d 687](#)

**Client/Matter:** -None-

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8. [Able Sales Co. v. Compania de Azucar, 406 F.3d 56](#)

**Client/Matter:** -None-

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**Search Type:** Natural Language

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9. [In re Polyester Staple Antitrust Litig., 2005 U.S. Dist. LEXIS 47179](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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10. [JES Props., Inc. v. USA Equestrian, Inc., 2005 U.S. Dist. LEXIS 43122](#)

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<b>11. <u>S. Coast Cab Co. v. City of Anaheim, 2005 U.S. Dist. LEXIS 63364</u></b>	
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<b>12. <u>George Miller Brick Co., Inc. v. Stark Ceramics, Inc., 9 Misc. 3d 151</u></b>	
<b>Client/Matter:</b> -None-	
<b>Search Terms:</b> "antitrust law"	
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<b>13. <u>TXU Generation Co., L.P. v. PUC of Tex., 165 S.W.3d 821</u></b>	
<b>Client/Matter:</b> -None-	
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<b>14. <u>Xcaliber Int'l Ltd., LLC v. Edmondson, 2005 U.S. Dist. LEXIS 26705</u></b>	
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<b>15. <u>California ex rel. Lockyer v. Safeway, Inc., 371 F. Supp. 2d 1179</u></b>	
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16. [Dixie Gas & Food, Inc. v. Shell Oil Co., 2005 U.S. Dist. LEXIS 12010](#)

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17. [Confederated Tribes of Siletz Indians of Or. v. Weyerhaeuser Co., 411 F.3d 1030](#)

**Client/Matter:** -None-

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18. [Shaw v. United States, 371 F. Supp. 2d 265](#)

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19. [Investors Corp. v. Bayer AG, 2005 Vt. Super. LEXIS 92](#)

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20. [Nilavar v. Mercy Health System-Western Ohio, 2005 U.S. Dist. LEXIS 60941](#)

**Client/Matter:** -None-

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21. [Ramallo Bros. Printing, Inc. v. El Dia, Inc., 392 F. Supp. 2d 118](#)

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22. [Mothershed v. Justices of the Supreme Court, 410 F.3d 602](#)

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23. [Miller's Pond Co., LLC v. City of New London, 273 Conn. 786](#)

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24. [Bradburn Parent Teacher Store, Inc. v. 3M, 2005 U.S. Dist. LEXIS 11375](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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25. [Novell, Inc. v. Microsoft Corp. \(In re Microsoft Corp. Antitrust Litig.\), 2005 U.S. Dist. LEXIS 11520](#)

**Client/Matter:** -None-

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26. [J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc., 2005 U.S. Dist. LEXIS 11676](#)

**Client/Matter:** -None-

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**Search Type:** Natural Language

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27. [MacArthur v. San Juan County, 416 F. Supp. 2d 1098](#)

**Client/Matter:** -None-

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28. [Freeman v. Lasky, Haas & Cohler, 410 F.3d 1180](#)

**Client/Matter:** -None-

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29. [In re Enron Corp., 327 B.R. 526](#)

**Client/Matter:** -None-

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30. [Stand Energy Corp. v. Columbia Gas Transmission Corp., 373 F. Supp. 2d 631](#)

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31. [United States v. Gosselin World Wide Moving, N.V., 411 F.3d 502](#)

**Client/Matter:** -None-

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32. <a href="#"><u>Tex. Commer. Energy v. TXU Energy, Inc., 413 F.3d 503</u></a>	
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33. <a href="#"><u>Minn. Life Ins. Co. v. AXA Inv. Mgr, 2005 U.S. Dist. LEXIS 12320</u></a>	
<b>Client/Matter:</b> -None-	
<b>Search Terms:</b> "antitrust law"	
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Cases	Practice Areas & Topics: Antitrust & Trade Law; Timeline: Oct 26, 2004 to Dec 31, 2022
34. <a href="#"><u>Am. Express Travel Related Servs. Co. v. Visa U.S.A., 2005 U.S. Dist. LEXIS 42852</u></a>	
<b>Client/Matter:</b> -None-	
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Cases	Practice Areas & Topics: Antitrust & Trade Law; Timeline: Oct 26, 2004 to Dec 31, 2022
35. <a href="#"><u>Tippecanoe Assocs. II, LLC v. Kimco Lafayette 671, Inc., 829 N.E.2d 512</u></a>	
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36. <a href="#"><u>ASAP Paging Inc. v. Centurytel of San Marcos Inc., 137 Fed. Appx. 694</u></a>	
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37. [Med. Sav. Ins. Co. v. HCA, Inc., 2005 U.S. Dist. LEXIS 20206](#)

**Client/Matter:** -None-

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38. [Asociacion de Detallistas de Gasolina de P.R., Inc. v. Shell Chem. Yabucoa Inc., 380 F. Supp. 2d 40](#)

**Client/Matter:** -None-

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39. [Am. Copper & Brass, Inc. v. Donald Boliden AB, 2005 U.S. Dist. LEXIS 43642](#)

**Client/Matter:** -None-

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40. [In re Enron Corp., 2005 Bankr. LEXIS 3470](#)

**Client/Matter:** -None-

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41. [Sickles v. Cabot Corp., 379 N.J. Super. 100](#)

**Client/Matter:** -None-

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42. [Chase Med., LP v. CHF Techs., Inc., 2005 U.S. Dist. LEXIS 13731](#)

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**Client/Matter:** -None-

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43. [In re Enron Corp., 326 B.R. 257](#)

**Client/Matter:** -None-

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44. [Jackson, Tenn. Hosp. Co. v. W. Tenn. Healthcare, Inc., 414 F.3d 608](#)

**Client/Matter:** -None-

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45. [Sanderson v. Culligan Int'l Co., 415 F.3d 620](#)

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46. [Teamsters Local Union No. 117 v. Sysco Food Servs. of Seattle, Inc., 2005 U.S. Dist. LEXIS 43789](#)

**Client/Matter:** -None-

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47. [Schor v. Abbott Labs., 378 F. Supp. 2d 850](#)

**Client/Matter:** -None-

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48. [Meijer, Inc. v. 3M, 2005 U.S. Dist. LEXIS 13995](#)

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49. [Olstad v. Microsoft Corp., 2005 WI 121](#)

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50. [In re GlaxoSmithKline PLC, 699 N.W.2d 749](#)

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51. [Medtronic Navigation, Inc. v. BrainLAB Medizinische Computersystems GmbH, 2005 U.S. Dist. LEXIS 21695](#)

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52. [In re Enron Corp., 2005 Bankr. LEXIS 3471](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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53. [In re Acacia Media Techs. Corp., 2005 U.S. Dist. LEXIS 37009](#)

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54. [Briggs & Stratton Corp. v. Kohler Co., 2005 U.S. Dist. LEXIS 14808](#)

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55. [eMag Solutions LLC v. Toda Kogyo Corp., 2005 U.S. Dist. LEXIS 44512](#)

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56. [Lundsford v. Callaway Golf Co., 2005 U.S. Dist. LEXIS 59896](#)

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57. [Mothershed v. Justices of the Supreme Court, 2005 U.S. App. LEXIS 14812](#)

**Client/Matter:** -None-

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58. [In re Enron Corp., 2005 Bankr. LEXIS 3472](#)

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**Search Terms:** "antitrust law"

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59. [Loeffel Steel Prods. v. Delta Brands, Inc., 387 F. Supp. 2d 794](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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60. [Polygram Holding, Inc. v. FTC, 416 F.3d 29](#)

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61. [Kendall v. Visa U.S.A. Inc., 2005 U.S. Dist. LEXIS 21449](#)

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62. [Kendall v. Visa U.S.A., Inc., 2005 U.S. Dist. LEXIS 21450](#)

**Client/Matter:** -None-

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63. [People's Choice Wireless, Inc. v. Verizon Wireless, 131 Cal. App. 4th 656](#)

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64. [Banner Pharmacaps, Inc. v. Perrigo Co., 2005 U.S. Dist. LEXIS 37842](#)

**Client/Matter:** -None-

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65. [McBee v. Delica Co., 417 F.3d 107](#)

**Client/Matter:** -None-

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66. [In re Enron Corp., 328 B.R. 75](#)

**Client/Matter:** -None-

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

67. [Wine & Spirits Retailers, Inc. v. Rhode Island, 418 F.3d 36](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

68. [N. Jackson Pharm., Inc. v. Caremark RX, Inc., 385 F. Supp. 2d 740](#)

**Client/Matter:** -None-



**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

69. [Smith Wholesale Co. v. Philip Morris USA Inc., 2005 U.S. Dist. LEXIS 18078](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

70. [Guichard v. Mandalay Pictures, LLC, 2005 U.S. Dist. LEXIS 45410](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

71. [Wilson Learning Corp. v. Schlechte, 2005 U.S. Dist. LEXIS 39631](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

72. [Adeduntan v. Hosp. Auth. of Clarke County, 2005 U.S. Dist. LEXIS 18281](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

73. [Florida v. Tenet Healthcare Corp., 420 F. Supp. 2d 1288](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

74. [Freeman Indus. LLC v. Eastman Chem. Co., 172 S.W.3d 512](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Cases

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

75. [Hydril Co., L.P. v. Grant Prideco, L.P., 385 F. Supp. 2d 609](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Cases

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

76. [Insignia Sys., Inc. v. News Corp., Ltd., 2005 U.S. Dist. LEXIS 42851](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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Cases

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

77. [MGA Entm't, Inc. v. Mattel, Inc., 2005 U.S. Dist. LEXIS 18594](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

78. [Mpt, Inc. v. Marathon Labels, Inc., 2005 U.S. Dist. LEXIS 18270](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Cases

Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

79. [Reifert v. S. Cent. Wis. Mls Corp., 2005 U.S. Dist. LEXIS 23431](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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Cases

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

80. [Andrx Pharms., Inc. v. Elan Corp., PLC, 421 F.3d 1227](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

81. [In re Wireless Tel. Servs. Antitrust Litig., 385 F. Supp. 2d 403](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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**Narrowed by:**

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

82. [Ariz. Cartridge Remanufacturers Ass'n v. Lexmark Int'l, Inc., 421 F.3d 981](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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**Narrowed by**

Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

83. [In re Visa Check/Mastermoney Antitrust Litig., 2005 U.S. Dist. LEXIS 18693](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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**Narrowed by:**

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022



84. [Alaska Vill. Elec. Coop., Inc. v. Crowley Marine Servs., 2005 U.S. Dist. LEXIS 39668](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

85. [Creative Copier Servs. v. Xerox Corp., 2005 U.S. Dist. LEXIS 19402](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

**Narrowed by:**

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Cases

**Narrowed by**

Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

86. [Basic Med. Care Plus, Inc. v. N.C. Mut. Life Ins. Co., 2005 U.S. Dist. LEXIS 33033](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

87. [Geneva Pharm. Tech. Corp. v. Barr Labs., 2005 U.S. Dist. LEXIS 19069](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

88. [Schermer v. State Farm Fire & Cas. Co., 702 N.W.2d 898](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

**Narrowed by:**

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Cases

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

89. [Tritent Int'l Corp. v. Commonwealth, 2005 U.S. Dist. LEXIS 20233](#)

**Client/Matter:** -None-



**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

90. [Slattery v. Apple Comput., Inc., 2005 U.S. Dist. LEXIS 50531](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

91. [Corey Airport Servs. v. City of Atlanta, 2005 U.S. Dist. LEXIS 62370](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

**Narrowed by:**

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

92. [K&R Nursing Servs. v. Genesis Health Ventures of Windsor, Inc., 2005 Conn. Super. LEXIS 2473](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

**Narrowed by:**

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

93. [Lde Corp. v. Dyno Nobel, 2005 U.S. Dist. LEXIS 60985](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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**Narrowed by:**

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

94. [Texas v. Organon USA Inc. \(In re Remeron End-Payor Antitrust Litig.\), 2005 U.S. Dist. LEXIS 27011](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

95. [Harrison Aire, Inc. v. Aerostar Int'l, 423 F.3d 374](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

**Narrowed by:**

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

96. [Pelfresne v. Village of Lindenhurst, 2005 U.S. Dist. LEXIS 23094](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

97. [Strawflower Elecs., Inc. v. Radioshack Corp., 2005 U.S. Dist. LEXIS 45205](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Cases

**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

98. [Flying Eagle Espresso, Inc. v. Host Int'l, Inc., 2005 U.S. Dist. LEXIS 37679](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

**Search Type:** Natural Language

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**Narrowed by**  
Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

99. [Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc., 424 F.3d 363](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022

100. [PSN III., Inc. v. Ivoclar Vivadent, Inc., 2005 U.S. Dist. LEXIS 21044](#)

**Client/Matter:** -None-

**Search Terms:** "antitrust law"

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Practice Areas & Topics: Antitrust & Trade Law; Timeline:  
Oct 26, 2004 to Dec 31, 2022





## Merkle v. Aetna Health, Inc.

United States District Court for the Southern District of Florida

April 27, 2005, Decided; April 27, 2005, Entered on Docket

CASE NO. 04-61713-CIV-COHN

### **Reporter**

2005 U.S. Dist. LEXIS 47586 \*; 2005 WL 6151455

PETER F. MERKLE, M.D., P.A., Plaintiff, v. AETNA HEALTH, INC., NEIGHBORHOOD HEALTH PARTNERSHIP, INC., HEALTH OPTIONS, INC. and VISTA HEALTHPLANS, INC., Defendants.

**Subsequent History:** Related proceeding at, Motion granted by, Settled by [Merkle v. Vista Healthplan, Inc., 2010 U.S. Dist. LEXIS 146761 \(S.D. Fla., Aug. 16, 2010\)](#)

## **Core Terms**

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providers, private right of action, motion to dismiss, allegations, predicate act, subscribers, reimbursement, conspiracy, wire fraud, mail, antitrust claim, state law claim, particularity, disclose, racketeering activity, dispute resolution, restraint of trade, customary charge, enterprise, rates

**Counsel:** [\*1] For M.D.,P.A. Peter F. Merkle, Plaintiff: Douglas Alan Blankman, Lawrence M. Kopelman, LEAD ATTORNEYS, Kopelman & Blankman, Fort Lauderdale, FL; Eric Lee, LEAD ATTORNEY, Lee & Amtzis, P.L., Boca Raton, FL; Nicole Reid Avallone, LEAD ATTORNEY, Lerach Coughlin Stoia Geller Rudman & Robbins, Boca Raton, FL; Patrick William Lawlor, LEAD ATTORNEY, Law Office of Patrick W. Lawlor, Deerfield Beach, FL; Paul Jeffrey Geller, Stuart Andrew Davidson, LEAD ATTORNEYS, Robbins Geller Rudman & Dowd LLP, Boca Raton, FL.

For Aetna Health Inc., Defendant: Christine Marie Nanfeldt, Hilarie Bass, Mark Paul Schnapp, LEAD ATTORNEYS, Greenberg Traurig, Miami, FL; Geoffrey M. Sigler, Miguel A. Estrada, LEAD ATTORNEYS, Gibson Dunn & Crutcher, Washington, DC; Glenn Jerrold Waldman, LEAD ATTORNEY, Waldman Trigoboff Hildebrandt Marx & Calnan, P.A., Weston, FL; Kevin R. Nowicki, LEAD ATTORNEY, Gibson Dunn & Crutcher, Irvine, CA; Richard J. Doren, LEAD ATTORNEY, Gibson Dunn & Crutcher, Los Angeles, CA.

For Neighborhood Health Partnership, Inc., Defendant: Patrick S. Coffey, LEAD ATTORNEY, Scott J. Fisher, Gardner Carton & Douglas, Chicago, IL; William Edward McIntyre, LEAD ATTORNEY, Daniel Alter, Bunnell Woulfe Kirschbaum [\*2] Keller McIntyre & Gregoire, Fort Lauderdale, FL.

For Health Options,Inc., Defendant: Michael Garrett Austin, LEAD ATTORNEY, Steven E. Siff, McDermott Will & Emery LLP, Miami, FL.

For Vista Healthplan Inc, Defendant: Steven Mark Ziegler, LEAD ATTORNEY, Andres Gonzalez, Steven M. Ziegler PA, Hollywood, FL; Dorothy Frances Easley, Easley Appellate Practice PLLC, Miami, FL.

**Judges:** JAMES I. COHN, United States District Judge.

**Opinion by:** JAMES I. COHN

## **Opinion**

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## **FINAL ORDER GRANTING MOTIONS TO DISMISS**

THIS CAUSE is before the Court upon Defendant Vista Healthplans, Inc.'s Motion to Dismiss [DE 52], Vista Healthplans' Motion for Judicial Notice [DE 53], Defendant Neighborhood Health Partnership, Inc.'s Motion to Dismiss [DE 55], Defendant Aetna Health, Inc.'s Motion to Dismiss [DE 56], and Defendant Health Options, Inc.'s Motion to Dismiss [DE 60]. The Court has carefully considered the motions, responses, replies and the argument of counsel made at a hearing held on April 19, 2005.

### I. BACKGROUND

Plaintiff, an orthopedic physician, filed this class action against four health maintenance organizations ("HMO's") asserting claims for violation of the federal Racketeer Influenced and Corrupt Organizations Act ("RICO"), federal **antitrust** [\*3] **law**, quantum meruit, unjust enrichment, and violation of [Florida Statute Section 641.513](#). Plaintiff alleges that beginning on or about May, 2003, the four Defendants engaged in a scheme to violate Florida law and federal law by paying non-participating emergency physicians at a rate below the usual and customary charges for those services.

Plaintiff and the putative class of plaintiffs ("Plaintiffs") are physicians who provide emergency services in hospitals. These physicians can be specialists in a variety of fields. The Defendants are health maintenance organizations offering health insurance to their insureds ("subscribers"), some of whom have required emergency care from Plaintiffs. Plaintiffs do not have a contract with these Defendants to provide such care. However, pursuant to [Florida Statute § 641.513](#), Plaintiffs are required to provide emergency treatment to Defendants' subscribers. Plaintiffs are also prohibited from billing these subscribers for any amount over the copayment or coinsurance required by Defendants, pursuant to Florida law and the contract between Defendants and the subscribers. In return, Defendants must compensate Plaintiffs. [Section 641.513\(5\)](#) states that [\*4] such compensation shall be the lesser of: (a) the provider's charges; (b) the usual and customary provider charges for similar services in the community where the services were provided; or (c) the charge mutually agreed to by the health maintenance organization and the provider within 60 days of the submittal of the claim. If there is no agreement, disputes arise regarding the meaning of subsection (b), in particular the amount of the "usual and customary" charges.

To resolve these disputes, in 2000, the Florida legislature enacted [Florida Statutes § 408.7057](#), which creates a voluntary, but binding, dispute resolution process for resolving claims between health care providers and health maintenance organizations. See [Health Options, Inc. v. Agency for Health Care Administration, 889 So.2d 849, 851-52 \(Fla. 1st DCA 2004\)](#). The Agency for Health Care Administration ("AHCA"), a state agency, has selected Maximus, Inc., an independent, third-party claim dispute resolution entity to review these claim disputes. [889 So.2d at 850](#). Under [§ 408.7057](#), AHCA does not have discretion to accept or reject a Maximus' decision, but rather must accept such decision and issue a final agency order within [\*5] 30 days. [Id. at 852](#). Defendants have submitted to the Court several decisions by AHCA approving payment of claims from providers similarly situated to Plaintiffs at 120% of Medicare reimbursement rates as being the usual and customary charges contemplated by [§ 641.513\(5\)\(b\)](#) [DE 53].<sup>1</sup>

In this action, therefore, based upon the Complaint and Defendant's motions to dismiss, there appear to be few facts, if any, in dispute. Defendants essentially admit, at least for purposes of the motions to dismiss, that after Maximus and AHCA approved 120% of Medicare reimbursement rates to providers covered by [§ 641.513](#) on June 11, 2003, they each separately decided to reduce their reimbursement rates to this level.<sup>2</sup> Nonetheless, the Court

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<sup>1</sup>The Court will grant, without any opposition in the record, Vista Healthplans' Motion for Judicial Notice of the Maximus/ACHA decisions.

<sup>2</sup>On June 11, 2003, Maximus rendered its initial decision in a claims dispute between BayCare Health System, Inc. and Blue Cross Blue Shield of Florida/Health [\*6] Options. Following BayCare's withdrawal of its claims, on August 11, 2003, AHCA rendered its final decision dismissing the matter. Exhibit D to Plaintiff's Omnibus Consolidated Opposition to Defendants' Motions [DE 67]. The First District Court of Appeal reversed this dismissal in the [Health Options](#) opinion cited *supra*.

analyzed each of the four Defendants' motions to dismiss under a [Rule 12\(b\)\(6\)](#) standard. As many of Defendants' arguments overlap and are similar, they will be discussed together.

## II. DISCUSSION

In ruling upon the motions to dismiss, despite the apparent lack of facts in dispute, the Court nonetheless views the factual allegations of the complaint as true and must be read to include any theory on which the plaintiff may recover. See [Linder v. Portocarrero, 963 F.2d 332, 334-336 \(11th Cir. 1992\)](#) (citing [Robertson v. Johnston, 376 F.2d 43 \(5th Cir. 1967\)](#)). With regard to the particular claims, the Court notes that although a principal issue in dispute is whether a private right of action exists for providers pursuant to [Florida Statute 641.513](#), the non-existence of such a cause of action does not automatically doom Plaintiffs' RICO and antitrust claims. Plaintiffs have also plead predicate acts in the RICO claims based upon mail fraud, wire fraud, and extortion. The Court will thus first discuss the RICO and antitrust claims without reliance upon the [\*7] existence of a private right of action under [Section 641.513](#).

### A. RICO Issues

In order to prove any RICO violation, Plaintiffs must prove the existence of an "enterprise" and a "pattern of racketeering activity." [18 U.S.C. § 1962](#); [Beck v. Prupis, 162 F.3d 1090 \(11th Cir. 1998\)](#). A "pattern of racketeering activity" requires the plaintiff to establish "at least two acts of racketeering activity." [18 U.S.C. § 1961\(5\)](#); [Republic of Panama, 119 F.3d at 948](#). When mail or wire fraud are alleged as the predicate acts that are indictable as racketeering activity, as in the instant case, a plaintiff must allege facts sufficient to support the element of intentional misrepresentation that is part of a "scheme to defraud." [Beck, 162 F.3d at 1095](#); [Republic of Panama, 119 F.3d at 949](#) (plaintiff must allege facts to support each element for at least two predicate acts).

#### 1. Enterprise

Defendants argue that Plaintiffs' allegations of the enterprise in this case are insufficient. See Compl. ¶¶ 135-143. Plaintiffs assert that pursuant to [U.S. v. Goldin, 219 F.3d 1271, 1274-75 \(11th Cir.\)](#), cert. denied, 531 U.S. 1015, 121 S. Ct. 573, 148 L. Ed. 2d 491 (2000) and [In re Managed Care Litigation, 298 F.Supp.2d 1259, 1277 \(S.D.Fla. 2003\)](#) the allegations [\*8] of the Complaint in this case are sufficient. Defendants assert that pursuant to [United States v. Turkette, 452 U.S. 576, 583, 101 S. Ct. 2524, 69 L. Ed. 2d 246 \(1981\)](#), Plaintiffs have pled insufficient allegations of participation and control in the alleged enterprise. However, upon a review of Plaintiffs' allegations in the Complaint, the Court concludes that pursuant to [Goldin](#), an Eleventh Circuit decision made after [Turkette](#) (for which review was denied), Plaintiffs have sufficiently alleged an enterprise and Defendants' participation and control thereof.

#### 2. Predicate Acts

Defendants assert several shortcomings with respect to Plaintiffs' allegations regarding the predicate acts. As noted above, though Defendants argue that violations of [§ 641.513](#) cannot constitute a predicate act as no private right of action exists, the RICO claims could be based upon predicate acts of mail or wire fraud,<sup>3</sup> irrespective of the existence of a private right of action under [§ 641.513](#).

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<sup>3</sup> Plaintiffs also attempt to assert acts of extortion as predicate acts. There are at least two reasons to reject this attempt. First, in [Scheidler v. NOW, 537 U.S. 393, 123 S. Ct. 1057, 154 L. Ed. 2d 991 \(2003\)](#), the Supreme Court held that a plaintiff must allege that a RICO defendant acquire [\*9] some property from injured plaintiffs. Though Plaintiffs assert that Defendants have withheld money belonging to Plaintiffs, rather than an act of extortion, the parties actually have a dispute over interpretation of "usual and customary" charges. Second, in this case the medical providers are required to provide services by statute and cannot balance

Defendants also assert that the allegations of mail and wire fraud lack the requisite particularity required by [Rule 9\(b\) of the Federal Rules of Civil Procedure](#). [Rule 9\(b\)](#) provides that "[i]n all averments of fraud . . . the circumstances constituting fraud . . . shall be stated with particularity." [Fed. R. Civ. P. 9\(b\)](#). The particularity requirement of [Rule 9\(b\)](#) serves an important purpose in fraud actions by "alerting defendants to the precise misconduct with which they are charged and protecting spurious charges of immoral and fraudulent behavior." [Ziemba v. Cascade Int'l, Inc.](#), 256 F.3d 1194 (11th Cir. 2001) (internal quotation marks omitted). The application [\*10] of [Rule 9\(b\)](#), however, must not abrogate the concept of notice pleading under the federal rules, *Id.*; [Friedlander v. Nims](#), 755 F.2d 810, 813 n.2 (11th Cir. 1985) ("[A] court considering a motion to dismiss for failure to plead fraud with particularity should always be careful to harmonize the directives of [rule 9\(b\)](#) with the broader policy of notice pleading."). Allegations of date, time, or place satisfy the requirement of [Rule 9\(b\)](#) that the circumstances of the fraud be alleged with particularity, but alternative means are also available to satisfy the rule. [Durham v. Business Management Associates](#), 847 F.2d 1505, 1512 (11th Cir. 1988).

Plaintiffs argue that the Complaint does provide sufficient particularity. See Compl. ¶¶ 153-156. Plaintiffs' theory of mail and wire fraud is that the Defendants' sending of Explanation of Benefits ("EOB's") to Plaintiffs containing the unlawful low paid amount fails to disclose that Defendants have concluded that the "usual and customary" requirement in [§ 641.513](#) can be met by payment of 120% of Medicare rate. Plaintiffs assert that the failure to disclose the wrongfully calculated payment amounts to a deception.

While the Court tends to agree with [\*11] Plaintiff that at first glance the requisite particularity has been alleged by use of the EOB's, the problem with Plaintiffs' argument is that the sending of the EOB's is not deceptive. As discussed in oral argument and agreed upon by counsel for Plaintiffs, to constitute mail or wire fraud, the acts must contain some deception and intent to deceive. There appears to be no dispute that the EOB's contain accurate information - that is, the amount stated on the EOB is the amount paid. See Exhibits 3, 5, 6 and 7 to Complaint.<sup>4</sup> Plaintiffs further argue that the Defendants knew that their payments were based upon 120% of the Medicare reimbursement rate, which cannot be in compliance with the "usual and customary charges" requirement in [§ 641.513](#).

Defendants [\*12] argue that Florida law does not require them to disclose the underlying computation of proprietary rates. In [Langford v. Rite Aid of Alabama, Inc.](#), 231 F.3d 1308, 1312 -1313 (11th Cir. 2000), the Eleventh Circuit affirmed the granting of a motion to dismiss in a case in which uninsured customers alleged pharmacists had a duty to disclose the differential pricing between uninsured versus insured customers. The Court held that a district court must look beyond statutory/regulatory duties, and also look beyond normal state common law duties, since "concealment of critical data, even without a formalized duty to disclose that data, can constitute mail and/or wire fraud in certain situations." [231 F.3d at 1312](#). The Eleventh Circuit ultimately found no duty to disclose this differential in pricing and affirmed the granting of a motion to dismiss the RICO claims in [Langford](#). *Id. at 1314*.

Plaintiffs, however, reply upon Judge Moreno's decision in [In re Managed Care Litigation](#), 298 F.Supp.2d at 1278. Judge Moreno followed the [Langford](#) decision quoted above, but denied the motion dismiss by concluding that: "these failed disclosures alleged in the [Second Amended Complaint] go to 'the heart of [\*13] their relationship' and disclosure was necessary to prevent the doctors from being misled by Defendants' apparent actions and statements." In oral argument, Plaintiff relied solely upon this decision to distinguish the present case from the [Langford](#) decision.

The allegations in Judge Moreno's case are distinguishable from the allegations in this case. As described by Plaintiffs' counsel at the hearing on Aetna's Motion to Transfer, in this case there are no allegations of "downcoding"

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bill their HMO patients. Thus, Defendants are not making any threats to Plaintiffs regarding their property, but rather are simply (allegedly) not paying enough under the statute.

<sup>4</sup> The Court may consider documents referred to by a plaintiff in a complaint which are central to the plaintiff's claim for purposes of a motion to dismiss without conversion of the motion to dismiss into a motion for summary judgment. [Brooks v. Blue Cross & Blue Shield of Fla.](#), 116 F.3d 1364, 1369 (11th Cir. 1997) (opinion of then United States District Court Judge Stanley Marcus attached to Eleventh Circuit opinion); [Smith Barney, Inc. v. Scanlon](#), 180 F.R.D. 444, 446 (S.D.Fla. 1998).

or affirmative misrepresentations on the EOB's. See Transcript of Hearing at pp. 14-16 [DE 69]. Thus, the Court concludes that as this case is more like Langford, in that the Defendants' EOB's are accurate but reflect undisclosed changes in rate calculations, the EOB's cannot form the basis of a claim of mail or wire fraud as predicate acts under RICO.<sup>5</sup>

In response to Plaintiff's argument that the Court must assume that the Maximus decision interpreting § 641.513 as allowing 120% of Medicare rates to be considered "usual and customary charges" is wrong, the Court concludes that the relevant issue before the Court is not whether the Maximus' decisions, as accepted by ACHA, are wrong or not, but rather whether Plaintiff can allege predicate acts and a pattern of racketeering activity necessary to state a RICO claim when the acts complained of are approved by a Florida state agency.<sup>6</sup> The fact of Maximus' decision, coupled with the lack of deception in the alleged predicate acts, leads this Court to conclude that it appears beyond a doubt that Plaintiffs can prove no set of facts in support of the RICO claims which would entitle them to relief. Conley v. Gibson, 355 U.S. 41, 78 S. Ct. 99, 2 L. Ed. 2d 80 (1957).

## **B. Antitrust Issues**

Defendants move to dismiss Plaintiff's claims of a conspiracy to restrain trade in the pursuant to Section 1 of the Sherman Act. The Eleventh Circuit has stated that:

Section 1 of the Sherman Act broadly prohibits "[e]very contract, combination ... or conspiracy, in restraint of trade or commerce ...." A § 1 conspiracy to restrain trade does not need to allege the specific element of a conspiracy to monopolize, but must allege 1) an agreement to enter a conspiracy, 2) designed to achieve an unlawful objective. It is fundamental that a plaintiff establish an agreement between two or more persons to restrain trade; unilateral conduct is not prohibited by § 1.

Aquatherm Industries, Inc. v. Florida Power & Light Co., 145 F.3d 1258, 1262 (11th Cir. 1998), [\*16] cert. denied, 526 U.S. 1050, 119 S. Ct. 1356, 143 L. Ed. 2d 517 (1999) (internal citations omitted).

Defendants argue that Plaintiffs have not alleged a specific geographic market, in that emergency services are generally provided to a local market, not an entire state. Defendants also assert that allegations of companies acting in parallel (parallelism) are insufficient to state a conspiracy in restraint of trade. See Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 588, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986) ("conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy"). The Eleventh Circuit has held that "price fixing plaintiffs must demonstrate the existence of 'plus factors' that remove their evidence from the realm of equipoise and render that evidence more probative of conspiracy than of conscious parallelism." Williamson Oil Co., Inc. v. Philip Morris USA, 346 F.3d 1287, 1301 (11th Cir. 2003).<sup>7</sup> Plaintiffs respond by stating that they have alleged several plus factors, including motive to conspire

<sup>5</sup> As for the letters Defendants' sent to subscribers informing them that the providers cannot bill the subscribers for the unpaid balance (Exhibit 2 to Complaint), these too are accurate statements containing no deception. Furthermore, as the Plaintiffs were not the recipients of those letters, Plaintiffs conceded that they cannot use these letters as predicate [\*14] acts which caused injury to Plaintiffs. Byrne v. Nezhat, 261 F.3d 1075, 1110 (11th Cir. 2001), citing Pelletier v. Zweifel, 921 F.2d 1465, 1499 (11th Cir. 1991).

<sup>6</sup> Though not necessary at this point (though the issue was fully briefed and argued), the Court does reject Defendants' argument that Plaintiffs cannot show any reliance upon Defendants' acts of sending [\*15] the EOB's because the providers are required to treat the patients before they are aware of the reimbursement rate. The providers are relying upon receipt from Defendants of "the usual and customary charges," pursuant to § 641.513, in return for their provision of emergency services to HMO subscribers. Thus, under the particular statutory duties of provision of care and payment to providers, the Court will infer that the reliance element is present in this case.

(financial gain), opportunity to conspire (use of same reimbursement guidelines and participation in industry coordination); [\*17] and sharp departure from normal business practices (sudden onset of reimbursement reductions). See Plaintiffs' Omnibus Consolidated Memorandum at 41-43 [DE 67].

This Court agrees with Defendants that their conduct in lowering reimbursement payments is consistent with each Defendant's self interest. Other than the sharp onset of the lowered [\*18] reimbursements, and access to industry software and guidelines, Plaintiffs have failed to allege any other plus factors. Moreover, though this conclusion is based upon a motion to dismiss standard, it is undisputed that the timing of the onset of Defendants' lowering of payments is explained by the Maximus ruling of June 11, 2003.

In addition, Plaintiffs have failed to sufficiently allege how competition is negatively affected by Defendants' conduct or what unlawful objective is to be achieved. Defendants and Plaintiffs do not compete. In fact, [§ 641.513](#) requires Plaintiffs to provide emergency care to Defendant's customers, and requires Defendants to pay providers for these services. Defendants' actions treat all providers equally. Defendants do not benefit from driving providers out of the business of providing health care services. Thus, the Court concludes that Plaintiffs have failed to state an antitrust claim.

### **C. ERISA Preemption**

Before turning to whether to consider Plaintiffs' state law claims, Defendant Aetna Health asserts in their brief that any such state law claims would be preempted by ERISA. Pursuant to ERISA "super-preemption," a state common law claim is removable if [\*19] it relates to an ERISA plan. [Metropolitan Life Ins. Co. v. Taylor, 481 U.S. 58, 66-67, 107 S. Ct. 1542, 95 L. Ed. 2d 55 \(1987\)](#). Four elements are required for complete preemption: 1) there must be a relevant ERISA plan; 2) plaintiff must have standing to sue under that plan; 3) the defendant must be an ERISA entity; and 4) the complaint must seek compensatory relief akin to that available under [29 U.S.C. § 1132\(a\)](#) (typically this will be a claim for benefits due under the plan). [Butero v. Royal Maccabees Life Insurance Company, 174 F.3d 1207, 1212 \(11th Cir. 1999\)](#). In this case, Plaintiff argues that the standing to sue element is missing.

Although providers can obtain ERISA standing through an assignment from a beneficiary, [Hobbs v. Blue Cross Blue Shield of Alabama, 276 F.3d 1236 \(11th Cir. 2001\)](#), Plaintiff argues that it seeks reimbursement as a non-participating provider pursuant to [§ 641.513](#), and not as an assignee under the ERISA plan. This Court agrees. Therefore, if Plaintiffs could bring a state law claim, such claims should not be dismissed on grounds of ERISA preemption.

### **D. Section 1367(c)- Declining to assert supplemental jurisdiction**

Defendants Health Options, Vista, and Neighborhood Health urge this Court [\*20] to decline to exercise supplemental jurisdiction over any remaining state law claims. With the dismissal of the federal claims, [28 U.S.C. § 1367\(c\)\(3\)](#) allows a district court to decline to exercise supplemental jurisdiction when all claims over which it has original jurisdiction have been dismissed, as is now the case herein.

The Court notes that the issue of whether Plaintiffs have a private right of action under [§ 641.513](#) is a close question.<sup>8</sup> Defendants put forth several arguments against reading [§ 641.513](#) as containing a private right of

<sup>7</sup> Examples of "plus" factors include: "(1) signaling of intentions; (2) permanent allocations programs; (3) monitoring of sales; (4) actions taken contrary to economic self-interest, including (a) little analysis of whether to follow price increases, (b) [competitors] pulling away from the discount cigarette market, (c) the May 1995 price increase lead by RJR and followed by Philip Morris, (d) Philip Morris' agreement to base the initial [Management Science Associates] ... payments on market capitalization rather than market share, and (e) 'excessive' price increases after the MSA; (5) nature of the market; (6) strong motivation; (7) reduction in the number of price tiers; (8) opportunities to conspire; (9) pricing decisions made at high levels; (10) the smoking and health conspiracy; and (11) foreign conspiracies." [Williamson Oil Co., 346 F.3d at 1305](#).

action. First, the language of the statute itself does not contain an explicit right of action. Second, the overall statutory scheme in Florida for HMO's includes a voluntary, though binding, dispute resolution provision in [§ 408.7057](#). Third, Defendants submitted extensive legislative history wherein attempts to include a private right of action have been defeated, and, a version of the HMO act which included a private right of action was vetoed by then Gov. Lawton Chiles because of such a suit provision (according to Defendants) [DE 54]. Defendants also assert that the legislative history of the current act contains no inference of a private right [\*21] of action. Finally, Defendants assert that the Florida Supreme Court has rejected a private right of action for subscribers against HMO's under the HMO Act. [Villazon v. Prudential Health Care Plan, 843 So.2d 842 \(Fla. 2003\)](#).

Plaintiffs also make credible arguments in favor of inference of a private right of action. For example, other parts of the health care laws support inference of a private right of action for providers to enforce [§ 641.513](#). For example, [§ 641.3154\(4\)](#), within the HMO Act, states in part that:

this prohibition [against balance billing the HMO subscriber] applies during the pendency of any claim for payment made by the provider to the organization for payment of the services **and any legal proceedings** or dispute resolution process to determine whether the organization is liable for the [\*22] services if the provider is informed that such proceedings are taking place.

[Fla. Stat. § 641.3154\(4\)](#) (emphasis added).<sup>9</sup> Plaintiffs also argue that prior to legislative enactment of a cause of action, Florida courts inferred a private right of action for automobile injuries under the Personal Injury Protection ("PIP") statutory scheme in [Fla. Stat. § 627.736](#).

Perhaps Plaintiffs' best argument is that [§ 641.513](#) was intended to require HMO's to pay for emergency care, in exchange for requiring providers to provide such care without billing subscribers beyond their copay. Thus, without a provider right of action to collect usual and customary charges from the HMO, no remedy is available.

Plaintiffs further contend that the voluntary Maximus dispute resolution process is not a viable remedy. Plaintiffs argue that the Maximus decisions have no legal value, as they are the result of "some unknown Maximus employee" making a determination that a payment rate of 120% of Medicare was appropriate. Plaintiffs also seek to distinguish [Villazon](#) as a case involving subscriber suits under the HMO Act, [\*23] which [Villazon](#) described as [Fla. Stat. §§ 641.17-641.3923](#), not including [§ 641.513](#). Moreover, subscribers do have contractual remedies not available to non-participating providers, who care for HMO subscribers pursuant to statute, not pursuant to a contract.

Plaintiffs also provide examples of other statutes where private rights of action have been inferred by the Courts. First, three District Court of Appeals have held that hospitals are liable for failing to enforce requirements that physicians who obtain hospital privileges have malpractice insurance or meet the conditions to not have such insurance. [Mercy Hosp., Inc. v. Baumgardner, 870 So.2d 130, 131 \(Fla.App. 3 Dist. 2003\)](#); [Robert v. Paschall, 767 So.2d 1227 \(Fla. 5th DCA 2000\)](#), review denied, 786 So. 2d 1187 (Fla.2001); [Baker v. Tenet Healthsystem Hosps., Inc., 780 So. 2d 170 \(Fla. 2d DCA 2001\)](#). However, the 4th DCA recently reached the opposite conclusion. [Plantation General Hosp. Ltd. Partnership v. Horowitz, 895 So. 2d 484, 2005 WL 293031, \\*2 \(Fla.App. 4 Dist. 2005\)](#).

While all of Plaintiffs' arguments regarding analogous statutes are well taken, each situation involves a Florida court inferring a private right of action in a state statute. As [\*24] a federal court, this Court must be particularly careful when inferring a new state law cause of action. [Swerhun v. Guardian Life Ins. Co. of America, 979 F.2d 195, 198 \(11th Cir. 1992\)](#) (citing [Farlow v. Union Cent. Life Ins. Co., 874 F.2d 791, 795 \(11th Cir. 1989\)](#)). In addition, given the novel nature of the claim and uncertainty over whether a private cause of action exists, it is all the more

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<sup>8</sup> With regard to Plaintiffs' claims of unjust enrichment or quantum meruit, counsel for Health Options appeared to concede, upon questioning by the Court of Plaintiffs' available remedies if no private right of action exists, that such claims could be brought in state court. The Court need not decide if such a concession was made, as it will decline to exercise supplemental jurisdiction.

<sup>9</sup> The Court notes that Defendant Aetna asserts that this reference is intended to mean ERISA litigation.

appropriate for this Court, pursuant to [Section 1367\(c\)\(1\)](#) ("novel or complex issue of State law") and [\(c\)\(3\)](#) (dismissal of all federal claims), to exercise its discretion and dismiss the state law claims set forth in Counts V through VII.

### III. CONCLUSION

The Court further concludes that affording Plaintiffs leave to file an amended complaint as to the RICO and antitrust claims would be futile in this case. As noted above, there are no material facts in dispute. Defendants, at least for purposes of this motion to dismiss, admit that they took the actions Plaintiffs assert form the basis of the RICO and antitrust claims. What is in dispute is whether those acts state a valid claim. In addition, the Court notes that Plaintiffs did not seek leave to amend as an alternative basis to deny the motions [\*25] to dismiss with prejudice.

Accordingly, it is **ORDERED AND ADJUDGED** as follows:

1. Vista Healthplans' Motion for Judicial Notice [DE 53] is hereby **GRANTED**;
2. Defendant Vista Healthplans, Inc.'s Motion to Dismiss [DE 52] is hereby **GRANTED**;
3. Defendant Neighborhood Health Partnership, Inc.'s Motion to Dismiss [DE 55] is hereby **GRANTED**;
4. Defendant Aetna Health, Inc.'s Motion to Dismiss [DE 56] is hereby **GRANTED**;
5. Defendant Health Options, Inc.'s Motion to Dismiss [DE 60] is hereby **GRANTED**;
6. The RICO and antitrust claims are hereby **DISMISSED with prejudice**, while the state law claims in Counts V through VII are hereby **DISMISSED, without prejudice**;
7. The Clerk may close this case and deny any other motions as moot.

**DONE AND ORDERED** in Chambers at Fort Lauderdale, Broward County, Florida, this 27th day of April, 2005.

/s/ James I. Cohn

JAMES I. COHN

United States District Judge

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## Riley v. R.I. Dep't of Envtl. Mgmt.

Superior Court of Rhode Island, Providence

April 27, 2005, Filed

C.A. NO. PC 04-0987

### **Reporter**

2005 R.I. Super. LEXIS 62 \*; 2005-1 Trade Cas. (CCH) P74,814

STEVEN RILEY v. RHODE ISLAND DEPARTMENT OF ENVIRONMENTAL MANAGEMENT, and FREDERICK J. VINCENT, in his capacity as interim director of the RHODE ISLAND DEPARTMENT OF ENVIRONMENTAL MANAGEMENT

**Subsequent History:** Affirmed by [Riley v. R.I. Dep't of Envtl. Mgmt., 941 A.2d 198, 2008 R.I. LEXIS 15 \(R.I., Feb. 14, 2008\)](#)

**Disposition:** [\*1] Court denies the declaratory relief prayed for by the Appellant and affirms the decision of the D.E.M Hearing Officer.

## **Core Terms**

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license, fishery, fishing, regulation, fundamental rights, commercial fishing, general assembly, rights, Marine, hearing officer, Sherman Act, moratorium, resources, substantial evidence, new license, endorsements, finfish, classification, argues, plenary power, occupation, provisions, violates, declaratory judgment, equal protection, summary judgment, anti trust law, exemption, fishermen, shellfish

## **LexisNexis® Headnotes**

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Governments > State & Territorial Governments > Licenses

### [HN1](#) State & Territorial Governments, Licenses

See [R.I. Gen. Laws § 20-2.1-5\(1\)\(ii\).](#)

Civil Procedure > ... > Declaratory Judgments > State Declaratory Judgments > Uniform Declaratory Judgment Act

Civil Procedure > Judgments > Declaratory Judgments > General Overview

Civil Procedure > ... > Declaratory Judgments > State Declaratory Judgments > General Overview

### [HN2](#) State Declaratory Judgments, Uniform Declaratory Judgment Act

The Uniform Declaratory Judgments Act, [R.I. Gen. Laws § 9-30-1](#) (1956) et seq., grants the Superior Court power to declare rights, status, and other legal relations whether or not relief is or could be claimed. The Declaratory Act also provides that the Superior Court may grant additional affirmative relief based on the declaratory judgment whenever necessary or proper provided subsequent supplementary proceedings are brought pursuant thereto.

Civil Procedure > Judgments > Declaratory Judgments > General Overview

### **[HN3](#) [] Judgments, Declaratory Judgments**

See [R.I. Gen. Laws § 9-30-2](#) (1956).

Civil Procedure > ... > Declaratory Judgments > State Declaratory Judgments > Discretionary Jurisdiction

Civil Procedure > Judgments > Declaratory Judgments > General Overview

Civil Procedure > ... > Declaratory Judgments > State Declaratory Judgments > General Overview

Civil Procedure > ... > Declaratory Judgments > State Declaratory Judgments > Uniform Declaratory Judgment Act

### **[HN4](#) [] State Declaratory Judgments, Discretionary Jurisdiction**

The purpose of the Uniform Declaratory Judgments Act, [R.I. Gen. Laws § 9-30-1 et seq.](#) (1956), is to facilitate the termination of controversies. The decision to issue a declaratory judgment lies within the trial justice's broad discretion. [R.I. Gen. Laws § 9-30-12](#) (1956) provides that the Declaratory Act should be liberally construed and administered. Existence of alternate methods of relief, including administrative, do not preclude declaratory judgment.

Administrative Law > Judicial Review > Standards of Review > General Overview

Administrative Law > Judicial Review > General Overview

### **[HN5](#) [] Judicial Review, Standards of Review**

Judicial review of contested agency decisions is governed by [R.I. Gen. Laws § 42-35-15\(g\)](#) (1956).

Administrative Law > Judicial Review > Standards of Review > General Overview

### **[HN6](#) [] Judicial Review, Standards of Review**

See [R.I. Gen. Laws § 42-35-15\(g\)](#) (1956).

Administrative Law > Judicial Review > Standards of Review > Substantial Evidence

Environmental Law > Administrative Proceedings & Litigation > Judicial Review

## **HN7** Standards of Review, Substantial Evidence

The reviewing court is precluded from substituting its judgment for that of the agency regarding witness credibility or the weight of evidence concerning questions of fact. The court's review is limited to determining whether substantial evidence exists to support the agency's decision. Substantial evidence means such relevant evidence that a reasonable mind might accept as adequate to support a conclusion, and means an amount more than a scintilla but less than a preponderance. The court will reverse factual conclusions of administrative agencies only when they are totally devoid of competent evidentiary support in the record. In deference to the agency, the court must uphold the agency's conclusions when they are supported by any legally competent evidence in the record.

[Administrative Law > Separation of Powers > Legislative Controls > Explicit Delegation of Authority](#)

[Governments > Legislation > Enactment](#)

[Administrative Law > Agency Rulemaking > General Overview](#)

[Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview](#)

[Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection](#)

## **HN8** Legislative Controls, Explicit Delegation of Authority

When an agency promulgates regulations pursuant to specific authority granted by the Rhode Island General Assembly, the regulations are legislative rules that carry the force and effect of law and enjoy a presumption of validity. To determine whether a rule is to be classified as legislative or interpretive, one must consider the power assigned to the administrative agency. If a statute expressly delegates power to interpret and define certain legislation to an agency, regulations promulgated pursuant to that power are legislative rules having the force of law. Legislative rules are valid if they are within the power granted by the General Assembly, are issued pursuant to proper procedure, and are reasonable as a matter of due process.

[Constitutional Law > ... > Fundamental Rights > Procedural Due Process > General Overview](#)

[Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview](#)

[Administrative Law > Judicial Review > Standards of Review > Arbitrary & Capricious Standard of Review](#)

[Constitutional Law > ... > Case or Controversy > Constitutionality of Legislation > General Overview](#)

[Constitutional Law > Equal Protection > Judicial Review > Standards of Review](#)

[Constitutional Law > Equal Protection > Nature & Scope of Protection](#)

## **HN9** Fundamental Rights, Procedural Due Process

If a regulation is challenged on constitutional due process or equal protection grounds and does not infringe upon a fundamental constitutional right or implicates a suspect class, the regulation must be rationally related to furthering a legitimate state interest in order to be upheld. Only if a regulation is without any reasonable basis and purely arbitrary will it be found unconstitutional under this standard.

Constitutional Law > Substantive Due Process > General Overview

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > General Overview

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Constitutional Law > Equal Protection > Nature & Scope of Protection

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > State & Territorial Governments > Licenses

#### **HN10** [blue icon] Constitutional Law, Substantive Due Process

In regard to [R.I. Gen. Laws § 20-2.1-1 et. seq.](#) (1956), the scope of the fundamental right protected in [R.I. Const. art. I, § 17](#), is that all the inhabitants of the state shall continue to enjoy and freely exercise equal access to the state's fishery resources. This gives the benefits of fishery to all the people in equal measure. The very nature and scope of the right to fish that [R.I. Const. art. I, § 17](#) protects is not unqualified; rather, it anticipates that reasonable legislative regulation is necessary to properly effectuate that right. If a statute or regulation contained restrictions that infringed upon the fundamental right of the inhabitants of the state to have equal access to the rights of fishery, then such a regulation or law would be subject to strict-scrutiny analysis. Such fishing is not merely for the profit and emolument of the fishermen engaged in the business. In addressing the substantive due process claim, the burden is on the plaintiffs to prove beyond a reasonable doubt that the provisions of the statute lack a substantial relation to the public health, safety, and welfare, or to the Legislature's constitutionally prescribed duty to protect and conserve the fishery resources of the state. There is no violation of equal protection or due process rights and the statute is constitutional.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Constitutional Law > Equal Protection > Judicial Review > Standards of Review

Governments > Legislation > Enactment

Governments > State & Territorial Governments > Legislatures

#### **HN11** [blue icon] Judicial & Legislative Restraints, Overbreadth & Vagueness of Legislation

Within the Rhode Island Constitution's broad grant of legislative power to the Rhode Island General Assembly lies its plenary power to regulate the fishing resources of the state. Furthermore, the whole subject of fisheries is under the fostering care of the General Assembly. Not all legislative classifications, however, are impermissible. The Legislature enjoys a wide scope of discretion in enacting laws that affect some classes of citizens differently from others. Strict scrutiny applies when a fundamental right has been impinged upon, or a suspect classification arises. The court will employ a minimal-scrutiny analysis, however, when assessing economic or social regulations that neither infringe on a fundamental right, nor result in a classification that is "suspect." The scope of the liberty interests protected by the Fourteenth Amendment includes the right of the individual to engage in the common occupations of life, and generally to enjoy those privileges long recognized as essential to the orderly pursuit of happiness by free men.

Governments > State & Territorial Governments > Legislatures

Governments > State & Territorial Governments > Licenses

## **HN12** [blue icon] **State & Territorial Governments, Legislatures**

The power to regulate the rights of fishery is, therefore, derived directly from the Rhode Island Constitution, not merely from a legislative enactment, and such constitutional authorizations are subject to an unquestionably strong and favorable presumption. It is well settled that the Rhode Island General Assembly has plenary power to regulate fisheries as dictated by [R.I. Const. art. I, § 17](#). Additionally, [R.I. Gen. Laws § 20-2.1-1](#) (1956) provides that the General Assembly has plenary authority and responsibility to provide for the conservation of natural resources of the state, including its marine fisheries. The General Assembly has plenary power to regulate the fisheries and as such, can reasonably regulate the number of commercial fishing licenses.

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Real Property Law > Water Rights > Nonconsumptive Uses > Fishing

Real Property Law > Water Rights > Nonconsumptive Uses > Watersports

## **HN13** [blue icon] **Natural Resources & Public Lands, Fish & Wildlife Protection**

Under [R.I. Const. art. I, § 17](#), the rights of fishery, and the privileges of the shore include but are not limited to fishing from the shore, the gathering of seaweed, leaving the shore to swim in the sea and passage along the shore. The "right of fishery" is defined as the general and common right of the citizens to take fish from public waters, such as the sea, great lakes, etc. Such rights are restricted however, by federal and state laws that establish fishing seasons, licensing requirements, catch limits, etc.

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > State & Territorial Governments > Legislatures

## **HN14** [blue icon] **Natural Resources & Public Lands, Fish & Wildlife Protection**

See [R.I. Const. art. I, § 17](#).

Governments > State & Territorial Governments > Legislatures

Governments > State & Territorial Governments > Licenses

## **HN15** [blue icon] **State & Territorial Governments, Legislatures**

[R.I. Gen. Laws § 20-2.1-1\(7\)](#) (1956) sets forth the Rhode Island General Assembly's findings which include a need to make the statutes and programs for marine fisheries management and licensure adaptable to changing conditions and circumstances. The purpose of the statute need only be legitimate, such that even if the fish populations were abundant, it would still be legitimate for the Rhode Island General Assembly to regulate the licensure and entry into the fishing industry. The fundamental purpose of the system of licensure adopted is to preserve, enhance, and allow for any necessary regeneration of the fisheries of the state, for the benefit of the people of the state, as an ecological asset and as a source of food and recreation. [R.I. Gen. Laws § 20-2.1-2](#)

outlines numerous legislative purposes. As such, the regulation of fishing resources need only be reasonably related to a legitimate governmental purpose under the rational basis test, which presumptively favors the constitutionality of the statute.

Governments > State & Territorial Governments > Licenses

**HN16** [  ] **State & Territorial Governments, Licenses**

R.I. Gen. Stat. [§ 20-2.1-13](#) states that the provisions of the licensing statute are necessary for the welfare of the Rhode Island and its inhabitants, and shall be construed liberally so as to effectuate its purposes.

Constitutional Law > Equal Protection > Judicial Review > Standards of Review

**HN17** [  ] **Judicial Review, Standards of Review**

Social and economic legislation that does not employ suspect classifications or impinge on fundamental rights must be upheld when the legislative means are rationally related to a legitimate governmental purpose. Under the rational basis test, the challenged regulation is afforded a strong presumption of validity. The rational basis test is satisfied if any reasonably conceivable set of facts could establish a rational relationship between the challenged regulation and the government's legitimate ends.

Constitutional Law > Equal Protection > Nature & Scope of Protection

Governments > Police Powers

Constitutional Law > Equal Protection > Judicial Review > Standards of Review

Governments > State & Territorial Governments > Licenses

**HN18** [  ] **Equal Protection, Nature & Scope of Protection**

The liberty interest protected by the Fourteenth Amendment includes the right of the individual to engage in the common occupations of life. The constitutional guarantee of a free fishery gives no peculiar rights to those resorting to it for commercial purposes. Preventing a person from obtaining a commercial fishing license to catch the fish with the highest market value simply does not violate that person's constitutionally protected rights. A license is in the nature of a privilege entitling the licensee to do something that he would not be entitled to do without the license. The right of personal liberty and the right to earn a livelihood in any lawful calling and to pursue any lawful trade or vocation is subject to the governmental right to require a license where justified under the police power. Additionally, a classification based on the possession of a sporting license does not burden a suspect group or a fundamental right and is, therefore, subject to review under the rational basis standard.

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > Police Powers

Real Property Law > Water Rights > Nonconsumptive Uses > Fishing

**HN19** [  ] **Natural Resources & Public Lands, Fish & Wildlife Protection**

[R.I. Const. art. I, § 17](#) grants people the freedom to exercise all the rights of fishery but simultaneously grants the government the police power to regulate and control the natural resources for the preservation, regeneration, and restoration of the natural environment.

Constitutional Law > Substantive Due Process > Scope

Governments > State & Territorial Governments > Licenses

Real Property Law > Water Rights > Nonconsumptive Uses > Fishing

#### [HN20](#) [L] Constitutional Law, Substantive Due Process

Nothing in the Rhode Island Constitution grants the people a fundamental right to commercial fishing licenses. Fundamental rights to the fishery exist, but they are not unfettered or unrestricted.

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > State & Territorial Governments > Licenses

#### [HN21](#) [L] Natural Resources & Public Lands, Fish & Wildlife Protection

[R.I. Gen. Laws § 20-2.1-5\(3\)](#) (1956) provides for new licenses such that, in order to obtain the multipurpose or principal effort license a person should first have the basic license for two years. This statute does not make the two year prerequisite recommendation a requirement, but priority is given to those basic license holders. In addition, [§ 20-2.1-5\(3\)](#) states that adding new licensees to the total number of licensees is permissible consistent with the management plan for issuance effective January 1 based on status of resource and economic condition of fishery. [R.I. Gen. Laws § 20-2.1-5\(3\)\(iii\)](#).

Business & Corporate Compliance > ... > Real Property Law > Zoning > Comprehensive Plans

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

#### [HN22](#) [L] Zoning, Comprehensive Plans

In regard to fishing, it may be true that any moratorium that lasts for more than one year should be viewed with special skepticism. However, it cannot possibly be concluded that every delay of over one year is constitutionally unacceptable.

Business & Corporate Compliance > ... > Real Property Law > Zoning > Comprehensive Plans

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > Local Governments > Administrative Boards

Governments > State & Territorial Governments > Licenses

#### [HN23](#) [L] Zoning, Comprehensive Plans

[R.I. Gen. Laws § 20-3-1](#) (1956) creates the Marine Fisheries Council, on which eight private citizens sit, after being appointed by the governor with the advice and consent of the senate. The Council shall serve in an advisory capacity only to the state and agencies of the state regarding marine fisheries issues and to the director of the department of environmental management for the planning, management, and regulation of marine fisheries. [R.I. Gen. Laws § 20-3-2](#). The Council shall advise the director on the development of the regulatory agenda for marine fisheries and shall have the power to initiate rule making by petition as provided for in [R.I. Gen. Laws § 42-35-6](#). [R.I. Gen. Laws § 20-2.1-10](#) provides powers and duties of the Council with regard to licensure. Annually, the Council must report to the governor and various members of the legislature any recommendations it may have for maintaining, improving, or changing laws, regulations, or management programs for marine fisheries. [R.I. Gen. Laws § 20-3-2\(b\)](#). In this way, the Council serves as an oversight committee, which can be petitioned by any interested party. Because of the existence of the Council, a mechanism exists by which private citizens can affect changes to Rhode Island Department of Environmental Management policies and rules, and the ban on new licenses does not necessarily and explicitly endure in perpetuity.

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

#### [HN24](#) **Agency Rulemaking, Rule Application & Interpretation**

See [R.I. Gen. Laws § 42-35-6](#).

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

#### [HN25](#) **Natural Resources & Public Lands, Fish & Wildlife Protection**

The Marine Fisheries Council is required to report annually to the governor, speaker of the house, president of the senate and other legislative members with regard to the advice it gave to state agencies, the response it received to the advice it gave, and any findings it has with regard to the status of the fisheries. [R.I. Gen. Laws § 20-3-2\(b\)](#).

Constitutional Law > Equal Protection > Judicial Review > Standards of Review

#### [HN26](#) **Judicial Review, Standards of Review**

To satisfy the rational basis test, the challenged regulation need not be the best means of promoting a legitimate government interest. A legislative choice is not subject to courtroom fact-finding and may be based on rational speculation unsupported by evidence or empirical data. Moreover, the challenged regulation need not be the least burdensome or the most effective means of accomplishing the regulatory goal. In fact, issues as to the degree, if any, that the limitations will in fact benefit fishery preservation are not relevant to a constitutional analysis.

Environmental Law > Natural Resources & Public Lands > Fish & Wildlife Protection

Governments > State & Territorial Governments > Licenses

#### [HN27](#) **Natural Resources & Public Lands, Fish & Wildlife Protection**

There is no dispute that the conservation of coastal fishery resources is a legitimate governmental objective. [R.I. Gen. Laws § 20-2.1-2](#) explicitly provides for restrictions on the number of license holders as a valid principle for adaptive fisheries management.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## [HN28](#) [L] **Monopolies & Monopolization, Attempts to Monopolize**

The Sherman Act makes no mention of the state as such, and gives no hint that it is intended to restrain state action or official action directed by a state. The Sherman Act's purpose is to suppress combinations to restrain competition and attempts to monopolize by individuals and corporations, which abundantly appears from its legislative history. In the alternative, there is no question that the state or its municipality becoming a participant in a private agreement or combination by others for restraint of trade violates the Sherman Act.

Antitrust & Trade Law > Sherman Act > General Overview

Governments > State & Territorial Governments > General Overview

## [HN29](#) [L] **Antitrust & Trade Law, Sherman Act**

The Sherman Act serves a salutary purpose in ensuring that the marketplace remain reasonably free and open, and in preventing combinations within the private sector from abridging that fundamental freedom in impermissible ways. But, states themselves have historically been accorded safe harbor in these stormy seas. Congress never intended that the Act be employed to handcuff state governments in the pursuit of their traditional regulatory functions.

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Governments > Legislation > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## [HN30](#) [L] **Antitrust & Trade Law, Exemptions & Immunities**

[R.I. Gen. Laws § 6-36-8](#) provides an exemption for state action, stating that nothing contained in it shall be construed to apply to activities or arrangements approved by any regulatory body or officer acting under statutory authority of this state or of the United States. The statute also provides that the exemptions shall be liberally construed in harmony with federal statutes and ruling judicial interpretations of the United States courts. [R.I. Gen. Laws § 6-36-8](#). The Rhode Island Department of Environmental Management is a regulatory agency that exists by legislative grant of power, and, as such, its actions in regulating the fishing industry are presumed valid and exempt from attack under [antitrust law](#).

**Judges:** INDEGLIA, J.

**Opinion by:** INDEGLIA

## **Opinion**

## **DECISION**

**INDEGLIA, J.** Before this Court is an appeal from a decision of the Rhode Island Department of Environmental Management (D.E.M.), denying Appellant Steven Riley a commercial fishing license with certain finfish and shellfish endorsements. Appellant has also presented a motion for declaratory relief requesting that this Court declare [G.L. 1956 § 20-2.1-5\(1\)\(ii\)](#) and Rule 7 of the Rules and Regulations Governing the Management of Marine Fisheries (Rule 7) unconstitutional, and order that Appellant be given the requested multi-purpose fishing license. Jurisdiction is pursuant to [G.L. 1956 § 42-35-15](#) and [G.L. 1956 § 9-30-1](#).

## **FACTS AND TRAVEL**

Appellant Steven Riley (Riley) sought and was denied a commercial fishing license. Riley applied for a principal effort commercial fishing license with shellfish/quahog and restricted finfish endorsements under [G.L. 1956 § 20-2.1-5](#). The Rhode Island [\*2] Department of Environmental Management (D.E.M.) denied his request based on the statutory language of [§ 20-2.1-5](#) that allowed only those who had such licenses as of December 31, 2002 (the end of the previous year) to obtain the license again, essentially prohibiting any new applicants from receiving said license.<sup>1</sup> [\*3] Riley was granted a commercial fishing license with lobster, non-quahog shellfish, and non-restricted finfish endorsements. Riley admitted that he had not possessed any commercial fishing licenses since the early 1970s. Additionally, Rule 7 states that there were no new principal effort licenses with quahog or restricted finfish endorsements available in 2003. Riley received the initial denial on February 27, 2003 and on March 9, 2003 timely filed a request for reconsideration with the Commercial Fishing License Review Board.<sup>2</sup>

On May 21, 2003, Riley timely filed a notice of appeal to the Administration Adjudication Division (A.A.D.) requesting a hearing; however, on or about June 6, 2003, the A.A.D. remanded the matter to the Commercial Fishing License Review Board for a hearing, which took place on July 21, 2003. On August 2, 2003, in a letter which stated that Riley had failed to meet the standard set for the in § 20-2.1-12 (b), Riley was denied at the Commercial Fishing License Review Board as well. On or about August 20, 2003, the D.E.M. gave its final denial to Riley.

On January 21, 2004, the parties presented oral argument before Chief Hearing Officer Kathleen Lanphear, who granted D.E.M.'s motion for summary judgment on January 26, 2004. Riley then filed the instant appeal in this Court, arguing that he has a fundamental right to choose his occupation [\*4] and, as such, cannot be denied the commercial fishing license, and that the statute violates equal protection and due process principles. He further argued that the Hearing Officer's decision was arbitrary and capricious and finally that the statute and Rule 7 violates the [Sherman Act](#). The Rhode Island Attorney General's Office informed Riley on March 10, 2004 that it would not intervene unless the Court felt such an intervention to brief constitutional issues would be helpful. However, the Attorney General's Office reserved the right to reconsider and intervene upon appeal.<sup>3</sup> A decision is herein rendered.

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<sup>1</sup> [Section 20-2.1-5\(1\)\(ii\)](#) provides that [HN1](#) [↑] "duly licensed persons in a fishery as of December 31 of the immediately preceding year, shall be eligible to obtain a principal effort license for the fishery sector for which they were licensed on December 31 of the immediately preceding year, which principal effort license shall allow its holder to fish in a fishery sector at the full harvest and gear levels."

<sup>2</sup> Prior to receiving any decision of the Commercial Fishing License Review Board, Riley was notified on April 22, 2003 that said Review Board had not yet been fully appointed. Riley asserts that the Board had, in fact, been appointed on April 16, 2003.

<sup>3</sup> This Court notes that the opinion of the Attorney General is not needed based on this Court's decision herein.

## **STANDARDS OF REVIEW**

### **Declaratory Judgment**

**HN2** [↑] The Uniform Declaratory Judgments Act (Declaratory Act), [G.L. 1956 § 9-30-1 et seq.](#), grants the Superior Court "power to declare rights, status, and other legal relations whether or not relief is or could [\*5] be claimed." The Declaratory Act also provides that the Superior Court may grant additional affirmative relief "based on the declaratory judgment 'whenever necessary or proper' provided subsequent 'supplementary proceedings' are brought pursuant thereto." [Capital Properties, Inc. v. State](#), 749 A.2d 1069, 1080 (R.I. 1999) (citing §§ [9-30-8](#), [9-30-12](#); [Sousa v. Langlois](#), 97 R.I. 196, 199, 196 A.2d 838, 841 (1964)). Section 9-30-2 provides in part, that

**HN3** [↑] "any person . . . whose rights, status, or other legal relations are affected by a statute, municipal ordinance, contract, or franchise, may have determined any question of construction or validity arising under the instrument, statute, ordinance, contract, or franchise and obtain a declaration of rights, status, or other legal relations thereunder."

**HN4** [↑] The purpose of the Declaratory Act is "to facilitate the termination of controversies." [Capital Properties, Inc.](#), 749 A.2d at 1080. The decision to issue a declaratory judgment lies within the trial justice's broad discretion. [Cruz v. Wausau Ins. Co.](#), 866 A.2d 1237, 1240 (R.I. 2005); [Sullivan v. Chafee](#), 703 A.2d 748, 751 (R.I. 1997) [\*6] (citing [Woonsocket Teachers' Guild Local Union 951 v. Woonsocket Sch. Comm.](#), 694 A.2d 727, 729 (R.I. 1997)). Section 9-30-12 provides that the Declaratory Act should be "liberally construed and administered." See also [Taylor v. Marshall](#), 119 R.I. 171, 180, 376 A.2d 712, 716-17 (1977) (stating existence of alternate methods of relief, including administrative, do not preclude declaratory judgment).

### **Administrative Appeal**

**HN5** [↑] Judicial review of contested agency decisions is governed by [G.L. 1956 § 42-35-15\(g\)](#) which provides:

**HN6** [↑] "The court shall not substitute its judgment for that of the agency as to the weight of the evidence on questions of fact. The court may affirm the decision of the agency or remand the case for further proceedings, or it may reverse or modify the decision if substantial rights of the appellant have been prejudiced because the administrative findings, inferences, conclusions, or decisions are:

- (1) In violation of constitutional or statutory provisions;
- (2) In excess of the statutory authority of the agency;
- (3) Made upon unlawful procedure;
- (4) Affected by other error of law;

(5) [\*7] Clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record; or  
(6) Arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion."

**HN7** [↑] The reviewing court is precluded from substituting its judgment for that of the agency regarding witness credibility or the weight of evidence concerning questions of fact. [Costa v. Registry of Motor Vehicles](#), 543 A.2d 1307, 1309 (R.I. 1988); [Carmody v. Rhode Island Conflict of Interest Comm'n](#), 509 A.2d 453, 458 (R.I. 1986). This Court's review is limited to determining whether substantial evidence exists to support the agency's decision. [Newport Shipyard v. Rhode Island Comm'n for Human Rights](#), 484 A.2d 893 (R.I. 1984). "Substantial evidence . . . means such relevant evidence that a reasonable mind might accept as adequate to support a conclusion, and means an amount more than a scintilla but less than a preponderance." [Caswell v. George Sherman Sand & Gravel Co., Inc.](#), 424 A.2d 646, 647 (R.I. 1981) (citing [Apostolou v. Genovesi](#), 120 R.I. 501, 508, 388 A.2d 821, 824-25 (1978)). [\*8] This Court will "reverse factual conclusions of administrative agencies only when they are totally devoid of competent evidentiary support in the record." [Milardo v. Coastal Resources Management Council](#), 434 A.2d 266, 272 (R.I. 1981). In deference to the agency, this Court "must uphold the agency's conclusions when they

are supported by any legally competent evidence in the record." *Rocha v. State Public Utilities Comm'n*, 694 A.2d 722, 725 (R.I. 1997) (quoting *Rhode Island Public Telecommunications Authority v. Rhode Island Labor Relations Bd.*, 650 A.2d 479, 485 (R.I. 1994)).

**HN8** When an agency promulgates regulations pursuant to specific authority granted by the General Assembly, "the regulations are legislative rules that carry the force and effect of law and enjoy a presumption of validity." *Parkway Towers Assoc. v. Godfrey*, 688 A.2d 1289, 1293 (R.I. 1997); see also *Newport Court Club Assocs. v. Town Council of Town of Middletown*, 800 A.2d 405, 409 (R.I. 2002) (quoting *Rhode Island Depositors Economic Protection Corp. v. Brown*, 659 A.2d 95, 100 (R.I. 1995)). "To determine whether [\*9] a rule is to be classified as legislative or interpretive, one must consider the power assigned to the administrative agency. If a statute expressly delegates power to interpret and define certain legislation to an agency, regulations promulgated pursuant to that power are legislative rules having the force of law." *Lerner v. Gill*, 463 A.2d 1352, 1358 (R.I. 1983) (citing *Batterton v. Francis*, 432 U.S. 416, 53 L. Ed. 2d 448, 97 S. Ct. 2399 (1977)); see also *In re Advisory Opinion to the Governor*, 732 A.2d 55, 69 (R.I. 1999). "Legislative rules are valid if they are within the power granted by the General Assembly, are issued pursuant to proper procedure, and are reasonable as a matter of due process." *Id. at 1358*; see also, *Parkway Towers*, 688 A.2d at 1293.

**HN9** If the regulation is challenged on constitutional due process or equal protection grounds and does not infringe upon a fundamental constitutional right or implicates a suspect class, the regulation must be rationally related to furthering a legitimate state interest in order to be upheld. *Newport Court Club Assocs.*, 800 A.2d at 415; *Rhode Island Depositors Economic Protection Corp. v. Brown*, 659 A.2d 95, 100 (R.I. 1995); [\*10] *In re Advisory Opinion to the House of Representatives*, 519 A.2d 578, 583 (1987). Only if a regulation is "without any reasonable basis and . . . purely arbitrary" will it be found unconstitutional under this standard. *Rhode Island Depositors Econ. Prot. Corp.*, 659 A.2d at 100.

## ANALYSIS

### CONSTITUTIONALITY OF THE STATUTE AND RULE

At the outset, Riley argues that he has a fundamental right to pursue a livelihood, which is protected by his right to life, liberty, and property under the *Equal Protection* and *Due Process Clauses* of the *Fifth* and *Fourteenth Amendments to the United States Constitution*. Riley further posits that even if no fundamental right to pursue a livelihood exists, he would still prevail constitutionally under a rational basis test on the grounds that the statute has irrationally created two classes: those with licenses as of December 31, 2002, and those without licenses as of that date. Riley alleges that treating similarly situated citizens differently in this allegedly arbitrary manner violates equal protection and due process rights. Riley also maintains that § 20-2.1-5 is unconstitutional because it violates [\*11] the state police powers. Riley also contends that § 20-2.1-5 and Rule 7 exceed the enabling statute's (G.L. 1956 § 20-3-2) authority.

D.E.M. responds by arguing that § 20-2.1-1 et seq. and Rule 7 are constitutional because legislative provisions enjoy a presumption of validity and the Appellant must prove unconstitutionality beyond a reasonable doubt, which he has not done. D.E.M. notes that the General Assembly has plenary power to regulate the fishing industry. D.E.M. also argues that the statute and rule do not violate equal protection because not all legislative classifications (in this case license and non-license holders) are constitutionally impermissible. D.E.M. contends that no fundamental right is involved and therefore, minimal scrutiny must be applied, under which the statute and rule withstand constitutional attack. Additionally, D.E.M. maintains that the statute neither violates substantive due process rights because regulation of commercial fishing licenses is not the type of state action that "shocks the conscience," nor has Appellant shown that a fundamental right been violated. Lastly, D.E.M. opines that the basis of Riley's present action [\*12] is merely his desire to fish the seafood stock that fetches higher market prices, when in actuality, he received a license to fish for other species and categories, just not those that bring the highest prices.

Recently the Rhode Island Supreme Court examined constitutional issues involving fishing statutes in *Cherenzia v. Lynch*, 847 A.2d 818 (R.I. 2004). In *Cherenzia*, a group of commercial fishermen argued that a statute barring use

of SCUBA gear to harvest shellfish from four coastal ponds violated their substantive due process and equal protection rights. *Id. at 820*. The fishermen argued the statute violated their fundamental rights of fishery and discriminated against a single class of fishermen -- those who use SCUBA gear -- and as such, strict scrutiny applied. *Id. at 821-22*. The State argued that the statute enjoyed a presumption of validity, the General Assembly had plenary power to regulate the fishing industry, and no fundamental right was implicated; thus only minimal scrutiny need be applied. *Id. at 822*.

Our Supreme Court held that the provisions of the statute in question that prohibited use of SCUBA [\*13] gear in harvesting shellfish did not "infringe on a fundamental constitutional right, nor [did] they create a suspect classification." *Cherenzia, 847 A.2d at 823*. The Supreme Court stated that [HN10](#) the "scope of the fundamental right protected in *art. I, sec. 17*, is that all the inhabitants of the state 'shall continue to enjoy and freely exercise' equal access to the state's fishery resources." *Id.* "This 'gives the benefits of fishery to all the people in equal measure.'" *Id.* (quoting *Opinion of the Senate, 87 R.I. 37 at 38, 137 A.2d 525 at 525-26*). The Supreme Court concluded that "the very nature and scope of the right to fish that *art. I, sec. 17* protects is not unqualified; rather, it anticipates that reasonable legislative regulation is necessary to properly effectuate that right." *Id. at 824* (referencing *State v. Cozzens, 2 R.I. 561, 563 (1850)*). "If a statute or regulation contained restrictions that infringed upon the fundamental right of the inhabitants of the state to have **equal access** to the "rights of fishery," then such a regulation or law would be subject to strict-scrutiny analysis." *Id.* (Emphasis added. [\*14] ) The Court also noted that such fishing was "not merely for the profit and emolument of the fishermen engaged in the business." *Id.* (quoting *Opinion to the Senate, 87 R.I. 37, 38-39, 137 A.2d 525, 526 (1958)*). In addressing the substantive due process claim, our Supreme Court held that "the burden was on [the plaintiffs] to prove beyond a reasonable doubt that the provisions of [the statute] lacked a substantial relation to the public health, safety, and welfare, or to the Legislature's constitutionally prescribed duty to protect and conserve the fishery resources of the state." *Id. at 826* (citing *Brunelle v. Town of South Kingstown, 700 A.2d 1075, 1084 (R.I. 1997)*). The Court found there was no violation of equal protection or due process rights and the statute was constitutional. *Id. at 826-27*.

Our Supreme Court has further recognized that [HN11](#) "within the constitution's broad grant of legislative power to the General Assembly lies its plenary power to regulate the fishing resources of the state." *Id. at 822* (citing *Opinion to the Senate, 87 R.I. 37, 40, 137 A.2d 525, 526 (1958)* and other cases). Furthermore, it noted [\*15] that "the whole subject of fisheries . . . [is] under the fostering care of the General Assembly." *Id.* (citing *State v. Kofines, 33 R.I. 211, 239, 80 A. 432, 443 (1911)*). With regard to the fisherman's claim of equal protection violations because of the alleged discrimination against the "class" of fisherman using SCUBA gear, the Court clarified that "not all legislative classifications, however, are impermissible." *Id. at 823* (citing *Kennedy v. State, 654 A.2d 708, 712 (R.I. 1995)*). The Court reiterated that "the Legislature enjoys "a wide scope of discretion in enacting laws that affect some classes of citizens differently from others." *Id.* (quoting *Boucher v. Sayeed, 459 A.2d 87, 91 (R.I. 1983)*). Strict scrutiny applies when a fundamental right has been impinged upon, or a suspect classification arises. *Id.* Our Supreme Court, "will employ a 'minimal-scrutiny' analysis, however, when assessing economic or social regulations that neither infringe on a fundamental right, nor result in a classification that is 'suspect.'" <sup>4</sup> *Id.* (referencing *Kennedy, 654 A.2d at 712*). The Court also recognized [\*16] that the United States Supreme Court has held that "the scope of the liberty interests protected by the *Fourteenth Amendment*" includes "the right of the individual to engage in the common occupations of life, and 'generally to enjoy those privileges long recognized . . . as essential to the orderly pursuit of happiness by free men.'" *Id.* (citing *Lynch v. Gontarz, 120 R.I. 149, 156, 386 A.2d 184, 188 (1978)*).

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<sup>4</sup> Other jurisdictions have held that regulations involving commercial fishing are properly reviewed under rational basis scrutiny. "Fishing, whether commercial or recreational, is not a fundamental right and those engaged in these activities are not a suspect class." *Vickers v. Egbert, 359 F. Supp. 2d 1358, 2005 U.S. Dist. LEXIS 3333, \*10-12 (S.D. Fla. 2005)* (citing *Sisk v. Texas Parks & Wildlife Dep't, 644 F.2d 1056, 1058 n.5 (5th Cir. 1981); United Boatmen of NJ v. Mosbacher, 1992 U.S. Dist. LEXIS 664, \*26-27 (D.N.J. 1992); LaBauve v. Louisiana Wildlife & Fisheries Comm'n, 444 F. Supp. 1370, 1382 (E.D. La. 1978); Gilbert v. Dep't of Fish & Game, Bd. of Fisheries, 803 P.2d 391, 399 (Ak. 1990); California Gillnetters Ass'n v. Dep't of Fish & Game, 39 Cal. App. 4th 1145, 1154-55, 46 Cal. Rptr. 2d 338, 343 (Cal. Ct. App. 1995); Lane v. Chiles, 698 So. 2d 260, 263 (Fla. 1997); State v. Weaver, 805 So. 2d 166, 170 (La. 2002)*).

[\*17] In the case at bar, Riley's fundamental "rights of fishery" have not been violated because he was granted a commercial license and maintains the right to fish recreationally.<sup>5</sup> The *Cherenzia* case expressly held that said fundamental rights of fishery deal with equal access to the fish resources, subject however, to reasonable state regulation. [847 A.2d at 824](#). [HN12](#)<sup>↑</sup> The power to regulate the rights of fishery is, therefore, derived directly from the Rhode Island Constitution, not merely from a legislative enactment, and such constitutional authorizations are subject to an unquestionably strong and favorable presumption.<sup>6</sup> [\*19] It is well settled that the General Assembly has plenary power to regulate fisheries as dictated by the [Rhode Island Constitution in Article 1, Section 17. Id. at 822-23](#). Additionally, § 20-2.1-1 provides that the General Assembly has "plenary authority and responsibility . . . to provide for the conservation of natural resources of the state, including its marine fisheries." In this matter, the D.E.M. cited the need to regulate and preserve the fish populations while not shortening the season or causing "overcrowding" in the fishing [\*18] industry.<sup>7</sup> Though Riley argues that the fish populations are not in danger of being depleted, this belief is not the deciding factor. The General Assembly has plenary power to regulate the fisheries and as such, can reasonably regulate the number of commercial fishing licenses.

[HN15](#)<sup>↑</sup> Section 20-2.1-1 sets forth the General Assembly's findings which include a need to make the "statutes and programs for marine fisheries management and licensure . . . adaptable to changing conditions and circumstances." Section 20-2.1-1(7). The purpose of the statute need only be legitimate, such that even if the fish populations were abundant, it would still be legitimate for the General Assembly to regulate the licensure and entry into the fishing industry.<sup>8</sup> The fundamental [\*20] purpose of the system of licensure adopted is to "preserve, enhance, and allow for any necessary regeneration of the fisheries of the state, for the benefit of the people of the state, as an ecological asset and as a source of food and recreation." [Section 20-2.1-2](#) (outlining numerous legislative purposes). As such, the regulation of fishing resources need only be reasonably related to a legitimate governmental purpose under the rational basis test, which presumptively favors the constitutionality of the statute.<sup>9</sup> [Cherenzia, 847 A.2d at 825](#) (citing [Kennedy v. State, 654 A.2d 708, 712-13 \(R.I. 1995\)](#)).

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<sup>5</sup> [HN13](#)<sup>↑</sup> Under the [Rhode Island Constitution, art. 1, sec. 17](#), "the rights of fishery, and the privileges of the shore . . . include but [are] not limited to fishing from the shore, the gathering of seaweed, leaving the shore to swim in the sea and passage along the shore." Black's Law Dictionary defines the "right of fishery" as "the general and common right of the citizens to take fish from public waters, such as the sea, great lakes, etc. [Shively v. Bowlby, 152 U.S. 1, 14 S. Ct. 548, 38 L. Ed. 331](#). Such rights are restricted however, by federal and state laws that establish fishing seasons, licensing requirements, catch limits, etc." Black's Law Dictionary 637 (6th ed. 1990).

<sup>6</sup> The Rhode Island Constitution provides that:

[HN14](#)<sup>↑</sup> "it shall be the duty of the general assembly to provide for the conservation of the air, land, water, plant, animal, mineral and other natural resources of the state, and to adopt all means necessary and proper by law to protect the natural environment of the people of the state by providing adequate resource planning for the control and regulation of the use of the natural resources of the state and for the preservation, regeneration and restoration of the natural environment of the state." [R.I. Const. art. 1, sec. 17](#).

<sup>7</sup> This Court agrees that a shortened fishing season would be problematic both for the commercial fishing industry and the economy in Rhode Island. Without comprehensive regulation of the fishing industry through licensing, etc. the number of parties fishing would likely increase and catch quotas would be met sooner, resulting in a significantly abbreviated fishing season. Though Appellant argues the fishing industry could regulate itself, the reality of a "Tragedy of the Commons" type instructs us otherwise. Too many participants lead to premature depletion of the resource, in this case, fish and shellfish species.

<sup>8</sup> [HN16](#)<sup>↑</sup> [Section 20-2.1-13](#) states that the provisions of the licensing statute are "necessary for the welfare of the state and its inhabitants, [and] shall be construed liberally so as to effectuate its purposes."

<sup>9</sup> [HN17](#)<sup>↑</sup> "Social and economic legislation . . . that does not employ suspect classifications or impinge on fundamental rights must be upheld . . . when the legislative means are rationally related to a legitimate governmental purpose." [Hodel v. Indiana, 452 U.S. 314, 331, 69 L. Ed. 2d 40, 101 S. Ct. 2376 \(1981\)](#) cited in [Medeiros v. Atlantic States Marine Fisheries Comm'n, 327 F. Supp. 2d 145, 151 \(D. R.I. 2004\)](#). "Under the rational basis test, the challenged regulation is afforded a 'strong presumption of validity.'" [Medeiros, 327 F. Supp. 2d at 151](#) (quoting [F.C.C. v. Beach Communications, Inc., 508 U.S. 307, 314, 124 L. Ed. 2d](#)

[\*21] With respect to the subject regulation, Riley attempts to trigger strict scrutiny thereof, by alleging a violation of his fundamental right to engage in the occupation of his choosing. However, he has not presented to this Court any compelling case law that recognizes such a fundamental right. Our Supreme Court has acknowledged that [HN18](#) [↑] the liberty interest protected by the [Fourteenth Amendment](#) includes "the right of the individual to engage in the common occupations of life . . ." [847 A.2d at 823](#) (quoting [Lynch v. Gontarz](#), [120 R.I. 149, 156, 386 A.2d 184, 188 \(1978\)](#)). Even if one were to consider fishing a "common occupation," it would be of little significance because Riley was granted a commercial fishing license, albeit a basic one. Our Supreme Court "has recognized that the constitutional guarantee of a ? free fishery ... gives no peculiar rights to those resorting to it for commercial purposes." [Opinion to the Senate](#), [87 R.I. 37, 38, 137 A.2d 525, 526 \(1958\)](#). Riley was not prevented from entering the field of commercial fishermen, but rather was simply denied an expanded license that allowed him to fish for certain types of fish, [\*22] which may be more profitable. Preventing a person from obtaining a commercial fishing license to catch the fish with the highest market value simply does not violate that person's constitutionally protected rights. "A license is in the nature of a privilege . . . entitling the licensee to do something that he would not be entitled to do without the license." [51 Am. Jur. 2d Licenses & Permits § 1](#) (2000). "The right of personal liberty and the right to earn a livelihood in any lawful calling and to pursue any lawful trade or vocation is subject to the governmental right to require a license where justified under the police power." [51 Am. Jur. 2d Licenses & Permits § 16](#) (2000). Additionally, "[a] classification based on the possession of a sporting license does not burden a suspect group or a fundamental right and is, therefore, subject to review under the rational basis standard." [Animal Legal Defense Fund, Inc. v. Fisheries & Wildlife Bd.](#), [416 Mass. 635, 624 N.E.2d 556, 560 \(Mass. 1993\)](#). As such, Riley's right to engage in the common occupations of life has not been infringed [\*23] upon, and the standard of review remains a rational basis.

[HN19](#) [↑] [Article 1, Section 17 of the Rhode Island Constitution](#) grants people the freedom to "exercise all the rights of fishery" but simultaneously grants the government the police power to regulate and control the natural resources "for the preservation, regeneration, and restoration of the natural environment." [R.I. Const. art. 1, sec. 17](#). Indeed, said section states that "it shall be the duty of the general assembly to provide for the conservation of the air, land, water, plant, animal, mineral and other natural resources of the state, and to adopt all means necessary and proper by law." *Id.* [HN20](#) [↑] Nothing in the Rhode Island Constitution grants the people a fundamental right to commercial fishing licenses. The [Cherenzia](#) case affirms that the fundamental rights to the fishery exist, but they are not unfettered or unrestricted. [847 A.2d at 824](#).

[HN21](#) [↑] [Section 20-2.1-5\(3\)](#) provides for new licenses such that, in order to obtain the multipurpose or principal effort license that Riley sought, a person should first have the basic license for two years. This statute does not make the two year prerequisite recommendation a requirement, [\*24] but priority is given to those basic license holders. In addition, [§ 20-2.1-5\(3\)](#) states that adding new licensees to the total number of licensees is permissible "consistent with the management plan for issuance effective January 1 . . . based on status of resource and economic condition of fishery." [Section 20-2.1-5\(3\)\(iii\)](#). Riley received a basic license, and perhaps after 2 years, he will be granted a license with greater privileges. Indeed, D.E.M. does issue principal effort licenses to new entrants after old licenses are traded in or retired.<sup>10</sup> Even if the D.E.M. decided not to issue additional new permits, instead choosing to preserve the status quo insofar as the number of permits issued, then such an action is permitted under the police power statute and presumed valid.

[\*25] Appellant argues that the statutory ban on issuing new licenses is unconstitutional. Such a prohibition on the issuance of new licenses under [G.L. 1956 § 20-2.1-5](#) and Rule 7 amounts to what is essentially a moratorium on new principal effort and multi-purpose fishing licenses. Neither the statute nor the rule specifically states when such

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[211, 113 S. Ct. 2096 \(1993\)](#)). "The rational basis test is satisfied 'if any reasonably conceivable set of facts could establish a rational relationship between [the challenged regulation] and the government's legitimate ends.'" *Id.* (citing [Montalvo-Huertas v. Rivera-Cruz](#), [885 F.2d 971, 978 \(1st Cir. 1989\)](#)).

<sup>10</sup> At oral argument, D.E.M. stated that thirteen licenses were issued to new entrants consistent with established priority methodology and D.E.M.'s exit/entrance procedures. See [G.L. 1956 § 20-2.1-5\(3\)](#); see also G.L. 1956 § 20-2.1-9(4) (setting forth matters considered in establishing license programs under statute).

a moratorium would end, but rather, as drafted could prohibit new license applicants from entering the industry indefinitely. Recently, the Rhode Island Supreme Court held that a three year moratorium that prevented a company from entering the high speed ferry business was valid under the relevant statute granting regulatory power to the agency. *Interstate Navigation Co. v. Div. of Pub. Utils. and Carriers of the State of Rhode Island*, 824 A.2d 1282 (R.I. 2003). The United States Supreme Court has also examined moratoriums in *Tahoe-Sierra Pres. Council, Inc. v. Tahoe Reg'l Planning Agency*, 535 U.S. 302, 152 L. Ed. 2d 517, 122 S. Ct. 1465 (2002). In *Tahoe-Sierra*, the U.S. Supreme Court stated [HN22](#) "it may be true that any moratorium that lasts for more than one year should be viewed with special [\*26] skepticism." [535 U.S. at 341](#). However, the Court also said that it "could not possibly conclude that every delay of over one year is constitutionally unacceptable." [Id. at 341-42](#) (acknowledging some moratoria last more than one year which interfere with expectations). In fact, "moratoriums have been approved when they form a part of a comprehensive plan to remedy a problem situation." [Q.C. Constr. Co., Inc. v. Gallo](#), 649 F. Supp. 1331, 1337 (D. R.I. 1986) (citing numerous cases).

In this case, while the moratorium on new principal effort licenses may be able to last indefinitely, there are mechanisms to amend or reevaluate such a ban with respect to its relation to a comprehensive regulatory scheme. [See id.](#) (stating moratoriums valid when part of plan to remedy problems); [see also Westwood Forest Estates, Inc. v. Village of So. Nyack](#), 23 N.Y.2d 424, 244 N.E.2d 700, 702, 297 N.Y.S.2d 129 (N.Y. 1969) (holding zoning moratorium on new construction improper where not in furtherance of comprehensive plan). [HN23](#) [Section 20-3-1](#) creates the Marine Fisheries Council (Council), on which eight private citizens sit, after being appointed by the governor [\*27] with the advice and consent of the senate.<sup>11</sup> [G.L. 1956 § 20-3-1](#). The Council "shall serve in an advisory capacity only to the state and agencies of the state regarding marine fisheries issues and to the director of the department of environmental management . . . for the planning, management, and regulation of marine fisheries . . ." [Section 20-3-2](#). "The Council shall advise the director on the development of the regulatory agenda for marine fisheries and shall have the power to initiate rule making by petition as provided for in [§ 42-35-6](#)."<sup>12</sup> [Section 20-2-1-10](#) (providing powers and duties of Council with regard to licensure). Annually, the Council must report to the governor and various members of the legislature "any recommendations it may have for maintaining, improving, or changing laws, regulations, or management programs for marine fisheries."<sup>13</sup> Section 20-3-2(b). In this way, the Council serves as an oversight committee, which can be petitioned by any interested party, presumably including someone similarly situated to Riley. Because of the existence of the Council, a mechanism exists by which private citizens can affect changes to D.E.M. policies [\*28] and rules, and the ban on new licenses does not necessarily and explicitly endure in perpetuity.

[\*29] Additionally, though the moratorium on new licenses may not be the best possible method of reaching the D.E.M.'s stated goals, under a rational basis review, it need not be. In fact, [HN26](#) "to satisfy the rational basis test, the challenged regulation need not be 'the best means of promoting a legitimate government interest.'" *Medeiros v. Atlantic States Marine Fisheries Comm'n*, 327 F. Supp. 2d 145, 151 (D. R.I. 2004) (quoting *New York State Trawlers Ass'n v. Jorling*, 16 F.3d 1303, 1309 (2d Cir. 1994)) (emphasis in original). "[A] legislative choice is not subject to courtroom fact-finding and may be based on rational speculation unsupported by evidence or empirical data." [Id.](#) (quoting *F.C.C. v. Beach Communications, Inc.*, 508 U.S. 307, 314, 124 L. Ed. 2d 211, 113 S. Ct. 2096 (1993)). "Moreover, the challenged regulation need not be the least burdensome or the most effective means of accomplishing the regulatory goal." [Id.](#) (citing *Starlight Sugar, Inc. v. Soto*, 253 F.3d 137, 146 (1st Cir.

<sup>11</sup> The Council is chaired by the director of the D.E.M. or whomever the director may designate. [G.L. 1956 § 20-3-1](#). The eight private citizen members of the Council "shall be chosen from among those with skill, knowledge, and experience in the commercial fishing industry, the sportfishing industry, and in the conservation and management of fisheries resources . . ." [Id.](#)

<sup>12</sup> [Section 42-35-6 of the Rhode Island General Laws](#) provides that [HN24](#) "any interested person may petition an agency requesting the promulgation, amendment, or repeal of any rule." In this way, any interested person could petition the Council with a challenge or amendment to Rule 7.

<sup>13</sup> Additionally, [HN25](#) the Council is required to report annually to the governor, speaker of the house, president of the senate and other legislative members with regard to the advice it gave to state agencies, the response it received to the advice it gave, and any findings it has with regard to the status of the fisheries. Section 20-3-2(b).

2001)). In fact, "issues as to the degree, if any, that the [] limitations will in fact benefit fishery preservation are not [\*30] relevant" to a constitutional analysis. Id. at 152. In this case, the ban on new licenses in G.L. 1956 § 20-2.1-5 and Rule 7 may not be the best or most effective method of achieving D.E.M.'s objectives as part of its comprehensive regulatory plan for the various fisheries. Still, it is nonetheless permissible because it is reasonable and rationally related to the government's legitimate purpose of regulating Rhode Island's natural fish resources.<sup>14</sup>

[\*31] Riley carries the burden of proving the statute and rule are unconstitutional beyond a reasonable doubt, and has failed to do so. Additionally, Riley has not persuaded this Court that either a fundamental right or a suspect class is involved. Thus, Riley's arguments fail to trigger heightened constitutional scrutiny. Additionally, the legislative classifications are permissible, and in this case, the regulation of the number of fisherman with permits is reasonable in accomplishing stated goals explicitly set forth in the statute, G.L. 1956 § 20-2.1-2. Accordingly, this Court declares that the General Assembly has the power to regulate in this area and in this manner.

### **VIOLATION OF THE SHERMAN ACT**

Riley further argues that said statute and Rule 7 are preempted by antitrust laws and § 1 of the Sherman Act as a restraint on trade. Riley asserts that D.E.M. has created a monopoly in the existing licensees, which violates the Sherman Act. D.E.M. argues that the statute and rule are not preempted by antitrust laws and § 1 of the Sherman Act because the statute and rule were established pursuant to a valid grant of legislative power, which exempts [\*32] them from the Sherman Act.

At the outset, Riley has presented no case law to override D.E.M.'s cited authority as to applicability, instead relying on the arguments of how the D.E.M.'s actions allegedly violate the Act by essentially creating a monopoly in the fishing industry with respect to certain finfish licenses. On the other hand, D.E.M. persuasively asserts the inapplicability of the Sherman Act based on the United States Supreme Court's decision in Parker v. Brown, 317 U.S. 341, 87 L. Ed. 315, 63 S. Ct. 307 (1943) and the Rhode Island Federal District Court's decision in Healey v. Bendick, et al., 628 F. Supp. 681 (D. R.I. 1986).

In Parker, the United States Supreme Court held that HN28 [↑] the Sherman Act made "no mention of the state as such, and [gave] no hint that it was intended to restrain state action or official action directed by a state." 317 U.S. at 351. The Court continued, stating the Sherman Act's "purpose was to suppress combinations to restrain competition and attempts to monopolize by individuals and corporations, [which] abundantly appears from its legislative history." Id. The Court also noted, in the alternative, that [\*33] there was "no question [that] the state or its municipality becoming a participant in a private agreement or combination by others for restraint of trade" violates the Sherman Act. Id. at 351-52 (referencing Union Pacific R. Co. v. United States, 313 U.S. 450, 85 L. Ed. 1453, 61 S. Ct. 1064 (1941)). The Supreme Court concluded that "the state in adopting and enforcing the [] program made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit." Id. at 352 (citing Olsen v. Smith, 195 U.S. 332, 344-45, 49 L. Ed. 224, 25 S. Ct. 52 (1904)).

In Healey, the Rhode Island Federal District Court followed the same reasoning of the Parker case. The Healey case involved the Rhode Island Marine Fisheries Council (M.F.C.). 628 F. Supp. at 681. The court stated that "inasmuch as the MFC's edicts were within the sphere of the authority delegated to that body by the Rhode Island General Assembly, the conduct that [plaintiff] castigates was undeniably the conduct of the state itself, [\*34] and

<sup>14</sup> HN27 [↑] "There is no dispute that the conservation of coastal [] fishery resources is a legitimate governmental objective." Medeiros, 327 F. Supp. 2d at 151 (citing New York State Trawlers Ass'n v. Jorling, 16 F.3d 1303, 1309 (2d Cir. 1994)). Section 20-2.1-2 explicitly provides for "restrictions on the number of license holders" as a valid principle for adaptive fisheries management. For findings of the General Assembly and other purposes of the statute in regulating commercial fishing licensure see G.L. 1956 § 20-2.1-1 and G.L. 1956 § 20-2.1-2. It is also noteworthy that the General Assembly enacted a moratorium on commercial fishing licenses from 1995 until 1998 and again from 2000 until 2003, during both of which, only renewal licenses were available.

therefore immune from Sherman Act charges under the "state action" principle of Parker." *Id. at 688*. The court went on to say:

**HN29** [↑] "The Sherman Act serves a salutary purpose in ensuring that the marketplace remain reasonably free and open, and in preventing combinations within the private sector from abridging that fundamental freedom in impermissible ways. But, states themselves have historically been accorded safe harbor in these stormy seas. Congress never intended that the Act be employed to handcuff state governments in the pursuit of their traditional regulatory functions. Both the basic tenets of federalism and the compelling force of precedent require that [plaintiff's] Sherman Act claim, which is brought solely against state actors, be dismissed." *Id. at 689*.

Additionally, the Sherman Act's Rhode Island state law counterpart can be found at G.L. 1956 § 6-36-1 et seq. **HN30** [↑] Section 6-36-8 provides an exemption for state action, stating that "nothing contained in this chapter shall be construed to apply to activities or arrangements approved by any regulatory body or officer acting under statutory authority [\*35] of this state or of the United States." The statute also provides that "the exemptions shall be liberally construed in harmony with federal statutes and ruling judicial interpretations of the United States courts . . ." Section 6-36-8. The D.E.M. is a regulatory agency that exists by legislative grant of power, and, as such, its actions in regulating the fishing industry are presumed valid and exempt from attack under antitrust law. Thus, this Court declares that Riley's claim that D.E.M violated antitrust laws and the Sherman Act fails.

## **D.E.M.'S DECISION**

With respect to the administrative appeal, Riley alleges that Hearing Officer's decision was not supported by substantial evidence and therefore fails to meet the standard required by G.L. 1956 § 42-35-15(g) and applicable case precedent. Newport Shipyard v. Rhode Island Comm'n for Human Rights, 484 A.2d 893 (R.I. 1984) (limiting court's review to determination of whether substantial evidence exists to support agency decision). Riley further argues that the hearing officer erred in granting summary judgment because discovery had not yet been completed. The [\*36] D.E.M. counters that the Hearing Officer took all evidence into consideration, weighing both sides, and arrived at a conclusion, which it believes was correct. Additionally, D.E.M. contends that summary judgment before the hearing officer was appropriate because Riley was not statutorily eligible for a license and, as such, there could be no factual dispute.

The Chief Hearing Officer provided a written order/opinion that discussed the analysis she employed to reach her decision, upholding the denial of the license.<sup>15</sup> Here, this Court is satisfied that the Hearing Officer, based her denial on substantial evidence. The Hearing Officer made several findings of fact in reaching her decision, including the following:

1. The Applicant, Steven J. Riley, did not possess a commercial fishing license as of December 31, 2002.
2. On February 21, 2003 Steven J. Riley applied for a commercial fishing license (Principal Effort License) with quahog and restricted finfish endorsements.
3. The Office of Boat Registration and Licensing issued a final denial by letter dated August 20, 2003.
4. Applicant filed an appeal with the Administrative Adjudication Division on September 16, 2003." [\*37] (Lanphear Decision at 7).

Additionally, the Hearing Officer made several conclusions of law prior to granting summary judgment in favor of D.E.M. including the following:

1. The Administrative Adjudication Division for Environmental Matters ("AAD") has jurisdiction over this matter pursuant to R.I. GEN. LAWS § 42-17.7-2; R.I. GEN. LAWS § 20-2.1-12(c); and Rule 6.7-10(i) of the Rules and Regulations Governing the Management of Marine Fisheries.

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<sup>15</sup> The Hearing Officer's authority prohibited her from addressing the constitutional issues raised by the Appellant.

2. The license sought by Applicant constitutes a new license as contemplated by [R.I. GEN. LAWS § 20-2.1-5 \(1\)\(ii\)](#) and the Rules and Regulations Governing the Management of Marine Fisheries.
3. Rule 7.2 of the Rules and Regulations Governing the Management of Marine Fisheries prohibits the issuance of new Principal Effort Licenses (including licenses with quahog and non-restricted finfish endorsements) for 2003.
4. Rule 7.2 of the Rules and Regulations Governing the Management of Marine Fisheries is consistent with [R.I. GEN. LAWS § 20-2.1-5 \(1\)\(ii\)](#) and furthers the statutory scheme and purposes of [\*38] the statute.
5. Pursuant to [R.I. GEN. LAWS § 20-2.1-5\(1\)\(ii\)](#) Applicant is not eligible for a principal effort license with quahog and non-restricted finfish endorsements.
6. There is no dispute as to any genuine issue of material fact and the Office of Management Services is entitled to judgment as a matter of law." (Lanphear Decision at 7-8).

The Hearing Officer also cited to two previous administrative decisions that denied fishing licenses in the same manner, basing the decision on the applicant's lack of a license prior to the date that the ban went into effect under [G.L. § 20-2.1-5\(1\)\(ii\)](#). The record evidences that Riley was not even eligible, *ab initio*, to obtain a license with the endorsements that he sought. As such, this Court finds that the Hearing Officer's denial of said license was consistent with constitutional and statutory provisions, was not arbitrary or capricious or affected by error of law, and was supported by reliable, probative, and substantial evidence. Additionally, since there were no material facts in dispute her grant of summary judgment was correct.

#### **[\*39] CONCLUSION**

Riley has not met his burden of demonstrating that his rights of due process and equal protection have been violated. This Court finds that both [G.L. 1956 § 20-2.1-5](#) and Rule 7 are constitutional because they are rationally related to the legitimate government purpose in protecting the welfare of the public and promoting conservation of natural fish resources through license limitations. Furthermore, antitrust laws, including the Sherman Act, do not apply to regulatory agencies, such as the D.E.M., on the facts of this case, due to a statutory exemption and valid precedent. For the reasons stated above, this Court finds that the police powers of the State and the plenary powers of the General Assembly to regulate the fisheries are determinative in this case. Additionally, substantial rights of the Appellant have not been prejudiced. The Hearing Officer's decision was based on reliable, probative, and substantial evidence, in accordance with constitutional and statutory provisions, and was not arbitrary or capricious or affected by error of law. Thus, this Court hereby denies the declaratory relief prayed for by the Appellant and affirms [\*40] the decision of the D.E.M Hearing Officer.

Counsel shall submit an appropriate order consistent with this opinion.



## Genesee Vending, Inc. v. R.J. Reynolds Tobacco Co.

United States District Court for the Eastern District of Michigan, Southern Division

May 2, 2005, Decided ; May 2, 2005, Filed

Case No. 04-71834

### **Reporter**

2005 U.S. Dist. LEXIS 17442 \*; 2005-01 Trade Cas. (CCH) P74,818

GENESEE VENDING, INC., et al., Plaintiffs, v. R.J. REYNOLDS TOBACCO CO., Defendant.

**Disposition:** [\*1] Defendant's January 24, 2005 Motion to Dismiss DENIED.

## **Core Terms**

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Cigarette, retail, Plaintiffs', purchasers, allegations, price discrimination, competitors, favored, amended complaint, benefits, consumer, products

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### [HN1](#) [] Complaints, Requirements for Complaint

Fed. R. Civ. P. 8(a) requires a complaint to contain a short and plain statement of the claim showing that the pleader is entitled to relief. The rules do not require a claimant to set out in detail the facts upon which he bases his claim. To the contrary, all the Rules require is a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### [HN2](#) [] Robinson-Patman Act, Claims

Under Fed. R. Civ. P. 12(b)(6), the factual allegations in the complaint must be regarded as true. The claim shall not be dismissed unless it appears beyond doubt that a plaintiff can prove no set of facts in support of his claim which

would entitle him to relief. To survive dismissal under [Rule 12\(b\)\(6\)](#), a complaint must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory.

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

[Antitrust & Trade Law > Clayton Act > General Overview](#)

[Antitrust & Trade Law > Clayton Act > Scope](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Primary Line Injuries](#)

[Antitrust & Trade Law > Robinson-Patman Act > Coverage > General Overview](#)

### [\*\*HN3\*\*](#) **Robinson-Patman Act, Claims**

The Clayton Act is an [antitrust law](#) that primarily protected against primary line price discrimination, or price discrimination tending to injure the price discriminator's competitors.

[Antitrust & Trade Law > Robinson-Patman Act > Coverage > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Primary Line Injuries](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Secondary & Tertiary Line Injuries](#)

[Antitrust & Trade Law > Robinson-Patman Act > General Overview](#)

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

### [\*\*HN4\*\*](#) **Robinson-Patman Act, Coverage**

The Robinson-Patman Act is intended to curb and prohibit all devices by which large buyers gained discriminatory preferences over smaller ones by virtue of their greater purchasing power. The Act protects against "primary-line" as well as "secondary-line" violations. "Secondary line" violations occur when a seller's discrimination impacts competition among the seller's customers; i.e., the favored purchasers and disfavored purchasers.

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

[Antitrust & Trade Law > Regulated Practices > Price Discrimination > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Secondary & Tertiary Line Injuries](#)

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

[Antitrust & Trade Law > Robinson-Patman Act > General Overview](#)

Antitrust & Trade Law > Robinson-Patman Act > Coverage > General Overview

#### [\*\*HN5\*\*](#) **Robinson-Patman Act, Claims**

Section 2(a) of the Robinson-Patman Act prohibits a supplier from discriminating in price between different purchasers of like grade and quality where the effect is substantially to lessen competition. [15 U.S.C.S. § 13\(a\)](#). To establish secondary-line price discrimination under § 2(a) of the Act, a plaintiff must demonstrate: (1) that the seller's sales were made in interstate commerce; (2) that the seller discriminated in price as between the two purchasers; (3) that the product or commodity sold to the competing purchasers was of the same grade and quality; and (4) that the price discrimination had a prohibited effect on competition. A private plaintiff must also show that it suffered actual injury to its business or property as a result of the price discrimination.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > Regulated Practices > Price Discrimination > Promotional Allowances & Services

Antitrust & Trade Law > Robinson-Patman Act > General Overview

#### [\*\*HN6\*\*](#) **Robinson-Patman Act, Claims**

Sections 2(d) and (e) of the Robinson-Patman Act deal with discrimination in the field of promotional services made available to purchasers who buy for resale. Among the "promotional services" covered by the Act are advertising, display materials, and promotional contests. The elements of a claim under § 2(d) and (e) differ from that under § 2(a) only in that it is unnecessary to prove a prohibited effect on competition. [15 U.S.C.S. § 13\(d\), \(e\)](#).

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > Regulated Practices > Price Discrimination > Promotional Allowances & Services

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

#### [\*\*HN7\*\*](#) **Price Discrimination, Competitive Injuries**

Plaintiffs in a Robinson-Patman Act action need not make reference to specific transactions or promotional programs in their complaint. Such pleading of the evidence is a matter for the discovery process, not for allegations of detail in the complaint. The complaint should not be burdened with possibly hundreds of specific instances. If it were, it would be comparatively meaningless at trial where the parties could adduce further pertinent evidence if discovered.

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

#### [\*\*HN8\*\*](#) **Pleadings, Rule Application & Interpretation**

Factual pleading is required only insofar as it is necessary to place a defendant on notice as to the type of claim alleged and the grounds upon which it rests, thereby enabling a defendant to prepare a responsive pleading.

**Counsel:** For Genesee Vending, Incorporated, Suing individually and on behalf of a class of similarly situated persons, Plaintiff: Douglas B. McFadden, John M. Shoreman, McFadden & Shoreman, Washington, DC.

For R. J. Reynolds Tobacco Company, Defendant: Daniel P. Malone, Lynn A. Sheehy, Butzel Long, Detroit, MI; Thomas Demitack, Jones Day, Cleveland, OH.

**Judges:** John Corbett O'Meara, United States District Judge.

**Opinion by:** John Corbett O'Meara

## Opinion

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### **OPINION AND ORDER DENYING DEFENDANT'S MOTION TO DISMISS AMENDED COMPLAINT**

Before the court is Defendant's Motion to Dismiss Plaintiffs' Amended Complaint, filed January 24, 2005. The court heard oral argument on Defendant's motion on April 29, 2005, and took the matter under advisement. For the reasons stated below, Defendant's motion is denied.

### **BACKGROUND FACTS**

Plaintiffs are 236 companies that own and operate cigarette vending machines in various locations across the country.<sup>1</sup> Plaintiffs are suing Defendant, R.J. Reynolds Tobacco Company ("RJR"), under the *Robinson-Patman Act*, alleging price discrimination. RJR manufactures cigarettes under brand names that include Winston, [\*\*2] Camel, and Salem. Plaintiffs claim that RJR discriminates against them in favor of a competing class of retailers: convenience stores, gas stations, mini-marts, kiosks, and discount stores. According to Plaintiffs, RJR provides convenience stores with price rebates, inventory buy-down promotions, advertising and display allowances, and consumer promotions, which have the effect of lowering the per pack price of cigarettes for convenience store customers. Plaintiffs allege that they are excluded from these sales and advertising programs, to their competitive disadvantage.

For each plaintiff, the Amended Complaint details the plaintiff's location, a specific competitor that receives allegedly more favorable treatment, and the products at issue. The allegations are virtually identical for each plaintiff; an example of these allegations is as follows:

Baton Rouge Cigarette Service is located in [\*\*3] Baton Rouge, LA and operates cigarette vending machines throughout Baton Rouge. Baton Rouge Cigarette Service owns and operates 714 cigarette vending machines. Baton Rouge Cigarette Service competes with other cigarette retail outlets, including but not limited to Swiftly's Food Mart, in the sale of Defendant's cigarette brands, including but not limited to Winston, Winston Lights, Camel, Camel Lights, Salem, and Salem Lights, to adult consumers. Baton Rouge Cigarette Service's retail competitors receive promotional benefits directly from Defendant, which include but are not limited to: advertising and display payments, inventory payments, consumer promotions, consumer price rebates and buy-down promotions. Neither the aforementioned promotional benefits, nor any proportionally equivalent benefits, are made available to Baton Rouge Cigarette Service. Defendant's cigarette brands and retail promotional benefits move continuously in a stream of interstate commerce. Defendant's discrimination in price and benefits against Baton Rouge Cigarette Service and in favor of its other retail customers has the effect of substantially lessening competition in the sale of cigarettes on a per pack [\*\*4] basis to adult consumers in the

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<sup>1</sup> Plaintiffs have styled their complaint as a class action. The court has not, however, ruled upon this issue.

marketplace. Defendant's misconduct adversely affects and injures, suppresses and eliminates competition between Baton Rouge Cigarette Service and Defendant's favored retail customers. By reason of Defendant's discrimination in price and benefits, Baton Rouge Cigarette Service has been injured in its business and property through losses in sales and profits in an amount not less than \$ 2,499,000.00. Defendant's continued misconduct in violation of the law threatens Baton Rouge Cigarette Service with future losses and injuries attributable directly to the violation.

Pls.' First Amended Compl. at P21 (Count I).

Defendant claims that Plaintiffs' amended complaint is flawed pursuant to [Rule 8\(a\)](#) and [Rule 12\(b\)\(6\)](#) because they fail to allege that they "competed against a retailer that bought directly from RJRT" and that retailer "received a discount that RJRT did not offer to that plaintiff." Def.'s Br. at 4. According to Defendant, "no plaintiff identifies a favored competing buyer, the product that each of them purchased from RJRT, when each of them bought it, the quantity that it purchased or the amount of the claimed price difference." Defendant [\*5] claims that these are "basic elements of a [Section 2\(a\)](#) [Robinson-Patman] violation." Plaintiffs contend that their allegations are sufficient to state a claim under the [Robinson-Patman Act](#).

## LAW AND ANALYSIS

### I. Standard of Review

[HN1](#)[] [Federal Rule of Civil Procedure 8\(a\)](#) requires a complaint to contain "a short and plain statement of the claim showing that the pleader is entitled to relief. . . ." The rules "do not require a claimant to set out in detail the facts upon which he bases his claim. To the contrary, all the Rules require is 'a short and plain statement of the claim' that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests." [Conley v. Gibson, 355 U.S. 41, 47, 2 L. Ed. 2d 80, 78 S. Ct. 99 \(1957\)](#).

[HN2](#)[] Under [Rule 12\(b\)\(6\)](#), "the factual allegations in the complaint must be regarded as true. The claim should not be dismissed unless it appears beyond doubt that plaintiff can prove no set of facts in support of his claim which would entitle him to relief." [Scheid v. Fanny Farmer Candy Shops, Inc., 859 F.2d 434, 436 \(6th Cir. 1988\)](#) (citations omitted); see also [\*6] [Conley, 355 U.S. at 45-46](#). To survive dismissal under [Rule 12\(b\)\(6\)](#), a complaint "must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory." [Scheid, 859 F.2d at 436](#) (citations omitted) (emphasis in original).

### II. Elements of a Robinson-Patman Claim

The [Robinson-Patman Act](#) was passed in 1936 as an amendment to the [Clayton Act](#). [HN3](#)[] "The [Clayton Act](#) is an [antitrust law](#) that primarily protected against 'primary line' price discrimination, or price discrimination tending to injure the price discriminator's competitors." [Lewis v. Philip Morris Inc., 355 F.3d 515, 520 \(6th Cir. 2004\)](#). Congress passed the [Robinson-Patman Act](#) to "protect small retail stores from the concentrated buying power of larger chain stores." [Id. at 520](#). [HN4](#)[] The Act was intended to "curb and prohibit all devices by which large buyers gained discriminatory preferences over smaller ones by virtue of their greater purchasing power." [Id.](#) The Act protects against "primary-line" as well as "secondary-line" violations. "Secondary line" violations occur "when [\*7] a seller's discrimination impacts competition among the seller's customers; i.e., the favored purchasers and disfavored purchasers." [Id.](#) (citation omitted). This case involves an alleged secondary-line violation, because it is the competitors of the "favored purchasers" that are claiming discrimination, rather than the competitors of R.J. Reynolds.

Plaintiffs' First Amended Complaint alleges violations of Sections 2(a), 2(d), and 2(e) of the Robinson-Patman Act ([15 U.S.C. §§13\(a\), \(d\), \(e\)](#)). [HN5](#)[] Section 2(a) of the Act prohibits a supplier from "discriminating in price between different purchasers of like grade and quality where the effect is substantially to lessen competition." [Id. at](#)

521 (citing 15 U.S.C. § 13(a)). To establish secondary-line price discrimination under section 2(a) of the Act (Plaintiffs' Count I), the plaintiff must demonstrate:

(1) that the seller's sales were made in interstate commerce; (2) that the seller discriminated in price as between the two purchasers; (3) that the product or commodity sold to the competing purchasers was of the same grade and quality; and (4) that the price discrimination [\*8] had a prohibited effect on competition.

Industrial Burner Sys., Inc. v. Maxon Corp., 275 F. Supp. 2d 878, 882 (E.D. Mich. 2003) (citing George Haug Co. v. Rolls Royce Motor Cars, Inc., 148 F.3d 136, 141 (2d Cir. 1998)). A private plaintiff must also show that "it suffered actual injury to its business or property as a result of the price discrimination." Id.

**HN6** [↑] Sections 2(d) and (e) of the Act "deal with discrimination in the field of promotional services made available to purchasers who buy for resale." Lewis, 355 F.3d at 521-22. Among the "promotional services" covered by the Act are advertising, display materials, and promotional contests. Id. at 522. The elements of a claim under Sections 2(d) and (e) differ from that under Section 2(a) only in that it is unnecessary to prove a prohibited effect on competition. See Lewis, 355 F.3d at 522 n.6, 7; 15 U.S.C. § 13(d), (e).

### III. Sufficiency of Plaintiffs' Complaint

Defendant complains that Plaintiffs do not sufficiently allege violations of Sections 2(a), (d), or (e) in their complaint. According to Defendant, [\*9] Plaintiffs' Section 2(a) claim is deficient because "none of the eleven Count I plaintiffs alleges that it competed against a retailer that bought directly from RJRT, as required by the statute, and that [the retailer] received a discount that RJRT did not offer to plaintiff. No plaintiff identifies a favored competing buyer, the product that each of them purchased from RJRT, when each of them bought it, the quantity that it purchased or the amount of the claimed price difference." Def. Br. at 4. Defendant contends that Plaintiffs' Section 2(d) and (e) claim is insufficient because Plaintiffs do not allege that "RJR provided a promotional allowance or service to a retailer against which the plaintiff competed, while not providing that promotional service to plaintiff." Id.

The pleading requirements for a Robinson-Patman claim are not as stringent as Defendant alleges. Defendant relies upon Mountain View Pharmacy v. Abbott Laboratories, 630 F.2d 1383 (10th Cir. 1980) and Chawla v. Shell Oil Co., 75 F. Supp. 2d 626 (S.D. Tex. 1999) for the proposition that Plaintiffs' complaint must set forth greater factual specificity or be dismissed. In [\*10] Mountain View, however, the plaintiffs' complaint failed "to specify any products that were the subject of discriminatory treatment, nor does it identify the favored and disfavored purchasers of a particular product. In view of the number of plaintiffs [13], defendants [28], and products involved in this suit, a complaint that fails to allege at least some of this information does not give fair notice of the grounds upon which the Robinson-Patman claim rests." Mountain View, 630 F.2d at 1388. See also Chawla, 75 F. Supp. 2d at 653-54 (holding that in case with 73 plaintiffs, the "case must be analyzed from the perspective of each Plaintiff separately. Plaintiffs have not even attempted to meet their individual pleading burden.").

In contrast, in this case, Plaintiffs have identified the products that were the subject of discriminatory treatment (cigarettes, including the Winston, Camel, and Salem brands) and at least one specific favored purchaser and disfavored purchaser for each plaintiff. See, e.g., Compl. at P21 (allegations specific to each plaintiff); National Assoc. of College Bookstores, Inc. v. Cambridge University Press, 990 F. Supp. 245, 253 (S.D. N.Y. 1997) [\*11] (distinguishing Mountain View and finding complaint sufficient where it "does identify products that were subject to discriminatory treatment, favored purchasers, and disfavored purchasers"). Plaintiffs also generally allege that (1) Defendant's sales were made in interstate commerce (Compl. at P15); (2) Defendant discriminated in price between Plaintiffs and Plaintiffs' retail competitors, by providing "rebates, buy-back and buy-down payments" to Plaintiffs' competitors, but not to Plaintiffs (Compl. at P18); (3) Defendant sells cigarettes of "identical grade and quality to Plaintiffs and to each individual Plaintiff's retail competitors" (Compl. at P15); and (4) that the price discrimination had a prohibited effect on competition (Compl. at P19). These are the required elements of a price discrimination claim under Section 2(a) and a claim under Sections 2(d) and (e). See, e.g., Industrial Burner Sys., 275 F. Supp. 2d at 882; Lewis, 355 F.3d at 522 n.6, 7; 15 U.S.C. §§ 13(a), (d), (e).

Contrary to Defendant's suggestion, [HN7](#)[<sup>1</sup>] Plaintiffs need not make reference to specific transactions or promotional programs in their complaint. [\*12]

Such pleading of the evidence . . . is a matter for the discovery process, not for allegations of detail in the complaint. The complaint should not be burdened with possibly hundreds of specific instances. . . if it were, it would be comparatively meaningless at trial where the parties could adduce further pertinent evidence if discovered.

*National Assoc. of College Bookstores*, 990 F. Supp. at 252 (quoting [Nagler v. Admiral Corp.](#), 248 F.2d 319, 326 (2d Cir. 1957)). See also [Mountain View](#), 630 F.2d at 1388 ("We are not demanding an inordinate level of factual specificity in the amended complaint. We recognize that [HN8](#)[<sup>1</sup>] factual pleading is required only insofar as it is necessary to place a defendant on notice as to the type of claim alleged and the grounds upon which it rests, thereby enabling a defendant to prepare a responsive pleading.").

In this case, Plaintiffs have given Defendant notice of the type of claim alleged and the grounds upon which it rests. Plaintiffs' First Amended Complaint comports with the requirements of [Rule 8\(a\)](#) and [Rule 12\(b\)\(6\)](#), in that Plaintiffs have plead all the elements of a Robinson-Patman [\*13] claim. Defendant can obtain further factual development of Plaintiffs' claims during discovery.

Accordingly, IT IS HEREBY ORDERED that Defendant's January 24, 2005 Motion to Dismiss is DENIED.

John Corbett O'Meara

United States District Judge

Dated: May 2, 2005

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End of Document

## *In re Monosodium Glutamate Antitrust Litig.*

United States District Court for the District of Minnesota

May 2, 2005, Decided

Civil File No. 00-MDL-1328 (PAM)

**Reporter**

2005 U.S. Dist. LEXIS 8424 \*; 2005-1 Trade Cas. (CCH) P74,781

In re Monosodium Glutamate Antitrust Litigation

**Subsequent History:** Reconsideration granted by, Complaint dismissed at [\*Inquivosa, S.A. v. Ajinomoto Co., Inc. \(In re Monosodium Glutamate Antitrust Litig.\), 2005 U.S. Dist. LEXIS 39641 \(D. Minn., Oct. 26, 2005\)\*](#)

**Prior History:** [\*Conopco, Inc. v. Daesang Japan, Inc. \(In re Monosodium Glutamate Antitrust Litig.\), 2003 U.S. Dist. LEXIS 23237 \(D. Minn., Dec. 23, 2003\)\*](#)

## Core Terms

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domestic, Defendants', commerce, anti-competitive, prices, subject matter jurisdiction, anti trust law, antitrust, Plaintiffs', conspiracy, cartel, effects, nucleotides, Sherman Act, profits, abroad, comity, purchasers, injuries, international cartel, motion to dismiss, allegations, causation, inflated, linked, resale

## LexisNexis® Headnotes

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Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrs & Objections > Motions to Dismiss

### [HN1](#) [down arrow] Motions to Dismiss, Failure to State Claim

A motion to dismiss for lack of subject matter jurisdiction under [\*Fed. R. Civ. P. 12\(b\)\(1\)\*](#) may challenge the complaint either on its face or on the factual truthfulness of its averments. Where a defendant challenges the complaint on its face, the court reviews the pleadings and affords the plaintiff the same protections that it would receive on a [\*Fed. R. Civ. P. 12\(b\)\(6\)\*](#) motion to dismiss. A court takes the factual allegations as true and will only dismiss the complaint if the plaintiff fails to allege an essential element for subject matter jurisdiction.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### [HN2](#) [down arrow] Motions to Dismiss, Failure to State Claim

When determining whether to grant a motion to dismiss for failure to state a claim upon which relief may be granted, a court must construe the pleadings in the light most favorable to the non-moving party, and view the facts alleged in the complaint as true. [Fed. R. Civ. P. 12\(b\)\(6\)](#). The court also must draw all reasonable inferences in the non-moving party's favor. The court may dismiss a claim only if relief cannot be afforded under any set of facts that could be proved consistent with the allegations.

Antitrust & Trade Law > International Aspects > Foreign Trade Antitrust Improvements Act

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

### [\*\*HN3\*\*](#) International Aspects, Foreign Trade Antitrust Improvements Act

The Foreign Trade Antitrust Improvements Act provides that the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), applies to foreign conduct only if: (1) the conduct has a direct, substantial, and reasonably foreseeable effect on United States commerce, and (2) such effect gives rise to a claim under the Sherman Act. [15 U.S.C.S. § 6a\(1\)-\(2\)](#).

Antitrust & Trade Law > Sherman Act > Claims

International Law > Authority to Regulate > Anticompetitive Activities

International Trade Law > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Antitrust & Trade Law > International Aspects > Foreign Trade Antitrust Improvements Act

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

### [\*\*HN4\*\*](#) Sherman Act, Claims

The purpose of the Foreign Trade Antitrust Improvements Act (FTAIA) is to establish that restraints on export trade only violate the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), if they have a direct and substantial effect on commerce within the United States or a domestic firm competing for foreign trade. The FTAIA is not intended to confer jurisdiction on injured foreign persons when that injury arose from conduct with no anticompetitive effects in the domestic marketplace.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

International Trade Law > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

### [\*\*HN5\*\*](#) Private Actions, Remedies

The Sherman Act, [15 U.S.C.S. § 1 et seq.](#), does not apply when a plaintiff cannot show a causal link between the domestic effect and their alleged injury. Rather, to invoke the protections of the Sherman Act, a plaintiff must show

that the defendant's conduct affected United States commerce and that the domestic effect gave rise to the plaintiff's injury.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

International Trade Law > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Antitrust & Trade Law > International Aspects > Foreign Trade Antitrust Improvements Act

International Law > Authority to Regulate > General Overview

## **HN6** [down] **Subject Matter Jurisdiction, Jurisdiction Over Actions**

The existence of a single, global conspiracy does not relieve the plaintiff's burden of satisfying the Foreign Trade Antitrust Improvements Act. Instead, the plaintiff must allege that its injury arose from the conspiracy's proscribed effects on United States commerce.

Governments > Courts > Judicial Comity

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Antitrust & Trade Law > International Aspects > Foreign Trade Antitrust Improvements Act

Civil Procedure > ... > Jurisdiction > Jurisdictional Sources > Statutory Sources

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Governments > State & Territorial Governments > Relations With Governments

International Law > Dispute Resolution > Comity Doctrine > General Overview

International Law > ... > Comity Doctrine > Areas of Law > Commercial Transactions

International Trade Law > General Overview

## **HN7** [down] **Courts, Judicial Comity**

The Foreign Trade Antitrust Improvements Act does not preclude the application of comity as a basis upon which to assert jurisdiction over foreign conduct, even where that conduct might otherwise be determined to have a direct, substantial and reasonably foreseeable anticompetitive effect on United States commerce. Where a court determines that the requirements for subject matter jurisdiction are met, a statute has no effect on the court's ability to employ notions of comity or otherwise to take account of the international character of the transaction.

Contracts Law > Contract Formation > Mistake > General Overview

Governments > Legislation > Interpretation

#### [\*\*HN8\*\*](#) [blue] **Contract Formation, Mistake**

A court ordinarily construes ambiguous statutes to avoid unreasonable interference with the sovereign authority of other nations. That rule of statutory construction cautions courts to assume that legislators take account of the legitimate sovereign interests of other nations when they write American laws. It thereby helps the potentially conflicting laws of different nations work together in harmony.

Governments > Courts > Judicial Comity

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

International Law > ... > Comity Doctrine > Areas of Law > Commercial Transactions

#### [\*\*HN9\*\*](#) [blue] **Courts, Judicial Comity**

America's antitrust laws, when applied to foreign conduct, can interfere with a foreign nation's ability independently to regulate its own commercial affairs. But American courts hold that application of our antitrust laws to foreign anticompetitive conduct is nonetheless reasonable, and hence consistent with principles of prescriptive comity, insofar as they reflect a legislative effort to redress domestic injury that foreign anticompetitive conduct has caused.

Antitrust & Trade Law > Sherman Act > General Overview

International Law > Authority to Regulate > Anticompetitive Activities

International Trade Law > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

#### [\*\*HN10\*\*](#) [blue] **Antitrust & Trade Law, Sherman Act**

The Sherman Act, [15 U.S.C.S. § 1 et seq.](#), applies to foreign conduct that was meant to produce, and did in fact produce, some substantial effect in the United States.

Antitrust & Trade Law > Sherman Act > Jurisdiction

International Law > Authority to Regulate > General Overview

International Trade Law > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

#### [\*\*HN11\*\*](#) [blue] **Sherman Act, Jurisdiction**

Any major activities on an international cartel would likely have the requisite impact on United States commerce to trigger U.S. subject matter jurisdiction under the Sherman Act, [15 U.S.C.S. § 1 et seq.](#) For example, if a domestic export cartel were so strong as to have a "spillover" effect on commerce within the U.S. by creating a world wide shortage or artificially inflated world wide price that had the effect of raising domestic prices, the cartel's conduct would fall within the reach of U.S. antitrust laws. Such an impact would, at least over time, meet the test of a direct, substantial and reasonably foreseeable effect on domestic commerce.

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Business & Corporate Law > Foreign Corporations > General Overview

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

## [HN12](#) International Aspects, International Application of US Law

American **antitrust law** is based on the principle that deterrence will be effective only if conspirators' anticipated sanctions exceed their potential profits. To deny a foreign plaintiff injured by an antitrust violation the right to sue would defeat these purposes. It would permit a price fixer or a monopolist to escape full liability for his illegal actions and would deny compensation to certain of his victims, merely because he happens to deal with foreign customers. An exclusion of all foreign plaintiffs would lessen the deterrent effect of treble damages. The conspiracy alleged by the respondents in this case operated domestically as well as internationally. If foreign plaintiffs were not permitted to seek a remedy for their antitrust injuries, persons doing business in both this country and abroad might be tempted to enter into anticompetitive conspiracies affecting American consumers in the expectation that the illegal profits they could safely extort abroad would offset any liability to plaintiffs at home. If, on the other hand, potential antitrust violators must take into account the full costs of their conduct, American consumers are benefitted by the maximum deterrent effect of treble damages upon all potential violators.

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

International Law > Authority to Regulate > Anticompetitive Activities

International Trade Law > General Overview

International Law > Authority to Regulate > General Overview

## [HN13](#) International Aspects, International Application of US Law

With respect to an international cartel, United States antitrust sanctions are ineffective at deterring anticompetitive conduct in the U.S. if they merely approximate the cartel's profits in the U.S. To ensure that international cartels are truly deterred and deprived of the fruits of their illegality, U.S. antitrust laws must also apply to foreign injury. Thus, when the anticompetitive conduct of an international cartel adversely affects U.S. commerce, which in turn causes foreign injury, the foreign plaintiff may seek recourse under the U.S. antitrust laws.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

## HN14[ Private Actions, Standing

To establish standing in an antitrust case, plaintiffs must prove more than injury casually linked to an illegal presence in the market. Plaintiffs must prove an antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. In addition, plaintiffs must establish that there was proximate causation between their harm and the alleged illegal market restraint. Thus, if plaintiffs' injuries are too remote and damages are too speculative, plaintiffs will fail to satisfy the standing requirement.

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For Petbowe Chemtrade Corp, Plus Sun Co., Ltd., Menssing Chemiehandel & Consultants, GmbH (MCC), on behalf of all others similarly situated, Plaintiffs: Daniel E Gustafson, Karla M Gluek, Gustafson Gluek PLLC, Mpls, MN; [\*2] Donald L Perelman, Fine Kaplan & Black, Philadelphia, PA; Gerald J Rodos, Barrack Rodos & Bacine, Philadelphia, PA; Howard J Sedran, Levin Fishbein Sedran & Berman, Philadelphia, PA; Joseph Goldberg, Freedman Boyd & Daniels, Albuquerque, NM; Martin D Chitwood, Chitwood Harley Harnes LLP, Atlanta, GA; Richard A Lockridge, W Joseph Bruckner, Lockridge Grindal Nauen PLLP, Mpls, MN; Samuel D Heins, Heins Mills & Olson, PLC, Mpls, MN.

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For Kyowa Hakko Kogyo Co., Ltd., Defendant: Christopher V Roberts, Weil Gotshal & Manges - NY, New York, NY; Douglas R Boettge, William L Greene, Leonard Street and Deinard - Mpls, Mpls. MN.

**Judges:** Paul A. Magnuson, United States District Court Judge.

**Opinion by:** Paul A. Magnuson

## Opinion

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### **MEMORANDUM AND ORDER**

This document relates to:

*Inquivosa, S.A., et al. v. Ajinomoto Co., Inc., et al.*, Civ. No. 03-2997

This matter is before the Court on Defendants' Motion to Dismiss for Lack of Subject Matter Jurisdiction and Standing. For the reasons [\*3] that follow, the Court denies the Motion.

### **BACKGROUND**

Plaintiffs are foreign corporations who purchased monosodium glutamate ("MSG") and/or nucleotides directly from one or more Defendants in transactions that occurred outside of the United States.<sup>1</sup> Plaintiffs allege that Defendants and an undetermined number of unnamed co-conspirators participated in a global price-fixing and market allocation scheme to increase the world-wide price of MSG and nucleotides. Plaintiffs also claim that Defendants' conduct in forming and implementing the global conspiracy exerted direct and substantial effects on United States trade and commerce by inflating the prices paid by purchasers in the United States. (Am. Compl. PP 13-28.) In addition, Plaintiffs allege that price movements in one geographic sub-market were inextricably linked to all other markets so that the prices charged by Defendants and their co-conspirators in other countries were highly correlated with United States prices. (*Id.* PP 39-42.)

[\*4] According to Plaintiffs, Defendants fixed United States prices and controlled United States markets not merely to capture cartel profits in the United States, but also to allow the cartel to be effective anywhere in the world. Because MSG and nucleotides are fungible commodities, Defendants and their co-conspirators allegedly "knew that their conspiracy would not succeed unless they coordinated their prices and market shares in markets across the world." (*Id.* P 43.) Thus, Defendants allegedly included the United States in the cartel precisely to extract cartel profits from purchasers around the world without risk of arbitrage. (*Id.*)

Plaintiffs' alleged injury is that they purchased overpriced MSG and nucleotides abroad because Defendants' unlawful conspiracy prevented them from buying competitively priced MSG and nucleotides from the United States. (*Id.* PP 54-56.)

Defendants Ajinomoto Co. Inc., Ajinomoto U.S.A., Inc., Takeda Pharmaceutical Company Limited (f/k/a Takeda Chemical Industries, Ltd.), Kyowa Hakko Kogyo Co., Ltd. now seek dismissal of the Amended Complaint under [Federal Rules of Civil Procedure 12\(b\)\(1\)](#) and [12\(b\)\(6\)](#) [\*5] .<sup>2</sup>

## DISCUSSION

### A. Standard of Review

**HN1** [↑] A motion to dismiss for lack of subject matter jurisdiction under [Rule 12\(b\)\(1\)](#) may challenge the complaint either on its face or on the factual truthfulness of its averments. [\*Titus v. Sullivan\*, 4 F.3d 590, 593 \(8th Cir. 1993\)](#). When a defendant challenges the complaint on its face, the Court reviews the pleadings and affords the plaintiff the same protections that it would receive on a [Rule 12\(b\)\(6\)](#) motion to dismiss. See [\*Osborn v. United States\*, 918 F.2d 724, 729 n.6 \(8th Cir. 1990\)](#). [\*6] The Court takes the factual allegations as true and will only dismiss the complaint if the plaintiff fails to allege an essential element for subject matter jurisdiction. See [\*Titus\*, 4 F.3d at 593](#).

**HN2** [↑] When determining whether to grant a motion to dismiss for failure to state a claim upon which relief may be granted, the Court must construe the pleadings in the light most favorable to the non-moving party, and view the facts alleged in the complaint as true. See [\*Fed.R.Civ.P. 12\(b\)\(6\)\*](#); [\*Hamm v. Groose\*, 15 F.3d 110, 112 \(8th Cir. 1994\)](#). The Court also must draw all reasonable inferences in the non-moving party's favor. [\*United States v. Stoltz\*, 327 F.3d 671, 674 \(8th Cir. 2003\)](#). The Court may dismiss a claim only if relief cannot be afforded under any set of facts that could be proved consistent with the allegations. [\*Hafley v. Lohman\*, 90 F.3d 264, 266 \(8th Cir. 1996\)](#).

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<sup>1</sup> Plaintiffs are attempting to sue on behalf of themselves and all foreign purchasers of MSG or nucleotides from any of the named Defendants or Defendants' co-conspirators from January 1, 1984, through November 1, 1999. (Am. Compl. P 45.)

<sup>2</sup> Defendants CJ Corp. (f/k/a Cheil Jedang Corporation) and CJ America, Inc. joined and adopted this Motion. Defendant Archer Daniels Midland Company also joined this Motion, and filed a Motion of its own based on the statute of limitations. On March 17, 2005, Plaintiffs voluntarily dismissed with prejudice all claims asserted against Archer Daniels Midland. Eight other Defendants failed to appear for this Motion. It is unclear whether service has been effected or refused by these Defendants.

## B. Subject Matter Jurisdiction

Defendants contend that the Court lacks subject matter jurisdiction over this action because the *Sherman Act* does not apply to Plaintiffs' antitrust claim. Plaintiffs counter that the Court [\*7] has subject matter jurisdiction because the effect of Defendants' conspiracy on United States commerce "gave direct rise to Plaintiffs' antitrust claims and injuries." (Am. Compl. P 4.)

Congress enacted the *Foreign Trade Antitrust Improvements Act* ("FTAIA") in 1982 to clarify the application of United States antitrust laws to international business transactions. See [15 U.S.C. § 6a](#). Specifically, [HN3](#) the FTAIA provides that the Sherman Act applies to foreign conduct only if: (1) the conduct has a "direct, substantial, and reasonably foreseeable effect" on United States commerce, and (2) "such effect gives rise to a claim" under the Sherman Act. *Id.* at [§ 6a\(1\)-\(2\)](#); see also H.R. Rep 97-686, 1982 WL 25066, at \*8 [HN4](#) (the purpose of the FTAIA is to "establish that restraints on export trade only violate the Sherman Act if they have a direct and substantial effect on commerce within the United States or a domestic firm competing for foreign trade"); *Id.* at \*11(the FTAIA is not intended "to confer jurisdiction on injured foreign persons when that injury arose from conduct with no anti-competitive effects in the domestic marketplace").

The United [\*8] States Supreme Court recently addressed the scope of the FTAIA in *F. Hoffmann-La Roche Ltd v. Empagran, S.A.*, [542 U.S. 155, 159 L. Ed. 2d 226, 124 S. Ct. 2359 \(2004\)](#). In *Empagran*, the price-fixing conduct significantly and adversely affected customers both within and outside the United States. However, the adverse foreign effect was independent of any adverse domestic effect. The Supreme Court held that [HN5](#) the Sherman Act did not apply when a plaintiff cannot show a causal link between the domestic effect and their alleged injury. *Id.* at [2366-71](#). Rather, to invoke the protections of the Sherman Act, a plaintiff must show that the defendant's conduct affected United States commerce and that the domestic effect gave rise to the plaintiff's injury. *Id.* at [2371-72](#).

### 1. Foreign Injury Dependent on Domestic Effect

The *Empagran* Court expressly declined to address the issue presented in this case: whether subject matter jurisdiction exists when a plaintiff's foreign injury is allegedly linked to the domestic effects of the allegedly anti-competitive conduct. *Id.* at [2372](#). Instead, it remanded the issue to the District of Columbia Circuit Court [\*9] of Appeals.

Notably, however, the Supreme Court referred to *Industria Siciliana Asfalti, Bitumi S.p.A. v. Exxon Research & Eng'r Co.*, [1977 U.S. Dist. LEXIS 17851, 1977 WL 1353 \(S.D.N.Y. Jan. 18, 1977\)](#), and distinguished that case from the scope of its holding. In *Industria Siciliana*, the district court found that it had subject matter jurisdiction to decide a Sherman Act claim based on a foreign injury suffered by a foreign company. When discussing the case in *Empagran*, the Supreme Court expressly noted that the foreign injury in *Industria Siciliana* was "inextricably bound up with . . . domestic restraints of trade, and that the plaintiff was injured . . . by reason of an alleged restraint of our domestic trade." [124 S. Ct. at 2370](#) (internal citations and quotations omitted). Reference to *Industria Siciliana* indicates that subject matter jurisdiction exists when a plaintiff shows that its foreign injury arose from the domestic effect of the defendant's conduct.

Since *Empagran*, few courts have squarely addressed the issue of whether subject matter jurisdiction exists when the foreign injury is dependent on the domestic effect of anti-competitive conduct. See, [\*10] e.g., *MM Global Servs. v. Dow Chem. Co.*, [329 F. Supp. 2d 337 \(D. Conn. 2004\)](#). In *MM Global*, the defendants allegedly compelled the plaintiffs to engage in a price maintenance conspiracy with respect to the resale of Union Carbide products in India, and refused to accept orders if the prospective resale prices to end-users in India were below certain levels. *Id.* at [340](#). By doing so, the defendants allegedly sought to ensure that prices charged by the plaintiffs to end-users in India would not erode the prices to the end-users in the United States. *Id.* As a result of this price fixing, the plaintiffs alleged that competition in the sale and resale of Union Carbide products was improperly diminished and restrained. *Id.* The amended complaint further alleged:

As a direct and proximate result of the defendants' fixing of minimum resale prices and other terms of sale, competition in the sale and resale of products in and from the United States was improperly diminished and

restrained, and as the result of such effect on competition, the plaintiffs were injured by being precluded from effectively and fully competing and maximizing their sales [\*11] of products.

*Id. at 342* (emphasis in original).

The district court found that the plaintiffs sufficiently alleged that the defendants' conduct had an effect on competition in and from the United States and that the foreign plaintiffs were injured as a result of that effect. It therefore denied the motion to dismiss. *Id.*

## 2. Causation

Defendants argue that Plaintiffs' claim must fail because Plaintiffs do not and cannot allege that the United States prices were the direct cause of the alleged foreign price-fixing. In *Empagran*, the Supreme Court recognized that a claim based on foreign injury that depends on the domestic effect of the defendant's anti-competitive conduct involves but-for causation. [124 S. Ct. at 2372](#). Defendants contend that but-for causation cannot meet the requirements of the FTAIA. They argue that the "gives rise to" language in [§ 6a\(2\)](#) requires that Plaintiffs show that they were injured directly and immediately by the effect on United States commerce.

Defendants rely on [Associated General Contractors of California, Inc. v. California State Counsel of Carpenters, 459 U.S. 519, 74 L. Ed. 2d 723, 103 S. Ct. 897 \(1983\)](#) and [Den Norske Stats Oljeselskap AS v. HeereMac VOF, 241 F.3d 420 \(5th Cir. 2001\)](#) [\*12] to argue that direct causation is required. In *Associated General Contractors*, the Supreme Court found that the complaint contained only "somewhat vaguely defined links" between the plaintiffs' injury and the alleged restraint in the construction market, and consequently held that the alleged harm resulting from a violation of the antitrust laws was too attenuated and speculative to set forth a claim. [459 U.S. at 540-46](#).

In *Den Norske*, a Norwegian oil corporation conducting business exclusively in the North Sea brought an antitrust conspiracy claim against providers of heavy-lift barge services, alleging that the defendants' conduct inflated the plaintiff's operating costs in the North Sea and also inflated oil prices in the United States market. Notably, the plaintiff did not allege that the higher prices in the United States market gave rise to its claim. Rather, it alleged that the conspiracy compelled it to charge higher prices for the crude oil it exported to the United States. Thus, it was the plaintiff's injury in the North Sea that was a "necessary prerequisite" to the injury suffered in the United States domestic market. *Id. at 422-25*. Because the [\*13] plaintiff failed to show that the effect on United States commerce gave rise to the plaintiff's claim, the Fifth Circuit dismissed the action for lack of subject matter jurisdiction. *Id. at 427*. The court emphasized that [HNG](#) the existence of a single, global conspiracy did not relieve the plaintiff's burden of satisfying the FTAIA. Instead, the plaintiff must allege that its injury arose from the conspiracy's proscribed effects on United States commerce. *Id. at 427 n. 24*.

The allegations in the Amended Complaint distinguish this case from both [Associated General Contractors](#) and [Den Norske](#). Plaintiffs allege that Defendants' anti-competitive conduct adversely affected United States commerce and that their injury was inextricably intertwined with the injury Defendants inflicted on the United States market. Specifically, Plaintiffs allege that prices in the United States were directly and substantially linked with the prices Plaintiffs paid and that Defendants' unlawful conduct deliberately prevented Plaintiffs from purchasing MSG and nucleotides from the United States. (Am. Compl. PP 41, 43.) In addition, Plaintiffs allege that the adverse domestic effect of Defendants' [\*14] anti-competitive conduct was "necessary to achieve Plaintiffs' injuries abroad." (*Id.* P 56.) They reason that Defendants could not have maintained their international price fixing cartel -- and therefore Plaintiffs would not have suffered their foreign injuries -- without the adverse effect on United States commerce. In addition, Plaintiffs contend that if the cartel had not affected the United States market, Plaintiffs would have obtained MSG and/or nucleotides from the United States market at competitive prices. (*Id.*)

These allegations aver a far more direct causal relationship between the domestic effect and Plaintiffs' injury than [Associated General Contractors](#), [Den Norske](#), and other cases where the plaintiffs allegedly suffered foreign injury independent of domestic harm. Cf. [Eurim-Pharm v. Pfizer Inc., 593 F. Supp. 1102, 1106-07 \(S.D.N.Y. 1984\)](#) (motion to dismiss for lack of subject matter jurisdiction granted when plaintiff failed to allege that defendants' alleged foreign price-fixing and market allocation scheme resulted in an anti-competitive effect on United States commerce

or any facts demonstrating a causal connection between the defendants' [\*15] conduct in Europe and the price increase in United States), with [MM Global Servs., 329 F. Supp. at 342](#) (subject matter jurisdiction exists when foreign plaintiffs injured abroad assert a causal connection between their injuries and the United States effects of defendants' conduct). Accordingly, the Court finds that Plaintiffs have alleged a sufficient link between the domestic effect caused by Defendants' anti-competitive conduct and Plaintiffs' injury.

### 3. Policy Considerations

Defendants also argue that the Court should dismiss this action for comity considerations. [HN7](#)[] The FTAIA does not preclude the application of comity as a basis upon which to assert jurisdiction over foreign conduct, even where that conduct might otherwise be determined to have a direct, substantial and reasonably foreseeable anti-competitive effect on United States commerce. [Hartford Fire Ins. Co. v. California, 509 U.S. 764, 798, 125 L. Ed. 2d 612, 113 S. Ct. 2891 \(1993\)](#); see also H.R. Rep. 97-686, 1982 WL 25066, at \*13 ("If a court determines that the requirements for subject matter jurisdiction are met, this bill would have no effect on the court's ability to employ notions of comity . . . [\*16] . or otherwise to take account of the international character of the transaction.").

Indeed, the Supreme Court greatly considered the issue of comity in *Empagran*:

[HN8](#)[] This Court ordinarily construes ambiguous statutes to avoid unreasonable interference with the sovereign authority of other nations . . . This rule of statutory construction cautions courts to assume that legislators take account of the legitimate sovereign interests of other nations when they write American laws. It thereby helps the potentially conflicting laws of different nations work together in harmony -- a harmony particularly needed in today's highly interdependent commercial world.

[HN9](#)[] No one denies that America's antitrust laws, when applied to foreign conduct, can interfere with a foreign nation's ability independently to regulate its own commercial affairs. But our courts have long held that application of our antitrust laws to foreign anticompetitive conduct is nonetheless reasonable, and hence consistent with principles of prescriptive comity, insofar as they reflect a legislative effort to redress domestic injury that foreign anticompetitive conduct has caused.

[124 S. Ct. at 2366.](#) [\*17] Ultimately, the Supreme Court found it unreasonable to apply United States antitrust laws to foreign conduct insofar as that conduct causes independent foreign harm and that foreign harm alone gives rise to the plaintiff's claim. [Id. at 2367.](#)

Defendants piggyback on the reasoning in *Empagran* and argue that finding subject matter jurisdiction in this case would unjustifiably interfere with foreign sovereigns' antitrust enforcement systems. Specifically, Defendants note that the application of American private treble-damages remedies to anti-competitive conduct taking place abroad has generated significant controversy. See [id. at 2368](#) (courts should not allow private foreign entities to come to the United States and "bypass their own less generous remedial schemes, thereby upsetting a balance of competing considerations that their own domestic antitrust laws embody").

However, the policy concerns reflected in *Empagran* are not present in this case, where Plaintiffs allege that the foreign harm they suffered was inextricably related to the anti-competitive conduct's effect on domestic commerce. Indeed, the *Empagran* court limited its invocation [\*18] of comity to cases where "foreign conduct . . . causes independent foreign harm and that foreign harm alone gives rise to the plaintiff's claim." [Id. at 2367](#) (emphasis added); see also [Hartford Fire Ins. Co., 509 U.S. at 796](#) [HN10](#)[] ("It is well established by now that the Sherman Act applies to foreign conduct that was meant to produce and did in fact produce some substantial effect in the United States"). Furthermore, legislative history indicates that Congress intended to apply the [Sherman Act](#) to international cartel activity that impacted United States commerce:

[HN11](#)[] Any major activities on an international cartel would likely have the requisite impact on United States commerce to trigger United States subject matter jurisdiction. For example, if a domestic export cartel were so strong as to have a "spillover" effect on commerce within this country -- by creating a world-wide shortage or

artificially inflated world-wide price that had the effect of raising domestic prices -- the cartel's conduct would fall within the reach of our antitrust laws. Such an impact would, at least over time, meet the test of a direct, substantial and reasonably foreseeable [\*19] effect on domestic commerce.

H.R. Rep. 97-686, 1982 WL 25066, at \*13.

In addition to the comity considerations, the Court notes that Plaintiffs allege that Defendants were keenly aware that they had to include the United States in their cartel to extract cartel profits throughout the world. [HN12](#) [↑] American antitrust law is based on the principle that deterrence will be effective only if conspirators' anticipated sanctions exceed their potential profits. As the Supreme Court explained in [Pfizer, Inc. v. Government of India, 434 U.S. 308, 54 L. Ed. 2d 563, 98 S. Ct. 584 \(1978\)](#):

To deny a foreign plaintiff injured by an antitrust violation the right to sue would defeat these purposes. It would permit a price fixer or a monopolist to escape full liability for his illegal actions and would deny compensation to certain of his victims, merely because he happens to deal with foreign customers.

Moreover, an exclusion of all foreign plaintiffs would lessen the deterrent effect of treble damages. The conspiracy alleged by the respondents in this case operated domestically as well as internationally. If foreign plaintiffs were not permitted to seek a remedy for their antitrust injuries, [\*20] persons doing business in both this country and abroad might be tempted to enter into anti-competitive conspiracies affecting American consumers in the expectation that the illegal profits they could safely extort abroad would offset any liability to plaintiffs at home. If, on the other hand, potential antitrust violators must take into account the full costs of their conduct, American consumers are benefitted by the maximum deterrent effect of treble damages upon all potential violators.

*Id. at 315.*

[HN13](#) [↑] As it relates to an international cartel, United States antitrust sanctions are ineffective at deterring anti-competitive conduct in the United States if they merely approximate the cartel's profits in the United States. To ensure that international cartels are truly deterred and deprived of the fruits of their illegality, United States antitrust laws must also apply to foreign injury. Thus, when the anti-competitive conduct of an international cartel adversely affects United States commerce, which in turn causes foreign injury, the foreign plaintiff may seek recourse under the United States antitrust laws. See H.R. 97-686, 1982 WL 25066, at \* [\*21] 13 ("Any major activities of an international cartel would likely have the requisite impact on United States commerce to trigger United States subject matter jurisdiction").

## C. Standing

Defendants also maintain that Plaintiffs lack antitrust standing and therefore fail to state a claim upon which relief may be granted. Specifically, Defendants contend that Plaintiffs' harm is too remote and is not the type of injury covered by United States antitrust law. Defendants also submit that Plaintiffs are not the proper party to bring this action.

[HN14](#) [↑] To establish standing, Plaintiffs "must prove more than injury casually linked to an illegal presence in the market. Plaintiffs must prove an antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful." [Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 \(1977\)](#); see also [Assoc. Gen. Contractors, 459 U.S. at 538-45](#) (setting forth factors to determine whether a plaintiff lacks antitrust standing). In addition, Plaintiffs must establish that there was proximate causation between their harm and [\*22] the alleged illegal market restraint. [Int'l Travel Arrangers v. Northwest Airlines, Inc., 723 F. Supp. 141, 149 \(Magnuson, J.\)](#). Thus, if Plaintiffs' injuries are too remote and damages are too speculative, Plaintiffs will fail to satisfy the standing requirement. [Int'l Travel Arrangers, 723 F. Supp. at 149-50; see also de Atucha v. Commodity Exch., Inc., 608 F. Supp. 510, 518 \(S.D.N.Y. 1985\)](#) (plaintiff lacked standing because the alleged relationship between the plaintiff's injury and United States effects was too attenuated to allow the antitrust claim; any recovery for a foreign injury would not accurately reflect congressional intent).

Plaintiffs allege that they were direct purchasers of overpriced MSG and/or nucleotides who were forced to pay inflated prices abroad because Defendants' conspiracy prevented them from buying competitively priced MSG and/or nucleotides from the United States. Plaintiffs also allege that the injury was direct and was specifically intended by Defendants. Accordingly, Plaintiffs have sufficiently alleged that their injury arose from the United States effects of Defendants' anti-competitive actions. [\*23] Moreover, although the Court believes that damages will be difficult and complex in this case, they are not too speculative as to deny standing. Finally, Plaintiffs are proper enforcers of the antitrust laws since domestic direct purchasers cannot bring a claim to disgorge Defendants' overseas profits and domestic indirect purchasers would lack standing. See *III. Brick Co. v. State of Ill.*, 431 U.S. 720, 737-38, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977). Considering all of these factors, the Court finds that Plaintiffs have standing to bring their claims.

## CONCLUSION

Plaintiffs have craftily plead the Amended Complaint to allege a claim based upon the alternative theory recognized by the United States Supreme Court in *F. Hoffmann-La Roche Ltd. v. Empagran, S.A.*, 124 S. Ct. 2359 (2004). They have sufficiently alleged that Defendants' anti-competitive conduct had a "direct, substantial, and reasonably foreseeable effect" on United States commerce, and that Plaintiffs' harm is directly related to the adverse domestic effect. In addition, Plaintiffs have sufficiently set forth allegations to establish antitrust standing. Accordingly, **IT IS HEREBY ORDERED THAT:**

1. [\*24] Defendants' Motion to Dismiss (Clerk's Doc. No. 532) is **DENIED**; and
2. The parties shall conduct discovery exclusively relating to the alleged nexus between the domestic effects of Defendants' anti-competitive and Plaintiffs' alleged harm.

Dated: May 2, 2005

s/ Paul A. Magnuson

Paul A. Magnuson

United States District Court Judge

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## Bassett v. NCAA

United States District Court for the Eastern District of Kentucky

May 3, 2005, Decided

Civil Action No. 5:04-425-JMH

**Reporter**

2005 U.S. Dist. LEXIS 17570 \*; 2005-01 Trade Cas. (CCH) P74,822

CLAUDE L. BASSETT, Plaintiff, v. THE NATIONAL COLLEGIATE ATHLETIC ASSOCIATION, THE SOUTHEASTERN CONFERENCE, and THE UNIVERSITY OF KENTUCKY ATHLETIC ASSOCIATION, Defendants.

**Subsequent History:** Motion denied by [Bassett v. NCAA, 2005 U.S. Dist. LEXIS 39660 \(E.D. Ky., Nov. 8, 2005\)](#)

Affirmed by [Bassett v. Ncaa, 2008 U.S. App. LEXIS 12248 \(6th Cir.\) \(6th Cir. Ky., 2008\)](#)

## **Core Terms**

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allegations, antitrust, motion to dismiss, coaching, resignation, fraud claim, football, prospective contractual relation, civil conspiracy, Defendants', interview, Athletic, tape, antitrust violation, conspiracy, schools, ban

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN1 Motions to Dismiss, Failure to State Claim**

A motion to dismiss pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#) tests the sufficiency of the complaint.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### **HN2 Motions to Dismiss, Failure to State Claim**

Under the liberal notice pleading rules, a complaint need only put a party on notice of the claim being asserted against it to satisfy the federal rule requirement of stating a claim upon which relief can be granted. [Fed. R. Civ. P. 8\(a\)](#).

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN3** Motions to Dismiss, Failure to State Claim

A federal court may dismiss a complaint only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN4** Motions to Dismiss, Failure to State Claim

A court ruling on a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss must construe the complaint in the light most favorable to the plaintiff and accept as true all well-pleaded factual allegations.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN5** Motions to Dismiss, Failure to State Claim

Construing the complaint in the light most favorable to the petitioner, dismissal is proper only if it appears beyond doubt that the petitioner can prove no set of facts in support of his claims that would entitle him to relief."

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > General Overview

### **HN6** Heightened Pleading Requirements, Fraud Claims

The United States Court of Appeals for the Sixth Circuit interprets [Fed. R. Civ. P. 9\(b\)](#) as requiring plaintiffs to allege the time, place, and content of the alleged misrepresentation on which he or she relied; the fraudulent scheme; the fraudulent intent of the defendants; and the injury resulting from the fraud. While [Rule 9\(b\)](#) requires the circumstances constituting fraud or mistake to be stated with particularity, malice, intent, knowledge, and other condition of mind of a person may be averred generally. [Fed. R. Civ. P. 9\(b\)](#).

Antitrust & Trade Law > Sherman Act > General Overview

### **HN7** Antitrust & Trade Law, Sherman Act

See [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

### **HN8** Price Fixing & Restraints of Trade, Horizontal Refusals to Deal

While [§ 1](#) of the Sherman Act, [15 U.S.C.S. § 1](#), says "every," the United States Supreme Court has long held that Congress intended to outlaw only "unreasonable" restraints of trade.

Antitrust & Trade Law > ... > Private Actions > Standing > Clayton Act

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Clayton Act > Claims

Antitrust & Trade Law > Clayton Act > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > Damages

Antitrust & Trade Law > Regulated Practices > Private Actions > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > Prioritizing Resources & Organization for Intellectual Property Act

## [HN9](#) [+] Standing, Clayton Act

Section 4 of the Clayton Act creates a private cause of action for **antitrust law** violations and provides treble damages to any person injured in his business or property by reason of anything forbidden in the antitrust laws. [15 U.S.C.S. § 15](#).

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > Colleges & Universities

Antitrust & Trade Law > Sherman Act > General Overview

## [HN10](#) [+] Higher Education & Professional Associations, Colleges & Universities

By its plain language, [§ 1](#) of the Sherman Act, [15 U.S.C.S. § 1](#), only applies to the alleged antitrust violation if such violation is commercial in nature.

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > Colleges & Universities

Education Law > Intercollegiate & Interscholastic Athletics > Athletic Associations

Antitrust & Trade Law > Regulated Industries > General Overview

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## [HN11](#) [+] Higher Education & Professional Associations, Colleges & Universities

Some National Collegiate Athletic Association (NCAA) rules have been held to be commercial in nature and thus subject to antitrust scrutiny. Other NCAA rules, however, have been found to further the NCAA's noncommercial objectives; courts have held that the Sherman Act does not apply to these rules.

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > Colleges & Universities](#)

[Antitrust & Trade Law > Regulated Industries > Sports > General Overview](#)

[Antitrust & Trade Law > Regulated Industries > General Overview](#)

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Education Law > Intercollegiate & Interscholastic Athletics > Athletic Associations](#)

#### **[HN12](#) [+] Higher Education & Professional Associations, Colleges & Universities**

For purposes of the Sherman Act, the National Collegiate Athletic Association's Two-in-Four rule is commercial in nature as it regulates games that constitute sources of revenue for both member schools and promoters.

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > Colleges & Universities](#)

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

#### **[HN13](#) [+] Higher Education & Professional Associations, Colleges & Universities**

The Sherman Act does not apply to the National Collegiate Athletic Association's promulgation of eligibility requirements.

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > Colleges & Universities](#)

[Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview](#)

[Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

#### **[HN14](#) [+] Higher Education & Professional Associations, Colleges & Universities**

To state a claim for an antitrust violation, a plaintiff must allege an antitrust injury in his complaint. An "antitrust injury" is an (1) injury of the type the antitrust laws were intended to prevent and an (2) injury that flows from that which makes defendants' acts unlawful. Because the purpose of the antitrust laws is to protect competition rather than competitors, a plaintiff must allege injury, not only to himself, but to a relevant market. Thus, failure to allege an anticompetitive impact on a relevant market amounts to a failure to allege an antitrust injury.

Torts > Business Torts > Fraud & Misrepresentation > General Overview

## **HN15** [ ] **Business Torts, Fraud & Misrepresentation**

A viable fraud claim under Kentucky law requires that the defendant (a) made a material misrepresentation; (b) which was false; (c) which was known to be false or made recklessly; (d) which was made with inducement to be acted upon; (e) which plaintiff acted in reliance upon; and (f) which caused plaintiff injury.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## **HN16** [ ] **Motions to Dismiss, Failure to State Claim**

In order to survive a motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#), a plaintiff's complaint must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory.

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

Torts > Business Torts > Fraud & Misrepresentation > General Overview

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > General Overview

## **HN17** [ ] **Heightened Pleading Requirements, Fraud Claims**

Under [Fed. R. Civ. P. 9\(b\)](#), a complaint alleging fraud must allege with particularity those circumstances constituting fraud.

Civil Procedure > ... > Joinder of Parties > Compulsory Joinder > Indispensable Parties

Civil Procedure > Parties > General Overview

Civil Procedure > Parties > Joinder of Parties > General Overview

Civil Procedure > ... > Joinder of Parties > Compulsory Joinder > Necessary Parties

## **HN18** [ ] **Compulsory Joinder, Indispensable Parties**

[Fed. R. Civ. P. 19](#) provides a three-part test. First, the court determines whether a party should be joined (i.e., whether the party is necessary under [Rule 19\(a\)](#)). If so, the court asks whether joinder is feasible. If it is, the party is to be joined. If not, the court determines under [Rule 19\(b\)](#) whether "in equity and good conscience," the action should continue without him or be dismissed (i.e., whether the party is indispensable).

Civil Procedure > ... > Joinder of Parties > Compulsory Joinder > Necessary Parties

### [HN19](#) [blue icon] Compulsory Joinder, Necessary Parties

Fed. R. Civ. P. 19(a) states that a person is "necessary" and should be joined as a party if, in the person's absence complete relief cannot be accorded among those already parties. Fed. R. Civ. P. 19(a)(1).

Civil Procedure > ... > Joinder of Parties > Compulsory Joinder > Necessary Parties

### [HN20](#) [blue icon] Compulsory Joinder, Necessary Parties

A party is not "necessary" where it has not claimed an interest in the outcome of an action and complete relief can be ordered in its absence.

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

Torts > ... > Concerted Action > Civil Conspiracy > Elements

Torts > ... > Concerted Action > Civil Conspiracy > General Overview

### [HN21](#) [blue icon] Conspiracy, Elements

A viable cause of action for civil conspiracy requires that a plaintiff prove an unlawful/corrupt combination or agreement between the alleged conspirators to do by some concerted action an unlawful act.

Governments > Legislation > Statute of Limitations > Time Limitations

Torts > ... > Concerted Action > Civil Conspiracy > Defenses

Governments > Legislation > Statute of Limitations > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > Elements

### [HN22](#) [blue icon] Statute of Limitations, Time Limitations

Ky. Rev. Stat. Ann. § 413.140(1)(c) prescribes a one-year statute of limitations for civil conspiracy. This statute begins to run at the commission of the last act in furtherance of the conspiracy.

Torts > ... > Commercial Interference > Contracts > General Overview

### [HN23](#) [blue icon] Commercial Interference, Contracts

Kentucky law recognizes the tort of intentional interference with contractual relations as articulated in the Restatement (Second) of Torts § 766B.

Torts > ... > Prospective Advantage > Intentional Interference > Elements

Torts > ... > Commercial Interference > Contracts > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

#### **HN24** [blue icon] **Intentional Interference, Elements**

One who intentionally and improperly interferes with another's prospective contractual relation (except a contract to marry) is subject to liability to the other for the pecuniary harm resulting from loss of the benefits of the relation, whether the interference consists of (a) inducing or otherwise causing a third person not to enter into or continue the prospective relation or (b) preventing the other from acquiring or continuing the prospective relation.

Torts > ... > Prospective Advantage > Intentional Interference > Elements

Torts > ... > Commercial Interference > Contracts > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

#### **HN25** [blue icon] **Intentional Interference, Elements**

Thus, to set forth a cognizable claim for tortious interference with prospective contractual relations, a plaintiff must allege that the defendant intentionally and improperly interfered with his prospective contractual relations.

**Counsel:** [\*1] For Claude L. Bassett, Plaintiff: Joseph Edward Conley, Jr., Buechel & Conley - Crestview Hills, Crestview Hills, KY.; Rasheed A. Simmonds, Robert R. Furnier, Suraj J. Bhakta, Furnier & Thomas, LLP, Cincinnati, OH.

For National Collegiate Athletic Association, Defendant: Edward H. Stopher, Scott Allen Davidson, Boehl, Stopher & Graves, Louisville, KY.

For Southeastern Conference, Defendant: Katherine Gordon Maynard, Mark W. Merritt, Robert W. Fuller, III, Robinson, Bradshaw & Hinson, Charlotte, NC.

For University of Kentucky Athletic Association, Defendant: Douglas L. McSwain, Sarah Charles Wright, Stephen Lewis Barker, Kevin G. Henry, Sturgill, Turner, Barker & Moloney PLLC, Lexington, KY.

**Judges:** Joseph M. Hood, United States District Judge.

**Opinion by:** Joseph M. Hood

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

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This matter is before the Court on Defendants' motions to dismiss [Record Nos. 5, 7, and 9 respectively]. Plaintiff filed an omnibus memorandum in response to Defendants' motions to dismiss [Record No. 22/23], and each of the Defendants have replied [Record Nos. 31, 32, and 33 respectively]. Accordingly, this matter is now ripe for decision.

## FACTUAL BACKGROUND

[\*2] Plaintiff, Claude Bassett ("Bassett"), resigned from his position as assistant coach/recruiting coordinator for the University of Kentucky football team on November 19, 2000. He was employed by the University of Kentucky Athletic Association ("UKAA"). The catalyst for Bassett's resignation were allegations of impropriety relating to alleged National Collegiate Athletic Association ("NCAA") Rules violations.

On November 19, 2000, the University of Kentucky's Athletic Director, Larry Ivy, confronted Coach Bassett with allegations of impropriety. At the end of the meeting, Ivy gave Bassett a choice: (a) resign and, in exchange, no further action would be taken on the allegations made against him, or (b) face an investigation, potential criminal prosecution, and sure dismissal. In his complaint, Bassett claims he resigned believing that his resignation would end any further inquiry into his conduct and avoid the scandal that ultimately ensued. In resigning, Bassett asserts that he lost the due process protections enjoyed by athletics department employees subject to disciplinary action. Bassett claims that, had he known the University of Kentucky ("UK") would initiate a NCAA inquiry, [\*3] he never would have resigned.

The day after Bassett's resignation, on November 20, 2000, UK publicly disclosed that Bassett, along with several other assistants in the football program, had been fired. That day, UK made the decision to conduct an internal investigation of its football program for possible NCAA Rules violations. UK notified the NCAA Enforcement Services of the dismissals and of its intent to investigate. With the assistance of the Southeastern Conference ("SEC") Commissioner, UK undertook an investigation that lasted through February 2001. Meanwhile, through counsel, Bassett contacted the UK Compliance Officer, Sandy Bell ("Bell"), requesting that a meeting be arranged between Bassett and UK officials to discuss the allegations against him. This request was declined.

On January 4, 2001, Coach Bassett was interviewed; present were Bell, SEC Commissioner Roy Kramer, and SEC investigator Bill Seviers. Bassett consented to the request that his interview be tape-recorded. Bassett claims he was assured a copy of the tape. At the end of the first day, Bassett was told that, pursuant to NCAA Rules, he had a 24-hour window to reconsider his responses and submit to another [\*4] interview to correct any discrepancies. The next day, January 5, 2001, Bassett returned to correct his prior testimony, again allowing his interview to be tape-recorded.

Bassett claims that when he tried to obtain his interview tape UK Compliance Officer, Bell, disputed ever having promised him a copy. Moreover, Bassett claims Bell indicated to him that all taped interviews of witnesses were solely in the SEC's possession. When Bassett requested the SEC provide him with a copy of his taped interview, the SEC said they would make the tape available to him at a law firm located in Lexington, Kentucky. Bassett claims that, due to his limited resources, sending his counsel to Lexington, Kentucky to listen to a tape was a "luxury he could not afford."

On February 28, 2001, UK submitted the results of its internal investigation to the NCAA enforcement staff. In response, on March 30, 2001, the NCAA forwarded a preliminary inquiry to UK. NCAA enforcement staff later issued letters of official inquiry to Bassett, UK, and former head football coach Hal Mumme. Bassett's counsel responded to the allegations contained in the official inquiry by letter dated October 12, 2001. The letter stated [\*5] that,

because of financial constraints, Coach Bassett will be unable to appear before the NCAA Division I Committee on Infractions during its November 16-18, 2001 meeting when this matter will be considered. This letter will, hence, be his only response to the allegations barring any further NCAA inquiry with new allegations or request for additional explanation or information.

The NCAA released its Infractions Report on January 31, 2002. UK appealed one of the penalties imposed by the NCAA Division I Committee on Infractions - the imposition of a ban on post-season competition by the UK football team following the 2002 season - to the NCAA Division I Infractions Appeals Committee. On September 7, 2002, the Appeals Committee concluded that the ban was not excessive or inappropriate and affirmed the penalties imposed by the Committee on Infractions.

More than two years later, on September 17, 2004, Bassett filed a complaint against the NCAA, the SEC, and the UKAA alleging antitrust violations, fraud, civil conspiracy, and tortious interference with prospective contractual relations.

## STANDARD OF REVIEW

**HN1**<sup>1</sup> A motion to dismiss pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#) [\*6] tests the sufficiency of the complaint. Thus, **HN2**<sup>1</sup> under the liberal notice pleading rules, a complaint need only put a party on notice of the claim being asserted against it to satisfy the federal rule requirement of stating a claim upon which relief can be granted. [Fed. R. Civ. P. 8\(a\); Swierkiewicz v. Sorema N.A., 534 U.S. 506, 508, 152 L. Ed. 2d 1, 122 S. Ct. 992, \(2002\)](#) (holding that **HN3**<sup>1</sup> a court may dismiss a complaint only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations). **HN4**<sup>1</sup> A court must construe the complaint in the light most favorable to the plaintiff and accept as true all well-pleaded factual allegations. [Cooper v. Parrish, 203 F.3d 937, 944 \(6th Cir. 2000\)](#). **HN5**<sup>1</sup> Construing the complaint in the light most favorable to the petitioner, dismissal is proper only if "it appears beyond doubt that the [petitioner] can prove no set of facts in support of [his] claims that would entitle [him] to relief." [Forest v. United States Postal Serv., 97 F.3d 137, 139 \(6th Cir. 1996\)](#) (quoting [American Eagle Credit Corp. v. Gaskins, 920 F.2d 352, 353 \(6th Cir. 1990\)](#)). [\*7]

UKAA and the SEC also argue that Plaintiff's fraud claim should be dismissed pursuant to [Fed. R. Civ. P. 9\(b\)](#) for failing to plead with the requisite particularity. **HN6**<sup>1</sup> The Sixth Circuit interprets [Rule 9\(b\)](#) as requiring plaintiffs to "allege the time, place, and content of the alleged misrepresentation on which he or she relied; the fraudulent scheme; the fraudulent intent of the defendants; and the injury resulting from the fraud." [Coffey v. Foamex L.P., 2 F.3d 157, 161-162 \(6th Cir. 1993\)](#) (quotation omitted). While [Rule 9\(b\)](#) requires the circumstances constituting fraud or mistake to be stated with particularity, "malice, intent, knowledge, and other condition of mind of a person may be averred generally." [Fed. R. Civ. P. 9\(b\)](#).

## DISCUSSION

### I. Count I: Antitrust

Bassett's first claim, and purported basis for jurisdiction in federal court, accuses the NCAA, the SEC, and the UKAA of conspiring to prevent him from coaching at any of the NCAA's member schools. This conspiracy, Bassett alleges, violates the Sherman Antitrust Act, [15 U.S.C. § 1-2](#), and the Clayton [\*8] Act, [15 U.S.C. § 15](#), as it amounts to an unlawful group boycott.

**HN7**<sup>1</sup> [Section 1 of the Sherman Act](#) provides that, "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." [15 U.S.C. § 1](#).<sup>1</sup> **HN8**<sup>1</sup> While the statute says "every," the Supreme Court has long held that Congress intended to outlaw only "unreasonable" restraints. [State Oil Co. v. Khan, 522 U.S. 3, 10, 139 L. Ed. 2d 199, 118 S. Ct. 275 \(1997\)](#). The trade restraint alleged here is the group boycott of Bassett arising from NCAA imposed sanctions.

**HN10**<sup>1</sup> By its plain language, [Section One of the Sherman Act](#) only applies to the alleged antitrust violation [\*9] if such violation is commercial in nature. See [Worldwide Basketball & Sport Tours, Inc. v. NCAA, 388 F.3d 955, 958 \(6th Cir. 2004\)](#). Bassett claims that the antitrust violation alleged here, the alleged conspiracy to prevent him from coaching at any of the NCAA's member schools, arises from the NCAA's imposed sanctions. It is undisputed that

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<sup>1</sup> **HN9**<sup>1</sup> [Section 4 of the Clayton Act](#) creates a private cause of action for [antitrust law](#) violations and provides treble damages to any person "injured in his business or property by reason of anything forbidden in the antitrust laws." [15 U.S.C. § 15](#).

sanctions imposed on Bassett stemmed from the NCAA's enforcement of its rules governing recruiting, improper inducements, and academic fraud. Thus, in order for Section One of the Sherman Act to apply, the NCAA enforcement program, and the imposed sanctions arising therefrom, must be commercial in nature.

HN11[] Some NCAA rules have been held to be commercial in nature and thus subject to antitrust scrutiny. See Worldwide Basketball, 388 F.3d 955 (6th Cir. 2004) (finding that HN12[] the NCAA's Two in Four rule is commercial in nature as it regulates games that constitute sources of revenue for both member schools and promoters); National Collegiate Athletic Ass'n v. Board of Regents, 468 U.S. 85, 98, 82 L. Ed. 2d 70, 104 S. Ct. 2948 (1984) (finding NCAA's rules restricting television coverage of intercollegiate football games violated the Sherman Act). [\*10] Other NCAA rules, however, have been found to further the NCAA's noncommercial objectives; courts have held that the Sherman Act does not apply to these rules. See Smith v. NCAA, 139 F.3d 180, 186 (3d Cir. 1998) vacated on other grounds by NCAA v. Smith, 525 U.S. 459, 142 L. Ed. 2d 929, 119 S. Ct. 924 (1999) (finding that HN13[] the Sherman Act does not apply to the NCAA's promulgation of eligibility requirements).

Like the NCAA's eligibility rules, enforcement of the rules at issue here is not within the purview of antitrust law as it is not related to the NCAA's commercial or business activities. Rather than intending to provide the NCAA or any of its member schools with a commercial advantage, enforcement of rules governing recruiting, improper inducements, and academic fraud "primarily seek[s] to ensure fair competition in intercollegiate athletics." Id. at 185. Because the NCAA's enforcement program is not commercial in nature, sanctions arising therefrom do not constitute an illegal group boycott.

Moreover, even if the defendants' actions were subject the Sherman Act, Bassett's allegation of an antitrust violation still fails to state a claim upon which relief can be granted [\*11] as he has failed to allege an antitrust injury. HN14[] To state a claim for an antitrust violation, a plaintiff must allege an antitrust injury in his complaint. Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977). An "antitrust injury" is an (1) "injury of the type the antitrust laws were intended to prevent" and an (2) injury "that flows from that which makes defendants' acts unlawful." Id. Because the purpose of the antitrust laws is to protect competition rather than competitors, a plaintiff must allege injury, not only to himself, but to a relevant market. See Banks v. National Collegiate Athletic Ass'n, 977 F.2d 1081, 1087 (7th Cir. 1992); Brown Shoe Co. v. United States, 370 U.S. 294, 320, 8 L. Ed. 2d 510, 82 S. Ct. 1502 (1962). Thus, failure to allege an anti-competitive impact on a relevant market amounts to a failure to allege an antitrust injury. Id.

Bassett asserts, both in his complaint and in his response brief, that an alleged denial of due process caused him to be unjustly punished and that this amounts to an antitrust injury. The Court disagrees. At best, Bassett alleges injury to himself as a competitor in the marketplace and not [\*12] an injury to competition in a relevant market. Bassett's complaint fails to allege any anticompetitive effect on an identifiable market as a result of his being "banned" from coaching at NCAA schools. It is clear that the complaint alleges harm only to Bassett and not to competition itself. While, Bassett's response brief states that unjustified bans hurt competition among college football teams and create a competitive imbalance, he has not alleged any decrease in the supply or quality of coaching services, increase in the cost of coaching services, or any harm to consumers resulting from his punishment. In essence, he has not alleged *how* the college football coaching market, or the college football market, have suffered any anticompetitive effect by the application of facially neutral disciplinary rules. Bassett's conclusory allegations of an antitrust injury - unsupported by any factual allegations that resemble a cognizable antitrust claim - are insufficient.

In conclusion, the Court finds that Bassett's antitrust count must be dismissed for failure to state a claim on which relief can be granted.

## II. Count II: Fraud and Civil Conspiracy

Count II of Plaintiff's [\*13] complaint alleges that the three defendants engaged in fraud and civil conspiracy, precluding him from rejoining the college coaching ranks. Specifically, it alleges that UKAA and SEC employees lied

to Bassett in an effort to encourage him to take actions that would, and did, deprive him of certain due process guarantees, and that the NCAA relied upon knowingly tainted evidence to ban Bassett from college coaching. Defendants' assert that Bassett's complaint fails to allege facts sufficient to support these causes of action.

#### A. Fraud

[HN15](#) A viable fraud claim under Kentucky law requires that the defendant (a) made a material misrepresentation; (b) which was false; (c) which was known to be false or made recklessly; (d) which was made with inducement to be acted upon; (e) which plaintiff acted in reliance upon; and (f) which caused plaintiff injury. [Rivermont Inn, Inc. v. Bass Hotels & Resorts, Inc., 113 S.W.3d 636, 640 \(Ky. Ct. App. 2003\)](#). [HN16](#) In order to survive a motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#), a plaintiff's "complaint must contain either direct or inferential allegations respecting all the material elements [\*14] to sustain a recovery under some viable legal theory." [Glassner v. R.J. Reynolds Tobacco Co., 223 F.3d 343, 346 \(6th Cir. 2000\)](#) (quoting [Scheid v. Fanny Farmer Candy Shops, Inc., 859 F.2d 434, 436 \(6th Cir. 1988\)](#)). Furthermore, [HN17](#) under [Fed. R. Civ. P. 9\(b\)](#), "a complaint alleging fraud must allege with particularity those circumstances constituting fraud." [Glassner v. R.J. Reynolds Tobacco Co., 223 F.3d 343, 346 \(6th Cir. 2000\)](#) (citing [VanDenBroeck v. CommonPoint Mortg. Co., 210 F.3d 696, 701 \(6th Cir. 2000\)](#)).

##### 1. NCAA

The Court will first address the fraud claim as it applies to the NCAA. Simply, as a matter of law, Bassett's complaint fails to state a viable claim of fraud against the NCAA. None of the statements present in Bassett's complaint can possibly be construed as alleging one, much less all six, of the elements required under Kentucky law to state a cause of action for fraud against the NCAA. Bassett does not allege that the NCAA lied to him or that he acted in reliance upon any misrepresentation made by the NCAA. Moreover, in his response to the Defendants' motions to [\*15] dismiss, Bassett admits that his fraud claim focuses primarily upon the UKAA and the SEC. His claim of fraud against the NCAA consists only of an allegation that the NCAA relied on a distorted record to impose punishment. This allegation, on its own, is clearly insufficient to withstand the NCAA's [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss.

##### 2. SEC

Bassett's fraud claim against the SEC also fails. Bassett claims that the Defendants' fraudulent conduct encouraged him to take actions that deprived him of due process protections to which he was entitled as an employee of the UKAA, which, in turn, resulted in a disproportionate punishment. Assuming these allegations are true, which the Court must at this stage of the litigation, Bassett's complaint simply does not allege that the SEC caused any of his injuries. Bassett makes clear that his resignation is what led to his loss of due process protections. Bassett's complaint, however, does not allege that the SEC had any role in his resignation. Without allegations that the SEC had a role in the conduct causing Plaintiff his only alleged injuries, no fraud claim against the SEC can stand.

##### 3. [\*16] UKAA

Finally, the Court turns to Bassett's fraud claim as it applies to the UKAA. Bassett alleges that on November 19, 2000, acting on behalf of the UKAA, University of Kentucky Athletic Director Larry Ivy informed him that, if he resigned, no NCAA investigation would ensue. Bassett claims that, in reliance on this representation, he resigned and, in so doing, gave up his due process rights as a UKAA employee. Bassett seems to take the position that, as a result of this alleged fraud, he received an unjust punishment from the NCAA. These allegations set forth the elements required to state a common law fraud claim under Kentucky law.

The UKAA argues that, regardless of whether Bassett's complaint alleges the elements necessary to state a claim for fraud, his complaint must still be dismissed pursuant to [Fed. R. Civ. P. 19\(b\)](#), failure and inability to join an indispensable but immune party, to wit, the University of Kentucky. [HN18](#) Rule 19 provides a three-part test. First, the Court determines whether a party should be joined (*i.e.*, whether the party is necessary under [Rule 19\(a\)](#)). If so, the Court asks whether joinder is feasible. If it is, [\*17] the party is to be joined. If not, the Court determines

under [Rule 19\(b\)](#) whether "in equity and good conscience," the action should continue without him or be dismissed (i.e., whether the party is indispensable).

As it applies to the case *sub judice*, [HN19](#)<sup>↑</sup> [Rule 19\(a\)](#) states that a person is "necessary" and should be joined as a party if, "in the person's absence complete relief cannot be accorded among those already parties." [Fed. R. Civ. P. 19\(a\)\(1\)](#). Bassett claims that Ivy, acting on behalf of the UKAA, made a material misrepresentation upon which Bassett detrimentally relied. Accordingly, the wrong, if any, was committed by Ivy acting on behalf of Bassett's employer, the UKAA. If Bassett's fraud claim involves the University of Kentucky, it does so only tangentially as Bassett seeks nothing from the University. Thus, the UKAA has failed to show that, in the University's absence, complete relief cannot be accorded among those already parties.

In the alternative, Defendant UKAA argues that the University of Kentucky is a necessary party because disposition of the case in the University's absence may impair or impede the University's ability [\*18] to protect its interest. See [Fed. R. Civ. P. 19\(a\)\(2\)](#). The University, however, has not claimed an interest relating to the subject matter of the action *sub judice*. [HN20](#)<sup>↑</sup> A party is not "necessary" where it has not claimed an interest in the outcome of an action and complete relief can be ordered in its absence. [Ferrofluidics Corp. v. Advanced Vacuum Components, Inc.](#), 968 F.2d 1463, 1472 (1st Cir. 1992).

Because the University of Kentucky is not a "necessary" party under [Fed. R. Civ. P. 19\(a\)](#), Defendant's motion to dismiss based on [Fed. R. Civ. P. 19\(b\)](#) fails.

## B. Civil Conspiracy

[HN21](#)<sup>↑</sup> A viable cause of action for civil conspiracy requires that a plaintiff prove "an unlawful/corrupt combination or agreement between the alleged conspirators to do by some concerted action an unlawful act." [James v. Wilson](#), 95 S.W.3d 875, 897 (Ky. Ct. App. 2002) (*citing* [Montgomery v. Milam](#), 910 S.W.2d 237, 239, 42 12 Ky. L. Summary 39 (Ky. 1995)).

Bassett's complaint accuses the NCAA of fraud not as a primary actor, but as a coconspirator. Assuming Bassett's [\*19] complaint alleges facts necessary to state a claim of civil conspiracy, it still must be dismissed on the grounds that it is barred by the applicable statute of limitations. [HN22](#)<sup>↑</sup> [KRS 413.140\(1\)\(c\)](#) prescribes a one-year statute of limitations for civil conspiracy. This statute begins to run at the commission of the last act in furtherance of the conspiracy. [District Union Local 227 v. Fleischaker](#), 384 S.W.2d 68 (Ky. Ct. App. 1964). Construing the complaint in the light most favorable to Bassett, the latest possible date of any act in furtherance of the alleged conspiracy was September 17, 2002, when the NCAA Infraction Appeals Committee issued its report and upheld the sanctions imposed by the Infractions Committee. Plaintiff, however, did not file his complaint until September 17, 2004, more than two years after the last alleged act. Accordingly, Bassett's claim for civil conspiracy is time-barred and must be dismissed pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#).

In Bassett's response to NCAA's motion to dismiss, he claims that the NCAA may also have liability for aiding and abetting. Nowhere in the complaint, [\*20] however, is there any allegation of aider and abettor liability. Because it was not plead, the Court will not engage in a legal analysis of liability under this theory of law.

## III. Count III: Tortious Interference

The Court now turns to Bassett's state law claim of tortious interference with prospective contractual relations. Bassett claims that the NCAA intentionally and improperly interfered with his prospective contractual relations insofar as it forbid NCAA member institutions from hiring him.

[HN23](#)<sup>↑</sup> Kentucky law recognizes the tort of intentional interference with contractual relations as articulated in the [Restatement \(Second\) of Torts § 766B](#):

**HN24**[] One who intentionally and improperly interferes with another's prospective contractual relation (except a contract to marry) is subject to liability to the other for the pecuniary harm resulting from loss of the benefits of the relation, whether the interference consists of

- (a) inducing or otherwise causing a third person not to enter into or continue the prospective relation or
- (b) preventing the other from acquiring or continuing the prospective relation.

*Cullen v. South East Coal Co., 685 S.W.2d 187, 189-90 (Ky. Ct. App. 1983).* [\*21] **HN25**[] Thus, to set forth a cognizable claim under this theory, Bassett must allege that the NCAA intentionally and improperly interfered with his prospective contractual relations. Bassett's complaint does this; it clearly states that, by forbidding its member institutions from hiring him, the NCAA intentionally and improperly interfered with Bassett's prospective contractual relations.

The NCAA sets forth many persuasive arguments in its motion to dismiss. Such arguments, however, are more properly geared toward a motion for summary judgment. At this time, the Court cannot dismiss Bassett's claim against the NCAA for intentional interference with his prospective contractual relations as he has alleged facts sufficient to support such a claim.

## CONCLUSION

Assuming as true the allegations set forth in Plaintiff's complaint,

## IT IS ORDERED,

- (1) that UKAA's motion to dismiss [Record No. 5] be, and the same hereby is, **GRANTED IN PART and DENIED IN PART;**
- (2) that Bassett's claim of fraud, found in Count II of his complaint, as it applies to the UKAA, survives the UKAA's motion to dismiss;
- (2) that NCAA's, motion to dismiss [Record No. 7] be, and the same hereby is, [\*22] **GRANTED IN PART and DENIED IN PART;**
- (3) that Count III of Bassett's complaint - tortious interference with prospective contractual relations - survives NCAA's motion to dismiss;
- (4) that SEC's motion to dismiss [Record No. 9] be, and the same hereby is, **GRANTED.**

This the 3rd day of May, 2005.

## Signed By:

**Joseph M. Hood**

**United States District Judge**



## Brennan v. Concord EFS, Inc.

United States District Court for the Northern District of California

May 4, 2005, Decided ; May 4, 2005, Filed

No C-04-2676 VRW

### **Reporter**

369 F. Supp. 2d 1127 \*; 2005 U.S. Dist. LEXIS 9243 \*\*; 2005-1 Trade Cas. (CCH) P74,815

PAMELA BRENNAN et al, Plaintiffs, v CONCORD EFS, INC et al, Defendants.

**Subsequent History:** Motion granted by [In re ATM Fee Antitrust Litig., 2005 U.S. Dist. LEXIS 36195 \(N.D. Cal., Dec. 5, 2005\)](#)

## **Core Terms**

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interchange, motion to dismiss, joint venture, banks, network, issuing bank, conspiracy, allegations, rule of reason, cooperative, plaintiffs', transactions, price fixing, horizontal, card, pleadings, realtor, fixing, zero, fair notice, defendants', subsidiary, antitrust, surcharge, entities, motions, procompetitive, withdrawals, ancillary, appears

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

### [HN1](#) [] Motions to Dismiss, Failure to State Claim

On a motion to dismiss, all well-pleaded allegations of material fact are taken as true and construed in a light most favorable to the non-moving party.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

### [HN2](#) [] Motions to Dismiss, Failure to State Claim

[Fed. R. Civ. P. 12\(b\)\(6\)](#) motions to dismiss essentially test whether a cognizable claim has been pleaded in the complaint.

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### [HN3](#) [] Complaints, Requirements for Complaint

Fed. R. Civ. P. 8(a) states that a plaintiff's pleadings must contain a short and plain statement of the claim showing that the pleader is entitled to relief, provides the standard for judging whether such a cognizable claim exists. This standard is a liberal one that does not require a plaintiff to set forth all the factual details of the claim; rather, all that the standard requires is that a plaintiff give the defendant fair notice of the claim and the grounds for making that claim. To this end, a plaintiff's complaint should set forth either direct or inferential allegations with respect to all the material elements of the claim.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

#### **HN4** [] Motions to Dismiss, Failure to State Claim

Under Fed. R. Civ. P. 12(b)(6), a complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of its claim which would entitle it to relief. All material allegations in the complaint must be taken as true and construed in the light most favorable to plaintiff.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Joint Contracts

Business & Corporate Law > Joint Ventures > General Overview

Mergers & Acquisitions Law > Antitrust > Joint Ventures

Antitrust & Trade Law > Exemptions & Immunities > Exempt Cartels & Joint Ventures

#### **HN5** [] Types of Contracts, Joint Contracts

Antitrust law doesn't frown on all joint ventures among competitors--far from it. If a joint venture benefits consumers and doesn't violate any applicable per se rules, it will often be perfectly legal.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Joint Contracts

Business & Corporate Law > Joint Ventures > Formation

Mergers & Acquisitions Law > Antitrust > Joint Ventures

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Exempt Cartels & Joint Ventures

Mergers & Acquisitions Law > Antitrust > Antitrust Statutes > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Business & Corporate Law > Joint Ventures > General Overview

#### **HN6** [] Types of Contracts, Joint Contracts

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"Joint venture" is not a mantra to escape per se analysis: It is not the case that the mere existence of a bona fide joint venture means that participating companies may use the enterprises to do anything they please with full immunity from per se analysis under [§ 1](#) of the Sherman Antitrust Act, [15 U.S.C.S. § 1](#), including price fixing. The issue with respect to legitimate joint ventures is whether the price fixing is "naked" (in which case the restraint is illegal) or "ancillary" (in which case it is not).

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## [HN7](#) Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

The core question of whether a restriction such as fixing automatic teller machines interchange fee is a "naked" restraint or an "ancillary" restraint is quintessentially one of fact.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Joint Contracts

Mergers & Acquisitions Law > Antitrust > Antitrust Statutes > General Overview

Business & Corporate Law > Joint Ventures > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## [HN8](#) Types of Contracts, Joint Contracts

The law is this: Horizontal restraints in the context of a procompetitive joint venture remain unlawful per se unless they are necessary to (or, in certain formulations, "reasonably ancillary to") the achievement of the joint venture's procompetitive benefits.

Evidence > Judicial Notice > General Overview

## [HN9](#) Evidence, Judicial Notice

Judicial notice at the pleadings stage is properly invoked to fill in a small gap in an otherwise complete portrait painted by the complaint.

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For Wells Fargo & Co., Wells Fargo Bank, N.A., Defendants: Donald Baker, Baker and Miller, Washington, DC; J. Thomas Rosch, Joshua N. Holian, Mark Jeremy Seifert, Latham & Watkins LLP, San Francisco, CA.

For Servus Financial Corp., Defendant: Joshua N. Holian, Mark Jeremy Seifert, Latham & Watkins LLP, San Francisco, CA.

**Judges:** VAUGHN R WALKER, United States District Chief Judge.

**Opinion by:** VAUGHN R WALKER

## **Opinion**

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### **[\*1128] ORDER**

In this putative class action, plaintiffs assert that defendants -- banks and other entities involved in the processing of withdrawals from automated teller machines (ATMs) in the "Star" ATM network ("Star") -- have engaged in horizontal price fixing declared illegal by section 1 of the Sherman Antitrust Act, [15 USC § 1](#). Plaintiffs argue that defendants' conduct is condemned *per se*; they disclaim any intention of proceeding on a rule of reason theory. Several defendants move to dismiss the complaint (or for judgment on the pleadings) on the ground that Star is a procompetitive cooperative joint venture subject only to rule of reason analysis. Doc # # 26, 29, **[\*\*4]** 42. Other defendants move to dismiss on the ground that the complaint does not sufficiently allege their involvement in setting the terms of Star's operations. Doc # # 17, 33.

I

**HN1** "On a motion to dismiss, all well-pleaded allegations of material fact are taken as true and construed in a light most favorable to the non-moving party." [Wyler Summit Partnership v Turner Broadcasting System, Inc, 135 F3d 658, 661 \(9th Cir 1998\)](#) (citing [Parks School of Business, Inc v Symington, 51 F3d 1480, 1484 \(9th Cir 1995\)](#)). Accordingly, what follows is drawn from plaintiffs' complaint (Doc # 1), taking its allegations as true.

As almost anyone who has an ATM card knows, withdrawals can be made from an account at one bank -- the bank that issues the ATM card (the "issuing bank") -- using an ATM owned by a third party (the "ATM owner"). Only

banks can issue ATM cards, but banks and non-banks alike can operate ATMs. Transactions in which the issuing bank is not the ATM owner -- known as "foreign ATM transactions" -- are mediated by an ATM network that connects the ATM to the issuing bank. One such network (the subject of this suit) is Star, which is owned by defendant **[\*\*5]** Concord EFS, Inc ("Concord EFS"); Concord EFS is a wholly owned subsidiary of First **[\*1129]** Data Corp ("First Data"). Compl (Doc # 1) P 8. Transactions in which the issuing bank is also the ATM owner -- known as "on us" transactions, see Doc # 26 at 6 n4 -- do not involve the ATM network; such transactions are not the subject of this suit.

Another thing that ATM cardholders know is that while "on us" transactions are typically free, foreign ATM transactions involve fees. First, there is the "ATM surcharge," which is typically displayed on the ATM screen and collected by the ATM owner as part of the cardholder's withdrawal. The ATM surcharge ranges from zero (offered as an promotional enticement by some ATM operators) to \$ 3.00 or more. Second, there is the "foreign ATM fee," which is assessed by the issuing bank and typically appears on the cardholder's bank statement as a fee. The foreign ATM fee ranges from zero (offered by banks that own few ATMs and are at a competitive disadvantage relative to banks that own many ATMs) to about \$ 2.00 (currently the fee charged by the large banks that are defendants here). Third, there is a "switch fee" on the order of \$ 0.05 paid by the issuing **[\*\*6]** bank to the ATM network (Star in this case) for the network's services in mediating a foreign ATM transaction. Fourth, there is an "interchange fee" of \$ 0.45 or \$ 0.55 paid by the issuing bank to the ATM owner for use of the foreign ATM. See Compl (Doc # 1) P 1 (defining fees); P 2 & Fig A (diagraming typical foreign ATM transaction); P 52 (describing current foreign ATM fees); P 57 (describing interchange fees).

This suit concerns the interchange fee, which is fixed by Star and applies to all foreign ATM transactions mediated by the network. Presently, the interchange fee is \$ 0.45 for on-bank-premise cash withdrawals and \$ 0.55 for off-bank-premise cash withdrawals. Id P 57. The interchange fee is supposedly passed on to plaintiffs -- ATM cardholders who have paid (or expect to pay) foreign ATM fees for transactions mediated by Star -- in the form of artificially inflated foreign ATM fees.

The complaint is somewhat fuzzy on Star's corporate constitution, but at a minimum, see id P 8, Star is controlled directly or indirectly via its board of directors by a host of large banks that are defendants in this case: Bank of America Corp ("B of A"); Bank One Corp; Bank One NA; J P **[\*\*7]** Morgan Chase & Co ("JPMorgan Chase"); Citibank (West) FSB ("Citibank"); SunTrust Banks, Inc ("SunTrust"); Wachovia Corp ("Wachovia"); Wells Fargo & Co; Wells Fargo Bank, NA; Servus Financial Corp ("Servus") (collectively, the "defendant banks"). The whirlwind of bank mergers and acquisitions in the last five years makes for quite a tangle of rights and liabilities, but the complaint clearly states that each of the defendant banks either (1) is entitled to appoint outside directors to the Star board of directors, or (2) controls or succeeded to the rights and liabilities of an entity that was so entitled. Id PP 9-14. (The one exception is Wachovia Bank NA, which appears in the complaint's caption but is mentioned nowhere in the complaint.) Through this control structure the defendant banks "have caused Star to continue to impose [i]nterchange [f]ees," from which the defendant banks benefit, both because they charge foreign ATM fees and because the defendant banks receive interchange fees to the extent they own ATMs. Id P 61.

Although the defendant banks control Star, an ATM network derives value from the participation of a large number of issuing banks and ATM owners -- indeed, **[\*\*8]** the complaint effectively concedes that Star is a joint venture that benefits consumers and fosters competition among issuing banks by allowing smaller banks that cannot afford to deploy a large number of **[\*1130]** ATMs nonetheless to compete with larger banks that do own many ATMs. Id P 49. As such, Star accepts as members issuing banks and ATM owners other than the defendant banks. Id P 50. Although bound by Star's network policies, those issuing banks and ATM owners have "virtually no role" in setting network policies; but the bank defendants "have a significant role in establishing network policies." Id. On information and belief, plaintiffs allege that "some or all of the [b]ank [d]efendants" serve on an advisory committee "with the authority to veto or propose operating rules for the network and external [interchange rates and fees payable between or passed to network participants." Id P 58. Although plaintiffs implicitly concede that some horizontal restraints are necessary to create Star and thereby benefit consumers, plaintiffs contend that "[i]mposing fixed [i]nterchange [f]ees is unnecessary to Star operations." Id P 64.

Plaintiffs seek both damages (for past payment of [\*\*9] putatively inflated foreign ATM fees) and an injunction (against future fixing of interchange fees). Plaintiffs propose to proceed on behalf of four classes: two classes of California residents (one seeking retrospective damages relief; the other seeking injunctive relief), and two classes of non-California residents (seeking similar relief). Combined, those classes would roughly comprise all persons and business entities who (1) opened a bank account with a bank defendant and (2) either (a) paid a foreign ATM fee directly to a bank defendant or its affiliate or (b) currently have a bank account with a bank defendant.

## II

Several dispositive motions are now before the court. Some are motions to dismiss pursuant to [FRCP 12\(b\)\(6\)](#) for failure to state a claim upon which relief can be granted; some are motions for judgment on the pleadings pursuant to [FRCP 12\(c\)](#). The pertinent legal standard is the same. [\*In re World War II Era Japanese Forced Labor Litigation\*, 114 F Supp 2d 939, 944 \(ND Cal 2000\)](#) (citing [\*Enron Oil Trading & Transp Co v Walbrook Insurance Co\*, 132 F3d 526, 529 \(9th Cir 1997\)](#)). [\*\*10] aff'd sub nom [\*Deutsch v. Turner Corp.\*](#) 324 F.3d 692 (9th Cir 2003). Accordingly, the court will treat all pending motions under [FRCP 12\(b\)\(6\)](#) and refer to them as "motions to dismiss."

[HN2](#) [FRCP 12\(b\)\(6\)](#) motions to dismiss essentially "test whether a cognizable claim has been pleaded in the complaint." [\*Scheid v Fanny Farmer Candy Shops, Inc\*, 859 F2d 434, 436 \(6th Cir 1988\)](#). [HN3](#) [FRCP 8\(a\)](#), which states that a plaintiff's pleadings must contain "a short and plain statement of the claim showing that the pleader is entitled to relief," provides the standard for judging whether such a cognizable claim exists. [\*Lee v City of Los Angeles\*, 250 F3d 668, 679 \(9th Cir 2001\)](#). This standard is a liberal one that does not require a plaintiff to set forth all the factual details of the claim; rather, all that the standard requires is that a plaintiff give the defendant fair notice of the claim and the grounds for making that claim. [\*Leatherman v Tarrant County Narcotics Intell & Coord Unit\*, 507 US 163, 168, 122 L. Ed. 2d 517, 113 S. Ct. 1160 \(1993\)](#) (citing [\*Conley v Gibson\*, 355 US 41, 47, 2 L. Ed. 2d 80, 78 S. Ct. 99 \(1957\)](#)). [\*\*11] To this end, a plaintiff's complaint should set forth "either direct or inferential allegations with respect to all the material elements of the claim". [\*Wittstock v Van Sile, Inc\*, 330 F3d 899, 902 \(6th Cir 2003\)](#).

[HN4](#) Under [Rule 12\(b\)\(6\)](#), a complaint "should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of [its] claim which would entitle [it] to relief." [\*Hughes v Rowe\*, 449 US 5, 9, 11311 66 L. Ed. 2d 163, 101 S. Ct. 173 \(1980\)](#) (citing [\*Haines v Kerner\*, 404 US 519, 520, 30 L. Ed. 2d 652, 92 S. Ct. 594 \(1972\)](#)). See also [\*Conley\*, 355 US at 45-46](#). All material allegations in the complaint must be taken as true and construed in the light most favorable to plaintiff. See [\*In re Silicon Graphics Inc Sec Litig\*, 183 F3d 970, 980 n10 \(9th Cir 1999\)](#).

The court will first take up the bank defendants' motions to dismiss on the ground that plaintiffs do not state a claim for a per se violation of the antitrust laws. Then the court will turn to the individual motions by Bank One Corp and JPMorgan Chase and by First Data to dismiss for failure adequately to allege those entities' involvement in setting [\*\*12] Star's terms.

## A

Citibank and Suntrust (the "Citibank movants") (Doc # 26) and B of A, Bank One Corp, Bank One NA and JPMorgan Chase (the "B of A movants") (Doc # 29) move to dismiss the complaint for failure to state a per se antitrust claim. Although the bank defendants' memoranda in connection with these motions run several dozen pages, the nub of their argument is a simple syllogism: (1) Restraints in furtherance of procompetitive cooperative joint ventures are subject to rule of reason analysis, see, e.g., [\*Broadcast Music, Inc v Columbia Broadcasting System, Inc\*, 441 US 1, 60 L. Ed. 2d 1, 99 S. Ct. 1551 \(1979\)](#) ("BMI"); [\*National Collegiate Athletic Association v Board of Regents\*, 468 US 85, 82 L. Ed. 2d 70, 104 S. Ct. 2948 \(1984\)](#) ("NCAA"); (2) fixing the interchange fee is necessary to the existence of Star, the joint venture at issue; therefore (3) the fixing of the interchange fee should be analyzed under the rule of reason.

Defendants' logic is impeccable, but the syllogism's minor premise -- that fixing the interchange fee is necessary -- is an inherently factual contention that cannot properly be resolved on a motion to dismiss. In fact, plaintiffs have pled exactly the opposite: "Imposing [\*\*13] fixed [i]nterchange [f]ees is unnecessary to Star operations.

Interchange [f]ees neither create a product that would not exist absent the fees nor enhance or promote competition in the ATM market." Compl (Doc # 1) P 64. This is a factual contention and it is axiomatic that the court must accept it as true for purposes of the present motions. It is a plausible inference from plaintiffs' complaint, for example, that modern information technology could inexpensively automate competitive price setting among even the hundreds or thousands of Star members, making fixed interchange fees unnecessary to Star's existence. If plaintiffs are right, then horizontal price fixing is horizontal price fixing -- and it is beside the point that prices were fixed in the context of an otherwise-lawful joint venture.

The court must note at the outset that plaintiffs' challenge to the "fixed interchange fee" is susceptible of two interpretations, only one of which is the proper subject of a per se challenge. On the one hand, plaintiffs might seek to replace the \$ 0.45 or \$ 0.55 fee with a fee of \$ 0.00 -- a "zero fee," so to speak. This interpretation is suggested by the historical account of [\[\\*\\*14\]](#) interchange fees described in PP 49-60 of the complaint and the conclusion in P 62 that "the widespread adoption of [s]urcharges has eliminated any purported justification for [i]nterchange [f]ees." Under the "zero fee" argument, plaintiffs would contend that although interchange fees were necessary back when ATM owners had no other source of remuneration (that is, when surcharges were banned), interchange fees can now be set at zero because ATM owners can fend for themselves through surcharges. But to say that interchange fees should be abolished (the same thing as "set at zero") is to concede that [\[\\*1132\]](#) setting the interchange fee with certainty at some level is necessary to Star's existence -- which is fatal to plaintiffs' per se claim. (Indeed, such an argument is not an antitrust argument at all, for it amounts to a dispute over prices and competition law is not concerned with setting a proper price.) By contrast to the "zero fee" argument, plaintiffs do have a viable per se argument if what they seek is to permit competitive (e.g., bilateral) negotiation of interchange fees among issuing banks and ATM owners. The court proceeds -- as must plaintiffs to maintain a [\[\\*\\*15\]](#) per se case -- on the premise that a challenge to the "fixed interchange fee" is a challenge not to the fee's existence but to the fixed nature of the fee; that is, plaintiffs challenge the fixing of the interchange fee.

On that understanding, recent Ninth Circuit authority is squarely on plaintiffs' side. In [\*Freeman v San Diego Ass'n of Realtors, 322 F3d 1133 \(9th Cir 2003\)\*](#) (Kozinski, J), the Ninth Circuit considered a joint venture among several realtor associations to create a centralized multiple listing service (MLS) database. Access to the centralized MLS database, maintained by Sandicor, was sold to individual realtors, with the realtor associations providing billing services and technical support. Sandicor charged realtors \$ 44 per month; the realtor associations agreed that Sandicor would pay \$ 22.50 per month to each of them for each subscriber they supported. [\*Id. at 1146\*](#). The plaintiffs -- realtors who contended they were overpaying for MLS services -- brought suit to challenge the fixed \$ 22.50 price for support services. The Ninth Circuit held that the realtor associations' agreement to fix support services pricing was illegal [\[\\*\\*16\]](#) per se under [\*section 1 of the Sherman Act\*](#). [\*Id. at 1150-54\*](#). Indeed, the Ninth Circuit explicitly rejected the argument that "the inherent cooperative aspects of the MLS as a joint venture warrant more deferential review," explaining that "any elements of novelty and cooperation in the MLS are irrelevant to whether support fees are fixed or set competitively." [\*Id. at 1151\*](#). Put succinctly:

**HN5**  **Antitrust law** doesn't frown on all joint ventures among competitors -- far from it. If a joint venture benefits consumers and doesn't violate any applicable per se rules, it will often be perfectly legal. The decision to combine MLS databases fits comfortably within this category. The further decision to fix support fees does not.

[\*Id. at 1157\*](#) (citation omitted).

The same point is made in [\*Dagher v Saudi Refining, Inc, 369 F3d 1108 \(9th Cir 2004\)\*](#), petition for cert pending. Dagher concerned a joint venture between the oil refining and marketing companies Texaco and Shell; the joint venture included an agreement to fix prices in the retail market for gasoline produced under the joint venture. The Ninth Circuit summarized the question [\[\\*\\*17\]](#) presented and its holding:

The question we confront in this case \* \* \* is not whether two companies engaged in run-of-the-mill price fixing. Instead, the defendants have asked us to find an exception to the per se prohibition on price-fixing where two entities have established a joint venture that unifies their production and marketing function, yet: continue to sell their formerly competitive products as distinct brands. In doing so, the companies fixed the prices of these

two brands of gasoline, Texaco and Shell, by agreeing ex ante to charge the same price for each. We think the exception the defendants seek is inconsistent with the Sherman Act as it has been understood to date.

Id. at 1116. And again, the Ninth Circuit explained that HN6[ "joint venture" is not a mantra to escape per se analysis:

[\*1133] It is not the case \* \* \* that the mere existence of a bona fide joint venture means that participating companies may use the enterprises to do anything they please with full immunity from per se analysis under § 1, including price fixing. \* \* \* [T]he issue with respect to legitimate joint ventures is whether the price fixing is "naked" [\*18] (in which case the restraint is illegal) or "ancillary" (in which case it is not).

Id. at 1118 (citing Herbert Hovenkamp, XI Antitrust Law P 1908 (1998) ("[A] restraint is not saved from the 'naked' classification simply because it is included in some larger joint venture arrangement that is clearly efficient.")).

HN7[ The core question identified in Dagher -- whether a restriction such as fixing the interchange fee is a "naked" restraint or an "ancillary" restraint -- is quintessentially one of fact, and one that plaintiffs have pled in their favor in the complaint. If the restraint proves to be naked, it is subject to per se analysis and plaintiffs have stated a claim. Against these elementary propositions, the bank defendants offer several arguments, none of which persuades.

The B of A movants try to beg the question. See, e.g., Doc # 29 at 7:22-8:3 ("In the context of an arrangement like this, in which some form of agreement among the parties is necessary to permit the system to operate, it is well established \* \* \* that the per se doctrine does not apply."); id at 9:5 (referring to the fixed interchange fee as "one of the many rules that have [\*19] been adopted of necessity to make the network work"); id at 11:1-2 ("The challenged interchange fee is therefore plainly ancillary to a lawful joint enterprise \* \* \*"). These conclusory statements are, of course, insufficient to sustain a motion to dismiss.

The Citibank movants do somewhat better in arguing that "[w]ithout [the] advance certainty of obligation [that comes from a fixed interchange fee], no bank would agree to pay out money to individuals with whom it has no depository relationship" and that "there is no way that each member bank [or ATM owner, presumably,] possibly could reach agreement with each and every other bank about the terms on which they will make their machines available to each other." Doc # 26 4:3-5, 11-13. The Citibank movants also make a game theoretical argument that in the absence of a collective promise by the issuing banks to pay a minimum interchange fee to ATM owners, individually self-interested issuing banks would set foreign ATM fees so high that ATM owners would be unable to collect a surcharge large enough to entice them to enter the market -- and there would be no ATM service. See Doc # 115 at 6-7. Whatever the merits of these arguments, [\*20] they are intrinsically factual, contrary to plaintiffs' pleading and inappropriate for resolution at the motion to dismiss stage.

The bank defendants also rely on several cases to support their position, but they are distinguishable. For example, while BMI supports the bank defendants in stating that "[j]oint ventures and other cooperative arrangements are \* \* \* not usually unlawful," the BMI Court immediately added the caveat "at least not as price-fixing schemes where the agreement on price is necessary to market the product at all." 441 US at 23. Moreover, the "blanket license" to musical compositions offered by BMI was upheld as lawful by the Court not at the pleadings stage, but after an eight-week trial on the merits; it was this trial that established that "[a] middleman with a blanket license was an obvious necessity if the thousands of individual negotiations, a virtual impossibility, were to be avoided." Id. at 20.

[\*1134] Likewise, National Bancard Corp. (NaBanco) v. VISA U.S.A., Inc., 779 F.2d 592 (11th Cir 1986) ("NaBanco"), is distinguishable. There, the Eleventh Circuit based its rejection of a per se analysis on the fact that [\*21] the interchange fee between banks operating the Visa credit card payment system was a "necessary" term without which the system would not function." Id. at 602. And again, that conclusion rested on the district court's finding of fact following a nine-week bench trial that the interchange fee was "an agreement on the terms of interchange necessary for VISA to market its product and be an effective competitor." National Bancard Corp. (NaBanco) v. VISA U.S.A., Inc., 596 F. Supp. 1231, 1253 (SD Fla 1984).

NCAA is not especially helpful to the bank defendants in that it too followed an "extended trial," [468 US at 88](#), and ultimately held the restraints in question to violate the Sherman Act (albeit under a rule of reason analysis). NCAA supports the bank defendants in one respect, however: NCAA treated the question whether "the agreement on price is necessary to market the product at all" as germane to an efficiencies defense under a rule of reason analysis, see [id. at 113-15](#) (citing BMI), and (apparently) irrelevant to the threshold issue whether per se or rule of reason analysis governed the case, see [id. at 100-04](#). [\[\\*\\*22\]](#) This analytical reordering -- rarely if ever seen outside the context of sports leagues -- appears to be the product of the Court's pronouncement (again, following a lengthy trial) that "what is critical is that this case involves an industry in which horizontal restraints on competition are essential if the product is to be available at all." [Id. at 101](#). But a sports league, while appearing to be a joint venture of competitors (and on the field, they are), is really only one firm and cases involving the leagues may be essentially sui generis. See, e.g., Gary R. Roberts, Sports Leagues and the Sherman Act: The Use and Abuse of Section 1 to Regulate Restraints on Intraleague Rivalry, [32 UCLA L Rev 219 \(1984\)](#). For present purposes, it suffices to say that the ATM industry may be as exceptional as the televised college sports industry, but that is subject to proof by defendants.

The one case cited by the bank defendants that is both legally and procedurally on point is the decision by Judge White of this court in [Reyn's Pasta Bella LLC v Visa USA, Inc, 259 F Supp 2d 992 \(ND Cal 2003\)](#). In Reyn's, the court determined on a motion to dismiss [\[\\*\\*23\]](#) that a horizontal price fixing challenge to the fixing of credit card interchange fees should be analyzed under the rule of reason. Three reasons persuade this court not to follow Judge White's opinion in this case: First, the Reyn's court had the benefit of NaBanco's decision on a very similar (if not identical) set of credit card interchange fees; this court does not have analogous appellate authority with respect to the ATM interchange fee in this case. (Though similar in name, the interchange fees in the two industries are structurally rather different.) While perhaps not unflinchingly faithful to the Eleventh Circuit's analytical path in NaBanco and distinguishing that decision in certain respects, the Reyn's decision pragmatically took the same path as NaBanco in analyzing the credit card interchange fee under the rule of reason. Second, Reyn's did not have the benefit of Dagher and Freeman: Dagher was decided over a year after Reyn's, and although Freeman had issued only weeks before Reyn's, Reyn's does not cite Freeman, which may not have been brought to Judge White's attention. Third, Reyn's quotes the canonical language [\[\\*\\*24\]](#) from BMI -- that the rule of reason applies "where the agreement on price is necessary to market the product at all" -- [\[\\*1135\]](#) yet the analysis in Reyn's focuses entirely on whether the Visa payment system is a joint venture, and it ignores the "necessary" language of BMI. See [259 F Supp 2d at 1000](#).

In some respects, a better analogy to the case that plaintiffs have pled is a case not yet mentioned: [United States v Topco Associates, 405 US 596, 31 L. Ed. 2d 515, 92 S. Ct. 1126 \(1971\)](#). Topco was "a cooperative association of approximately 25 small and medium-sized regional supermarket chains." [Id. at 598](#). The cooperative procured and distributed to its members a variety of food and nonfood items, branded under various names owned by Topco. *Id.* As a buying cooperative, Topco's "very existence \* \* \* improved the competitive potential of Topco members with respect to other large and powerful chains." [Id. at 600](#). Topco was, in more recent parlance, a cooperative procompetitive joint venture. But the darker side of Topco -- its bylaws required horizontal territorial division among the association's members -- led the Court to condemn it as a per se violation [\[\\*\\*25\]](#) of the Sherman Act. [Id. at 608](#).

The parallels between this case and Topco are crystallized by Chief Justice Burger's dissent in Topco, in which he stressed the interbrand competition fostered by Topco's existence:

[W]e have here an agreement among several small grocery chains to join in a cooperative endeavor that, in my view, has an unquestionably lawful principal purpose; in pursuit of that purpose they have mutually agreed to certain minimal ancillary restraints that are fully reasonable in view of the principal purpose \* \* \*.

[Id. at 613](#) (Burger, CJ, dissenting). But of course, the Chief Justice's view did not prevail. [HN8](#) The law is this: Horizontal restraints in the context of a procompetitive joint venture remain unlawful per se unless they are necessary to (or, in certain formulations, "reasonably ancillary to") the achievement of the joint venture's procompetitive benefits.

The bank defendants offer various reformulations of their basic argument, but the court is constrained to reject them at this stage. Accordingly, the bank defendants' motions to dismiss (Doc # # 26, 29) are DENIED.

B

Bank One Corp and JPMorgan Chase move **[\*\*26]** to dismiss the complaint against them pursuant to [FRCP 12\(b\)\(6\)](#) on the ground that it fails adequately to allege their participation in the alleged conspiracy. Doc # 17. Bank One Corp and JPMorgan Chase contend that they are "nonoperating holding corporations," id at 1:22, and that the complaint does not explain how they participated in the alleged conspiracy or are liable for the actions of a subsidiary, Bank One NA. As alleged in the complaint, the holding company structure is this: JPMorgan Chase was created on July 1, 2004, by the holding company merger between J P Morgan Chase & Co and Bank One Corp. Bank One NA, which was a wholly owned subsidiary of Bank One Corp at the time of the July 2004 merger, had previously acquired Bank One of Arizona NA, which was entitled to appoint outside directors to Star's board. Compl (Doc # 1) P 10. In short, the complaint alleges that at present Bank One NA is a subsidiary of JPMorgan Chase; it is unclear whether Bank One Corp continues to exist following the July 2004 holding company merger. There is no dispute -- at least at this stage -- that Bank One NA has successor liability for Bank One of Arizona **[\*\*27]** NA's actions.

Bank One Corp and JPMorgan Chase make two arguments, both of which the court would have to accept to grant their **[\*1136]** motion to dismiss. One argument goes to vicarious liability, the other to conspiracy liability. As to vicarious liability, they contend that the complaint does not adequately plead alter ego liability on Bank One Corp's part for actions of Bank One NA; and that in turn, JPMorgan Chase cannot be liable because Bank One Corp had no liability to which JPMorgan Chase could have succeeded in the holding company merger. As for liability for conspiracy, Bank One Corp and JPMorgan Chase argue that the complaint's pleading format -- specifically, grouping them with the other bank defendants and alleging that the group in general conspired to fix interchange fees -- is inadequate under [FRCP 8](#), which sets a minimum threshold of defendant-by-defendant specificity that a plaintiff must meet.

These arguments are convincing. The allegations of the complaint regarding both the vicarious liability and conspiracy theories are simply legal conclusions without supporting facts. For example, plaintiffs allege that "Bank One [Corp] exercised **[\*\*28]** such dominion and control over Bank One, NA and Bank One Arizona that it is liable according to the law for the acts of Bank One, NA and Bank One Arizona." Compl (Doc # 1) P 10. See, e.g., [Neilson v Union Bank of California, NA, 290 F Supp 2d 1101, 1116 \(CD Cal 2003\)](#) ("Conclusory allegations of 'alter ego' status are insufficient to state a claim. Rather, a plaintiff must allege specifically both of the elements of alter ego liability, as well as facts supporting each.").

With respect to the conspiracy theory of liability, Bank One Corp and JPMorgan Chase are quite correct that the complaint lumps them in with the other bank defendants for purposes of pleading the conspiracy. They are equally correct that the allegations of the complaint doing the work under [FRCP 8](#) of pleading the conspiracy are not the generalized allegations of, for example, P 61 ("The [b]ank [d]efendants \* \* \* have caused Star to continue to impose [i]nterchange [f]ees \* \* \*."), but rather the particularized allegations of PP 9-14 that state how each bank, individually, exerted control over Star's rulemaking. Consequently, there are no allegations in **[\*\*29]** the complaint specifically connecting Bank One Corp and JPMorgan Chase to the alleged conspiracy that controlled Star. Cf [In re Sagent Technology, Inc, Derivative Litigation, 278 F Supp 2d 1079, 1094 \(ND Cal 2003\)](#) ("While [FRCP 8](#) requires only that the a pleading set forth a short and plain statement of the claim showing that the pleader is entitled to relief, the underlying requirement is that a pleading give fair notice of the claim being asserted and the grounds upon which it rests. A complaint that lumps together thirteen individual defendants, where only three of the individuals was alleged to have been present for the entire period of the events alleged in the complaint, fails to give fair notice of the claim to those defendants." (citation and quotation marks omitted)).

In response to this, plaintiffs argue principally that Bank One Corp and JPMorgan Chase are conspirators in this case for an entirely different reason -- to wit, because they exerted control over Visa USA Inc and Visa International Corp (collectively, "Visa") and Mastercard International Inc ("Mastercard"). Id PP 17-20. Visa and Mastercard own,

respectively, **[\*\*30]** Plus and Cirrus, the two worldwide ATM networks. Id PP 18-19. Plaintiffs contend -- and the complaint is far from clear on the causation or conspiracy in this -- that action by these two networks precipitated the adoption of ATM surcharges in all ATM networks. Id PP 54-55. This in turn rendered fixed interchange fees unnecessary. Id P 62. Plaintiffs' tale about the involvement of Bank One Corp and JPMorgan **[\*1137]** Chase in all this is not totally improbable. But the complaint is so poorly developed in this particular respect that it does not give fair notice under [FRCP 8](#) to Bank One Corp and JPMorgan Chase (or the court, for that matter) of the role they are alleged to have played in the conspiracy. Indeed, the complaint is ambiguous on just what the scope of the alleged conspiracy was: The complaint concentrates largely on the decisionmaking surrounding Star, yet Visa and Mastercard -- avowed competitors of Star, no less -- are announced as coconspirators, see Compl (Doc # 1) PP 17-18.

Accordingly, Bank One Corp and JPMorgan Chase's motion to dismiss is GRANTED. The defects in the complaint against these entities could possibly be resolved by an amended **[\*\*31]** pleading; accordingly, plaintiff's are given leave to amend their complaint against Bank One Corp and JPMorgan Chase. See [United States v Smithkline Beecham Clinic Labs, 245 F3d 1048, 1052 \(9th Cir 2001\)](#). On the other hand, the parties may wish to defer resolution of the liability of Bank One Corp and JPMorgan Chase by entering into a tolling agreement pending the outcome of other issues. The choice is, in the first instance, plaintiff's and then, possibly, Bank One Corp's and JPMorgan Chase's.

#### C.

First Data moves to dismiss the complaint on the ground that it fails to allege First Data's involvement in the claimed conspiracy. Doc # 33. First Data proceeds from a simple premise: The complaint states that "Concord [EFS] was acquired by First Data \* \* \*, the largest US credit card processor, and is now a wholly-owned subsidiary of First Data," Compl (Doc # 1) P 8, but beyond this, the complaint says nothing specific about First Data. Plainly, the allegation quoted above is insufficient to state a claim for alter ego liability on First Data's part for acts taken by its subsidiary Concord EFS. And although the complaint repeatedly refers to "the defendants" or "the **[\*\*32]** bank defendants" in the aggregate -- groups that include First Data, even though it is not a bank -- there are no allegations in the complaint specific to First Data that suggest how it could have taken the actions ascribed to "the defendants" or "the bank defendants." The court agrees with First Data that the complaint does not give it fair notice of the claims against it.

Plaintiffs' response largely ignores their complaint. They assert that "First Data has now owned Star for over a year," Doc # 109 at 16:10-11, but of course, that is not what the complaint alleges: The complaint asserts that First Data owns a corporation that in turn owns Star. Plaintiffs rely on material outside the complaint to suggest that First Data acts as Star's agent. Id at 18-19. They ask the court to take judicial notice of several hundred pages of SEC filings made by First Data, Doc # 111, and they parse this material at length in their filings, Doc # 109 at 5-10. Perhaps under certain circumstances, SEC filings are the proper subject of judicial notice; the court expresses no view on this question. [HNS↑](#) Judicial notice at the pleadings stage is properly invoked to fill in a small gap in an otherwise complete **[\*\*33]** portrait painted by the complaint. But here, the canvass is missing as well as the image: Plaintiffs would defeat a motion to dismiss by piling a ream of SEC filings (literally) onto one half-sentence in their complaint. This is not proper at the pleadings stage -- not as a matter of procedure and certainly not as a matter of good practice. Plaintiffs are manifestly in command of vast knowledge about First Data's activities; the length of their opposition paper, which runs to the very limits of Civ L R 7-4(b), more than amply illustrates that. Distilling the material in plaintiffs' **[\*1138]** opposition paper into an amended complaint should be trivial for plaintiffs, will likely give fair notice to First Data and will surely be a boon to the court.

Accordingly, First Data's motion to dismiss (Doc # 33) is GRANTED, and plaintiffs are given leave to file an amended complaint to amplify their allegations against First Data.

#### III

Plaintiffs have filed a paper styled "plaintiffs' submission regarding scheduling and arbitration." Doc # 120. Defendants have filed a paper in response. Doc # 125. Plaintiffs seek an order directing defendants (1) to state by a

date certain their intentions to file a [\*\*34] motion to compel arbitration and (2) if they so intend, to file such a motion by a date certain. The court is not entirely satisfied that it has the authority to force the issue, and even if the court were so empowered, the issue seems better resolved by litigating equitable defenses such as waiver and estoppel in the context of an actual motion to compel arbitration -- if and when such a motion should be presented to the court.

IV

In sum, the court DENIES the motions to dismiss the complaint for failure to state a per se antitrust claim (Doc # # 26, 29); GRANTS First Data's motion to dismiss (Doc # 33); and GRANTS Bank One Corp and JPMorgan Chase's motion to dismiss (Doc # 17). Plaintiffs are given leave to file an amended complaint. The parties may stipulate to a pleading schedule in accordance with their respective positions, but shall appear on July 13, 2005, at 10:00am for a hearing on any motions filed and for a scheduling conference, at which the parties should be prepared to address a discovery plan and any outstanding pleading issues. As previously set at the January 26, 2005, case management conference, defendants' initial disclosure are due 60 days from the date of [\*\*35] this order.

IT IS SO ORDERED.

May 4, 2005

VAUGHN R WALKER

United States District Chief Judge

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## [Am. Needle, Inc. v. New Orleans La. Saints](#)

United States District Court for the Northern District of Illinois, Eastern Division

May 5, 2005, Decided ; May 5, 2005, Filed

No. 04 C 7806

### **Reporter**

385 F. Supp. 2d 687 \*; 2005 U.S. Dist. LEXIS 9484 \*\*; 2005-1 Trade Cas. (CCH) P74,819

AMERICAN NEEDLE, INC., Plaintiff, vs. NEW ORLEANS LOUISIANA SAINTS, et al., Defendants.

**Subsequent History:** Reconsideration denied by [Am. Needle, Inc. v. New Orleans La. Saints, 385 F. Supp. 2d 727, 2005 U.S. Dist. LEXIS 18885 \(N.D. Ill., June 6, 2005\)](#)

Motion denied by [Am. Needle, Inc. v. New Orleans La. Saints, 2005 U.S. Dist. LEXIS 22967 \(N.D. Ill., Oct. 5, 2005\)](#)

## **Core Terms**

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trademarks, teams, apparel, logos, headwear, television, relevant market, carrying, license, sports, broadcasts, per se rule, manufacture, monopolize, antitrust, products, games, rule of reason, markets, league, definitions, consumers, football, courts, brand, motion to dismiss, interchangeable, defendants', cap, anti trust law

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrers & Objections > General Overview

### **HN1[] Motions to Dismiss, Failure to State Claim**

A [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss tests the sufficiency of the complaint, not the merits of the case. In deciding a motion to dismiss, the court must assume the truth of all well-pleaded allegations, making all inferences in the plaintiff's favor. The court should dismiss a claim only if it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

### **HN2[] Antitrust & Trade Law, Sherman Act**

See [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > Sherman Act > General Overview

### **[HN3](#)[] Antitrust & Trade Law, Sherman Act**

See [15 U.S.C.S. §2](#).

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

### **[HN4](#)[] Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason**

[15 U.S.C.S. § 1](#) of the Sherman Act outlaws only unreasonable restraints of trade. Thus, to determine whether a restraint of trade violates **antitrust law**, courts employ the rule-of-reason test, taking into account a variety of factors, including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint's history, nature, and effect. Because of the costs of the rule-of-reason test, courts employ a per se rule to establish illegal restraint, where prior experience allows the court to reach a conclusive presumption that the restraint has a predictable and pernicious anticompetitive effect and limited potential for pro-competitive benefit. Courts do not employ the per se rule unless the effect of the restraint of trade is obvious.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

### **[HN5](#)[] Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason**

Judicial precedent rejects the per se rule when reviewing trade restraints imposed by sports leagues.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

### **[HN6](#)[] Regulated Practices, Price Fixing & Restraints of Trade**

To determine whether a trade restraint runs afoul of **antitrust law** under the rule of reason, a court must determine the consequences of the restraint on the affected market. But, first, the relevant affected market must be defined. Likewise, claims of monopolization of trade under [15 U.S.C.S. § 2](#) of the Sherman Act also require a determination of the relevant market.

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### [\*\*HN7\*\*](#) [down] **Market Definition, Relevant Market**

A relevant market is composed of products whose use is interchangeable and for which there is a cross-elasticity of demand. In some cases, the relevant market for an antitrust action may be a distinct portion, or submarket, of a broader market. To determine whether there is a distinct product submarket, courts look to industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors. Regardless of whether the relevant market is properly viewed as a submarket, a plaintiff may not limit a market definition by excluding reasonable product substitutes in order to establish an unreasonable restraint or a monopolizing effect on the market. Incomplete or improperly circumscribed market definitions effectively write the market requirement out of **antitrust law**.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### [\*\*HN8\*\*](#) [down] **Regulated Practices, Market Definition**

In antitrust actions, courts repeatedly reject markets that are defined by a company's trademark.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### [\*\*HN9\*\*](#) [down] **Regulated Practices, Market Definition**

For purposes of an antitrust action, the distribution of sports-related intellectual property can be a market unto itself.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### [\*\*HN10\*\*](#) [down] **Regulated Practices, Market Definition**

In antitrust actions, a market is composed of products that have reasonable interchangeability for the purposes for which they are produced: price, use, and qualities considered.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Trademark Law > Conveyances > General Overview

Antitrust & Trade Law > Regulated Industries > Sports > General Overview

#### [\*\*HN11\*\*](#) [down] **Regulated Practices, Market Definition**

If a unique, separate market exists for the television rights of NCAA football games and NBA basketball games, the United States District Court for the Northern District of Illinois, Eastern Division, does not see how, as a matter of

law, a unique market cannot exist for the manufacture and distribution of merchandise carrying National Football League trademarks.

**Counsel:** [\[\\*\\*1\]](#) For American Needle, Inc, Plaintiff: Jeffrey M. Carey, Law Office of Jeffrey M. Carey, Buffalo Grove, IL.

For National Football League, Defendant: Gregg Levy, Derek Ludwin, Covington & Burling, Washington, DC; Earl Edward Farkas, Eugene E. Gozdecki, Gozdecki and DelGiudice, Chicago, IL.

For Reebok International Ltd., Defendant: Timothy Bunker Hardwicke, Alice E Decker, Matthew B Mock, Latham & Watkins LLP, Chicago, IL; John Thomas Rosch, Latham & Watkins, San Francisco, CA.

**Judges:** JAMES B. MORAN, Senior Judge.

**Opinion by:** JAMES B. MORAN

## **Opinion**

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### **[\*689] MEMORANDUM OPINION AND ORDER**

Plaintiff American Needle, Inc. (American Needle) brought this antitrust action against defendants, the National Football League (NFL), the individual owners of the NFL's member teams, National Football League Properties, Inc. (NFLP) and Reebok International, Ltd. (Reebok), for violation of the Sherman Act, [15 U.S.C. § 1 et seq.](#) Defendants move to dismiss the complaint for failure to state a claim. The motion is granted in part and denied in part.

### **BACKGROUND**

The following facts, taken from plaintiff's complaint, are, for purposes of this motion, accepted as true. American Needle, a [\[\\*\\*2\]](#) corporation headquartered in Buffalo Grove, Illinois, designs, manufactures, and sells headwear carrying the trademarked names and logos of various professional athletic teams. The NFL is an unincorporated association of professional football teams and their owners. The NFLP is a Delaware corporation established by the NFL and its member teams to license their trademarks. For many years, American Needle and other clothing manufacturers were licensed by the NFLP to use NFL teams' trademarks on their headwear and apparel. However, in December 2000, the NFL, NFLP and NFL team owners decided to change their licensing practices for the use of trademarks on headwear and apparel -- no longer would various manufacturers compete for licenses, nor would the NFLP grant multiple licenses. Instead, the NFLP would enter into an exclusive licensing agreement with one company for the manufacture, sale, and distribution of headwear and apparel carrying the trademarks of the NFL and its member teams. Subsequently, the NFLP entered into an exclusive licensing agreement with Reebok. American Needle's trademark license with the NFLP expired in March 2001 and was not renewed.

[\[\\*690\]](#) Plaintiff filed a five-count [\[\\*\\*3\]](#) complaint on December 1, 2004, alleging that defendants' agreement to grant an exclusive license for the use of NFL teams' trademarks on headwear and apparel constitutes a monopolization, a conspiracy to monopolize, and an attempt to monopolize various markets (counts I-III), in violation of section 2 of the Sherman Act, [15 U.S.C. § 2](#). Plaintiff also contends that the agreement constitutes a restraint of trade under the *per se* rule and the rule of reason (counts IV and V), in violation of [section 1 of the Act](#).

### **DISCUSSION**

**HN1** A [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) motion to dismiss tests the sufficiency of the complaint, not the merits of the case. [Triad Assocs., Inc. v. Chicago Hous. Auth., 892 F.2d 583, 586 \(7th Cir. 1989\)](#). In deciding a

motion to dismiss, the court must assume the truth of all well-pleaded allegations, making all inferences in the plaintiff's favor. [Sidney S. Arst Co. v. Pipefitters Welfare Educ. Fund, 25 F.3d 417, 420 \(7th Cir. 1994\)](#). The court should dismiss a claim only if it appears "beyond doubt that the plaintiff can prove no set of facts in support of his [\*\*4] claim which would entitle him to relief." [Conley v. Gibson, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 \(1957\)](#).

Counts IV and V of plaintiff's complaint allege violations of [section 1 of the Sherman Act](#), which states: [HN2](#) "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony." [15 U.S.C. § 1](#). Counts I, II and III of plaintiff's complaint allege violation of [section 2 of the Sherman Act](#), which states that [HN3](#) "every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony." [15 U.S.C. § 2](#).

In their motion to dismiss, defendants argue that plaintiff's claims for violations of the Sherman Act require it to identify the relevant market in which they have restrained and monopolized trade. [\*\*5] See, e.g., [Elliot v. United Center, 126 F.3d 1003, 1004-05 \(7th Cir. 1997\)](#); [Menasha Corp. v. News America Marketing In-Store, Inc., 238 F. Supp.2d 1024, 1032 \(N.D.Ill. 2003\)](#). Defendants assert that plaintiff has failed to identify such a relevant market. Plaintiff first maintains that even if this were true it would not defeat count IV because it states a claim for a *per se* violation of the Sherman Act and therefore does not require the identification of a relevant market.

The complaint alleges that the 32 professional football teams that constitute the NFL agreed to restrict the use of their intellectual property, opting to allow the NFLP to control it, and that the NFLP agreed to grant Reebok an exclusive license to use the trademarked names and logos of NFL teams on headwear and apparel. Plaintiff claims that this constitutes horizontal price-fixing and a group boycott, *per se* violations of the Sherman Act, which necessarily results in decreased output and/or supra-competitive prices. In their reply, defendants counter that a *per se* standard is inapplicable to the NFLP's agreement with Reebok because agreements involving members [\*\*6] of sports leagues must be analyzed under the rule of reason and these agreements cannot be labeled a group boycott or price-fixing. We agree that the *per se* rule does not apply to defendants' actions.

[\*691] Over a century ago the Supreme Court established that [HN4](#) [section 1 of the Sherman Act](#) outlaws only unreasonable restraints of trade. [United States v. Joint-Traffic Association, 171 U.S. 505, 43 L. Ed. 259, 19 S. Ct. 25 \(1898\)](#); see [Arizona v. Maricopa County Medical Society, 457 U.S. 332, 343, 73 L. Ed. 2d 48, 102 S. Ct. 2466 \(1982\)](#). Thus, to determine whether a restraint of trade violates [antitrust law](#), courts employ the rule-of-reason test, "taking into account a variety of factors, including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint's history, nature, and effect." [State Oil Co. v. Khan, 522 U.S. 3, 10, 139 L. Ed. 2d 199, 118 S. Ct. 275 \(1997\)](#). Because of the costs of the rule-of-reason test, courts have employed a *per se* rule to establish illegal restraint, where prior experience allows the court to reach a conclusive presumption that the restraint has a "predictable and pernicious anticompetitive effect" and "limited potential for procompetitive [\*\*7] benefit." *Id.*; [Maricopa County, 457 U.S. at 343](#). Courts do not employ the *per se* rule unless the effect of the restraint of trade is obvious. [Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 49-50, 53 L. Ed. 2d 568, 97 S. Ct. 2549 \(1977\)](#)("*Per se* rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive.").

[HN5](#) The Supreme Court has rejected the *per se* rule when reviewing trade restraints imposed by sports leagues. [NCAA v. Board of Regents of the University of Oklahoma, 468 U.S. 85, 100-101, 82 L. Ed. 2d 70, 104 S. Ct. 2948 \(1984\)](#). In [Board of Regents](#), members of the National Collegiate Athletic Association (NCAA) challenged the association's restraints on the sale of television broadcast rights. *Id.* Though the Supreme Court had found similar restraints to be illegal *per se* in other circumstances, it did not apply the *per se* rule but, rather, analyzed the restraints under the rule of reason. The court jettisoned the *per se* rule in that case because it involved "an industry in which horizontal restraints on competition are essential if the product [college football] is to be available at all." *Id.* In order to offer [\*\*8] intercollegiate athletic competition, the NCAA required joint cooperation and conformity to

rules. *Id.* Furthermore, the court found that many NCAA restraints resulted in a pro-competitive effect on the association's members, thus a fair evaluation of the restraints required consideration of the NCAA's justification for the regulations. *Id. at 103.*

Since the Supreme Court's decision in *Board of Regents*, courts have repeatedly rejected the *per se* rule when analyzing a trade restraint imposed by a sports league, opting instead for the rule of reason. See, e.g., *Chicago Professional Sports Limited Partnership v. NBA*, 961 F.2d 667, (7th Cir. 1992)(reviewing NBA's restriction on television broadcast rights under the rule of reason); *National Hockey League Players' Association v. Plymouth Whalers Hockey Club*, 325 F.3d 712, 719 (6th Cir. 2003)(reviewing hockey league's limitation on the eligibility of "overaged" players under rule of reason); *Law v. NCAA*, 134 F.3d 1010, 1019 (10th Cir. 1998)(stating that since athletic league competition requires horizontal agreements, "all horizontal agreements among NCAA [\*\*9] members, even those as egregious as price-fixing, should be subject to a rule of reason analysis."); see also *Overview: Looking Ahead at Sports and the Antitrust Law*, 14 Antitrust 15, 16 (Spring 2000) ("It is now settled that the practices typically associated with the organization of professional sports leagues and other organizations such as the NCAA are not subject to the *per se* rule."). Thus, even if plaintiff's allegations describe a trade restraint that has been held unlawful, see *Denny's Marina, Inc. v. [\*692] Renfro Productions, Inc.*, 8 F.3d 1217, 1220 (7th Cir. 1993) ("[A] horizontal price-fixing conspiracy . . . is *per se* an unreasonable restraint of trade."), a *per se* claim for violation of *section 1 of the Sherman Act* is inappropriate against the NFL.

Our analysis of *section 1 of the Sherman Act* does not end, however, because plaintiff also alleges a violation of the section based on the rule of reason. **HN6**<sup>↑</sup> To determine whether a trade restraint runs afoul of *antitrust law* under the rule of reason, a court must determine the consequences of the restraint on the affected market. See *Havco of America, Ltd. v. Shell Oil Co.*, 626 F.2d 549, 554 (7th Cir. 1980); **[\*\*10]** see also *42nd Parallel North v. E. Street Denim Co.*, 286 F.3d 401, 404 (7th Cir. 2002). But, first, the relevant affected market must be defined. *Adidas America, Inc. v. NCAA*, 64 F.Supp.2d 1097, 1101(D. Kan. 1999) ("The first step in an antitrust analysis is defining the relevant market or markets."). Likewise, claims of monopolization of trade under *section 2 of the Sherman Act* also require a determination of the relevant market. *United States v. Grinnell Corp.*, 384 U.S. 563, 571, 16 L. Ed. 2d 778, 86 S. Ct. 1698 (1966); *Bernard Food Industries, Inc. v. Dietene Co.*, 415 F.2d 1279, 1284 (7th Cir. 1969) ("A definition of the relevant market is an essential element of a violation under *Section 2 of the Sherman Act*." (superseded by statute on an unrelated issue)). Defendants assert that plaintiff has failed to identify a legitimate market on which it can base its remaining claims.

Plaintiff alleges that defendants' conduct has affected six relevant markets: (1) the market for licenses to use NFL and NFL teams' trademarks in the design, manufacture and sale of apparel, (2) the market for licenses to use these trademarks in the design, manufacture and sale of **[\*\*11]** headwear, (3) the wholesale market for the sale and distribution of apparel with these trademarks, (4) the wholesale market for the sale and distribution of headwear with these trademarks, (5) the market for the manufacture of apparel with the NFL and NFL teams' trademarks, and finally, (6) the market for the manufacture of headwear with these trademarks. Defendants argue that none of these alleged markets, which are all defined by the use of trademarks, can support plaintiff's antitrust claims because market definitions contingent on trademarks are inadequate as a matter of law. In addressing defendants' argument, we do not determine whether or not the facts support plaintiff's market definitions, but only determine whether the law will permit the sort of market definitions alleged. *Rohlfing v. Manor Care, Inc.*, 172 F.R.D. 330, 345 (N.D.Ill. 1997).

**HN7**<sup>↑</sup> A relevant market is composed of products whose use is interchangeable and for which there is a "cross-elasticity of demand." *Brown Shoe Co. v. United States*, 370 U.S. 294, 325, 8 L. Ed. 2d 510, 82 S. Ct. 1502 (1962); *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 394-95, 100 L. Ed. 1264, 76 S. Ct. 994 (1956) (stating that a relevant market **[\*\*12]** consists of "commodities reasonably interchangeable by consumers for the same purposes."). In some cases, the relevant market for an antitrust action may be a distinct portion, or submarket, of a broader market. *Brown Shoe Co.*, 370 U.S. at 325. To determine whether there is a distinct product submarket, courts look to "industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors." *Id.* Regardless of whether the relevant market is properly

viewed as a submarket, a plaintiff may not limit a market definition [\*693] by excluding reasonable product substitutes in order to establish an unreasonable restraint or a monopolizing effect on the market. *Adidas America, Inc.*, 64 F.Supp.2d at 1102. Incomplete or improperly circumscribed market definitions effectively write the market requirement out of **antitrust law**.

For this reason, **HN8** courts have repeatedly rejected markets that are defined by a company's trademark. See, e.g., *Generac Corp. v. Caterpillar Inc.*, 172 F.3d 971, 977 (7th Cir. 1999) [\*\*13] ("Product markets are not defined in terms of one trademark or another."); *Tunis Bros. Co., Inc. v. Ford Motor Co.*, 952 F.2d 715, 723-24 (3d Cir. 1991)(collecting cases); *Shaw v. Rolex Watch, U.S.A., Inc.*, 673 F.Supp. 674, 678 (S.D.N.Y. 1987)(collecting cases).<sup>1</sup> In these cases, parties have attempted to define a market based on a product's trademark, excluding interchangeable substitutes and ignoring the consumers' "cross-elasticity of demand" for products that serve a similar purpose. For example, in *Generac Corp.*, the Seventh Circuit found that the proper market in which to analyze Caterpillar's allegedly anti-competitive activity was not Olympian-trademarked generator sets, but all generator sets. *Id. at 977*. The court explained that trademarks do not distinguish separate markets because they "simply identify the origin of a product." *Id.* It further noted that "not even the most zealous antitrust hawk has ever argued that Amoco gasoline, Mobil gasoline, and Shell gasoline are three separate product markets." *Id.* Even a prestigious trademark, such as Mercedes-Benz "protects only the name or symbol of the product. Market power, if [\*\*14] any, is derived from the product, not from the name or symbol as such." *Mozart Co. v. Mercedes-Benz of North America, Inc.*, 833 F.2d 1342, 1346 (9th Cir. 1987).

Yet, the analysis from these trademark cases cannot be readily applied to the facts of the instant case. The trademarks integral to plaintiff's market definitions -- the names and logos of the NFL and its member teams -- do not serve to "identify the origin" of the products [\*\*15] that carry them. (The tag reading Reebok, as opposed to Nike or Adidas or Champion or American Needle, serves the generally accepted purpose of trademarks, informing the customer of the origin of the apparel and perhaps revealing something to the customer about its quality. But neither Reebok's trademark, nor that trademark's purpose, is relevant to our inquiry.) Nor is it clear that these NFL trademarks "protect only the name or symbol of the product." The NFL team names and logos that appear on apparel and headwear are not a "symbol" of the T-shirt or cap on which they appear. In fact, the NFL teams' trademarks carried on a T-shirt or cap may be more properly viewed as the product itself, rather than the T-shirt or cap.<sup>2</sup>

[\*\*16] [\*694] In *Generac*, the Seventh Circuit recognized the absurdity in claiming that one brand of gasoline was not interchangeable with another, and therefore constituted its own separate market. The same would be true in claiming that one brand of t-shirt or cap could not substitute for another brand. However, we must acknowledge that some portion of the market for headwear and apparel carrying NFL teams' trademarks has little to do with the items carrying the logos. Certainly some people purchase a shirt or hat with an NFL team's logo simply because they need a shirt or a hat. As defendants argue, apparel with a different logo or with no logo would serve as a reasonable substitute for these consumers. But, just as certainly, a significant segment of the market for NFL-branded headwear and apparel is purchasing the team logo. If a store sold out of hats carrying the Chicago Bears logo, these individuals would not necessarily find caps carrying logos for Spongebob, the University of Michigan, or even the Chicago Bulls to be reasonable substitutes. More likely, they would purchase a different item of apparel,

<sup>1</sup> Nonetheless, courts have not foreclosed the possibility that under certain circumstances a well-defined, distinct market could consist of just one brand of a product. See *U.S. Anchor Mfg., Inc. v. Rule Industries, Inc.*, 7 F.3d 986, 998 (11th Cir. 1993) ("A single branded product may, in rare cases, constitute its own relevant market.") (citing *Los Angeles Memorial Coliseum Commission v. NFL*, 726 F.2d 1381, 1393 (9th Cir.), cert. denied, 469 U.S. 990, 83 L. Ed. 2d 331, 105 S. Ct. 397 (1984)); *Tunis Bros. Co., Inc.*, 952 F.2d at 723.

<sup>2</sup> This is in contrast to the purpose of the NFL trademarks discussed in *Weber v. NFL*, 112 F. Supp. 2d 667 (N.D.Ohio 2000). In *Weber*, the plaintiff attempted to define a market around Internet domain names employing the trademarked names of NFL teams. The exact purpose of a domain name is to identify the origin and represent the content of the Internet site for which it serves as an address. Thus, the use of an NFL team name in a domain name does serve as a symbol of the product and the content one would find at that address.

such as a T-shirt or sweatshirt, or even a non-apparel item like a mug or key chain [\*\*17] that carries the Bears logo. The product for these consumers is the trademarked logo. This is not the case with the trademarks Pine-Sol, Olympian, Rolex, or Shell. Though customers may prefer those brand names for any number of reasons, what they are buying is a disinfectant household cleaner, *Clorox Co. v. Sterling Winthrop*, 117 F.3d 50 (2d Cir. 1997), an electric generator, *Generac Corp.*, 172 F.3d at 971, a high-end watch, *Shaw*, 673 F.Supp. at 674, or gasoline, *Chawla v. Shell Oil Co.*, 75 F.Supp.2d 626, 642 (S.D.Tex. 1999), all of which have reasonable substitutes under other brand names. But for many people purchasing headwear or apparel with an NFL team's logo, they are purchasing the ability to be identified with a particular team -- the right to be recognized as a fan. Defendants state that "Relevant markets include not just brands that consumers may prefer but all alternatives to which consumers could practically turn' if prices become anticompetitive." For consumers seeking to wear something in support of an NFL team, what is the alternative to which they can practically turn if the NFLP's exclusive contract [\*\*18] with Reebok allows this headwear and apparel to become anticompetitve?

Defendants cite *Carell v. Shubert Organization, Inc.*, 104 F.Supp.2d 236 (S.D.N.Y. 2000), to support their contention that a market narrowly defined by a product's trademark does not suffice for an antitrust claim. Unlike the other cases cited above, *Carell* involves trademarks which do not simply serve to identify the origin of a product. In *Carell*, a make-up designer claimed that the producers of the musical *Cats* had monopolized the market for intellectual property rights related to the show. *Id. at 241*. The court denied plaintiff's antitrust claim because there was no plausible basis on which to find that *Cats*-related makeup designs and other intellectual property was a market unto itself. *Id. at 264*. The court explained that customer preference for *Cats*-related products did not create a market unto itself, just as consumers' choice of Pepsi, NBC or TWA, over their respective competitors, does not establish each of their branded products as its own market. *Id. at 265* (quoting *Global Discount Travel Services v. Trans World Airlines, Inc.*, 960 F.Supp. 701, 705 (S.D.N.Y. 1997)). [\*\*19] The court also found no reason why "products associated with other Broadway shows or other forms of entertainment are not reasonably interchangeable with products associated with *Cats*." *Id. at 265*. But it is not customers' preference for headwear and apparel carrying NFL teams' names and logos that would establish it as a [\*695] separate market, it is the lack of reasonably interchangeable products. Declining to recognize a separate market for *Cats*-related products is more akin to declining to find a separate market for Chicago Bears-related headwear and apparel, than for all NFL-related headwear and apparel. Just as there are other Broadway plays and musicals, there are other NFL teams. However, we are not considering whether headwear and apparel carrying one NFL team's logo constitutes its own market, we are considering whether, as a matter of law, all headwear and apparel carrying NFL team logos cannot constitute a market unto itself. Both the Supreme Court and the Seventh Circuit have held in a different context -- the realm of television, not textiles -- that *HN9*[<sup>1</sup>] the distribution of sports-related intellectual property can be a market unto itself.

In *Board of Regents*, 468 U.S. at 111, [\*\*20] the Supreme Court found that the district court properly held that college football broadcasts constituted their own market. Since the audience for these broadcasts was "uniquely attractive," advertisers and broadcasters did not have reasonable alternatives for this product. *Id.* Hence, the Supreme Court held that the NCAA had monopoly power over a product without substitutes on the market. *Id. at 112*. Three decades earlier, the Court held that the even-narrower market for the promotion of championship boxing contests was separate from the market for all professional boxing events. *International Boxing Club of New York, Inc. v. United States*, 358 U.S. 242, 250-51, 3 L. Ed. 2d 270, 79 S. Ct. 245 (1959). Acknowledging that *HN10*[<sup>1</sup>] a "market is composed of products that have reasonable interchangeability for the purposes for which they are produced -- price, use and qualities considered," the court held that championship boxing contests were sufficiently separate from boxing contests in general because, among other reasons, they were uniquely attractive to fans. *Id. at 250* (quoting *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. at 404); *Board of Regents*, 468 U.S. at 112. [\*\*21]

The Seventh Circuit also found that a sport's television broadcasts constitute their own market, though the court's reasoning varied from that in *Board of Regents*. See *Chicago Professional Sports Limited Partnership v. NBA*, 961 F.2d 667, 673-74 (7th Cir. 1992). In *Chicago Professional Sports*, the owners of the Chicago Bulls and the television station, WGN, brought an antitrust action against the NBA alleging that its cap on the number of televised games was illegal. *Id. at 669*. The NBA argued that its basketball broadcasts were a small fraction of all television

entertainment, or even all televised sports, and therefore its restraints had a minimal impact on the overall market. *Id. at 673*. Although the Seventh Circuit did not find that the audience for NBA games distinguished a unique market for these broadcasts, it rejected the notion that the market could only be defined by the audience. Nor did it define the market as television entertainment or televised sports. See *id.* The court found that televised basketball games were the product and, therefore, caps on the number of games broadcast were a restraint on that [\*\*22] product market.<sup>3</sup> *Id. at 673-74*.

[\*696] Thus, in the case of a sport's broadcasts, whether a court looks to the broadcasts' audience or the product itself, it is a unique, separate market. Just as the Supreme Court and the Seventh Circuit distinguished televised collegiate football games and televised basketball games from the myriad of other television broadcasting, or even televised sports, so too could headwear and apparel carrying NFL teams' logos and other trademarks [\*\*23] be distinguished from all other headwear and apparel, including headwear and apparel carrying one of the myriad of other possible logos, or even the logo of a non-NFL sports team. NCAA games draw a unique audience, and NBA games constitute a unique product. Therefore, the sale of the rights to televise them is a market unto itself. See *Board of Regents, 468 U.S. at 112; Chicago Professional Sports, 961 F.2d at 673-74*. The sale of television rights is a method for these sports associations to merchandise and promote their core product: the athletic competition in which their member teams engage. The sale of headwear and apparel branded with team logos is another method. *HN11* [↑] If a unique, separate market exists for the television rights of NCAA football games and NBA basketball games, we do not see how, as a matter of law, a unique market cannot exist for the manufacture and distribution of merchandise carrying NFL trademarks.

Our analysis is limited to the issues raised in defendants' motion to dismiss. As pointed out above, we have not determined whether the markets plaintiff alleges do in fact exist, thereby supporting its claims. We have found only [\*\*24] that the law does not preclude an antitrust claim based on such markets. Even though plaintiff's market definitions do not fail due to reliance on NFL trademarks, they may still be improper. As indicated in our analysis, if the true product in this case is NFL teams' logos, not the items that carry them, then there may be no justification for limiting the relevant market to headwear and apparel that carry these logos. Perhaps, the market would more properly include all merchandise carrying NFL logos. Of course, this broader market definition would then alter the impact of the exclusive contract with Reebok, which is allegedly limited to the manufacture and distribution of headwear and apparel.<sup>4</sup>

[\*\*25] Many questions concerning the viability of plaintiff's claims remain. For example, it is far from clear, for a different reason, that NFL's control over the trademarks and logos is subject to the antitrust laws. The same reasoning that has led courts to reject the *per se* concept, when somewhat extended, can lead to the conclusion that the NFL should be viewed as a single source for the purpose of protecting the clubs' trademarks and logos. The league may be viewed much like a franchisor. The NFL may license others to use its trademarks and logos to affix to merchandise and apparel they make, just as McDonald's licenses its trademarks for use by others, who make hamburgers. The NFL may have as great an interest as McDonald's in protecting the good will inherent [\*697] in their marks by selectively choosing who may use them. See *Chicago Professional Sports Limited Partnership v. National Basketball Association, 95 F.3d 593, 599-600 (7th Cir. 1996)*. It is a rather dramatic assertion that the antitrust laws prohibit the NFL from determining who may use its trademarks and logos and,

<sup>3</sup> Though the markets in *Board of Regents, 468 U.S. at 85*, *International Boxing Club, 358 U.S. at 242*, and *Chicago Professional Sports, 961 F.2d at 667*, are more properly identified as "submarkets," this distinction is largely irrelevant since submarkets are legitimate markets for purposes of antitrust actions. Whether or not a market can be classified as a subset of another larger market does not impact the analysis if it is distinct enough to constitute its own legitimate market.

<sup>4</sup> Though it is not relevant to the inquiry before us and carries no weight at this stage in the litigation, it is worth noting that Reebok's 2004 Annual Report, contradicts the complaint's assertion that the company is "the exclusive provider of apparel and headwear bearing the Trademarks of the individual NFL Teams and the NFL." Reebok's Annual Report states that it has an exclusive right to manufacture and distribute NFL-branded replica jerseys, headwear, footwear and gloves and is the exclusive distributor of NFL-branded apparel and accessories in some distribution channels. However, it is "a non-exclusive distributor of NFL-branded apparel through catalogs, in retail stores that primarily carry NFL-branded products and in other retail channels."

therefore, its good will. But we leave that consideration to another day, as the present **[\*\*26]** contention is confined to whether or not there can be relevant markets. Given that plaintiff's market definitions are distinguishable from those that courts have found to be illegitimate due to their reliance on trademarks, and the fact that there is support in case law for distinguishing a separate market in this context, we deny defendants' motion to dismiss Counts I, II, III and V on the basis of improper market definitions.

### CONCLUSION

For the foregoing reasons, defendants' motion to dismiss count IV is granted, and their motion to dismiss counts I, II, III and V is denied.

JAMES B. MORAN

Senior Judge, U. S. District Court

May 5, 2005.

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## Able Sales Co. v. Compania de Azucar

United States Court of Appeals for the First Circuit

May 6, 2005, Decided

No. 04-1922

### **Reporter**

406 F.3d 56 \*; 2005 U.S. App. LEXIS 7902 \*\*; 2005-1 Trade Cas. (CCH) P74,782; 33 A.L.R. Fed. 2d 711

ABLE SALES COMPANY, INC., Plaintiff, Appellee, v. COMPAÑIA DE AZUCAR DE PUERTO RICO, Defendant, Appellant.

**Prior History:** **[\*\*1]** APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF PUERTO RICO. Hon. Juan M. Perez-Gimenez, U.S. District Judge.

## **Core Terms**

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commerce, sugar, refined sugar, imported, sales, raw, distributors, interstate, refinement, wholesalers, pricing, seller, district court, export, hundredweight, Robinson-Patman Act, intrastate, subject matter jurisdiction, transactions, inventory, discriminatory, processing, violations, argues, no evidence, **Antitrust Law**, competitor, regulation, predatory, selling

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

### **HN1 Price Discrimination, Competitive Injuries**

See [15 U.S.C.S. § 13\(a\)](#).

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Primary Line Injuries

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Secondary & Tertiary Line Injuries

Antitrust & Trade Law > Robinson-Patman Act > General Overview

### **HN2 Robinson-Patman Act, Claims**

The Robinson-Patman Anti-Discrimination Act encompasses two different types of violations: primary line violations and secondary line violations. Primary line violations are directed at injuring competition with the discriminating seller's direct competitors, whereas secondary line violations are directed at injuring competition among the discriminating seller's customers.

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Primary Line Injuries](#)

[Antitrust & Trade Law > Robinson-Patman Act > General Overview](#)

#### **HN3** **Robinson-Patman Act, Claims**

In general, primary line violations involve a claim by the injured party that a business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the relevant market.

[Antitrust & Trade Law > Robinson-Patman Act > Jurisdiction](#)

[Transportation Law > Interstate Commerce > Federal Powers](#)

[Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > Secondary & Tertiary Line Injuries](#)

[Antitrust & Trade Law > Robinson-Patman Act > General Overview](#)

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

[Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview](#)

[Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview](#)

[Governments > State & Territorial Governments > Boundaries](#)

#### **HN4** **Robinson-Patman Act, Jurisdiction**

Section 2(a) of the Robinson-Patman Anti-Discrimination Act does not extend jurisdiction to the full extent of Congress's constitutional power granted by the [Commerce Clause](#). The distinct "in commerce" language appears to denote only persons or activities within the flow of interstate commerce. The jurisdictional requirements of these provisions cannot be satisfied merely by showing that allegedly anticompetitive acquisitions and activities affect commerce. To satisfy the "in commerce" requirement, one of the discriminatory sales must cross a state line. As this requirement is jurisdictional, the burden to prove the interstate character of the sales is on the party asserting subject matter jurisdiction.

[Antitrust & Trade Law > Robinson-Patman Act > Claims](#)

[Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview](#)

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > Coverage > Commerce Requirement

#### **HN5** **Robinson-Patman Act, Claims**

Following the language of the statute, the U.S. Supreme Court holds that, in order to satisfy the "in commerce" requirement of the § 2(a) of the Robinson-Patman Anti-Discrimination Act, the defendant's activities must satisfy the following test: unless it appears that the defendant's alleged exclusive-dealing arrangements and discriminatory sales occur in the course of its interstate activities and that at least one of the defendant's allegedly discriminatory sales was made in interstate commerce, a plaintiff's claims must fail. In other words, if one of the discriminatory sales is in commerce, the seller is engaged in commerce and discrimination has occurred in the course thereof. The activities which must meet the in commerce requirements are the sales by the defendant seller.

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview

#### **HN6** **Contracts, Sales of Goods**

The flow of commerce is thought to end when the goods are stored in a seller's warehouse or storage facility for general inventory purposes, subject to an exception for when the goods are purchased and then stored in the seller's warehouse in response to a particular customer's needs.

Business & Corporate Compliance > ... > Governments > Agriculture & Food > Product Promotions

Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview

#### **HN7** **Agriculture & Food, Food Product Promotions**

In cases where the "flow of commerce" doctrine applies, the same entity engages in both the intrastate and interstate transaction. And courts hold that, to the extent that the purchasers are independent distributors in their pricing and marketing decisions, the flow of commerce is interrupted by the sale of the product.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

#### **HN8** **Robinson-Patman Act, Claims**

Under the Robinson-Patman Anti-Discrimination Act, in a situation where a wholly independent buyer purchases from a defendant seller, and there is no evidence of collusion or control between the seller and the independent buyer, the flow of commerce has ended and the intrastate seller cannot be held to have made the sale in commerce as a result of a subsequent interstate sale made by the independent buyer.

**Counsel:** Gina Ismalia Gutierrez-Galang, with whom Law Office Pedro E. Ortiz Alvarez was on brief, for appellant.

Carlos A. Rodriguez Vidal, with whom Myriam Fernandez Gonzalez, and Goldman Antonetti & Cordova, P.S.C. were on brief, for appellee.

**Judges:** Before Selya and Lynch, Circuit Judges. \*

**Opinion by:** LYNCH

## Opinion

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[\*57] **LYNCH, Circuit Judge.** This case presents the issue of the meaning of the jurisdictional "in commerce" requirement of § 2(a) of the Robinson-Patman Anti-Discrimination Act, [15 U.S.C. § 13](#).

Judgment was entered under the Act for Able Sales ("Able") and against Compania de Azucar de Puerto Rico ("CAPR"), a corporation that is primarily engaged in the refining of raw sugar and the subsequent sale of this sugar in the local Puerto Rico market. CAPR argues on appeal that the district court [\*2] did not have subject matter jurisdiction to entertain the suit brought by Able because the "in commerce" requirement was not met. Able is a corporation primarily engaged in the importation and distribution of refined sugar [\*58] in the local Puerto Rico market and a competitor of CAPR.

Specifically, CAPR argues that its sale of refined sugar to various local wholesalers and retailers in Puerto Rico does not satisfy the "in commerce" requirement of the statute. Able counters that any of three separate transactions -- (1) CAPR's importation of raw sugar into Puerto Rico for refinement and sale; (2) Able's importation of refined sugar from Florida; and/or (3) CAPR's sale of refined sugar to a local company which planned to export the sugar -- independently satisfy this requirement and thus provide a basis for subject matter jurisdiction in the district court.

The district court agreed and after a two day bench trial found that CAPR had violated [§ 2\(a\) of the Robinson-Patman Act](#) and awarded \$ 1,949,259.00 in damages to Able.

We hold that the transactions do not satisfy the "in commerce" requirement, reverse the judgment, and remand with directions that judgment be entered for CAPR. <sup>1</sup>

[\*\*3] I.

We briefly recount the facts, largely as found by the district court. CAPR does not dispute the district court's characterization of the facts.

Until December of 2000, the Puerto Rico Sugar Corporation ("PRSC"), a public corporation created by a Resolution of the Board of Governors of the Puerto Rico Land Authority in 1973, was the sole supplier of "Snow White" brand refined sugar in Puerto Rico. The Puerto Rico Department of Consumer Affairs ("DACO") established regulations which required PRSC to sell all of its two and five pound bags of refined sugar to ten exclusive distributors, one of which was Able. These distributors then sold the bags to wholesalers and retailers; DACO fixed the maximum prices for sugar that the distributors could offer.

In January 2001, the Puerto Rico Legislature moved away from governmental ownership and privatized the local sugar industry. See *5 P.R. Laws Ann. § 430a*. It transferred the operations and assets of the Mercedita Refinery to CAPR. Until September 2001, CAPR sold the existing inventory of refined sugar from the refinery to the distributors,

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\* Circuit Judge Torruella participated in oral argument in this case, but has since recused himself and has not participated in the decision of the case. The remaining two panelists, pursuant to 28 U.S.C. § 46(d), issue this opinion.

<sup>1</sup> Because we set aside the judgment awarded to Able, we do not address CAPR's second argument on appeal: that the district court erred in the calculation of damages.

including Able, at the price of \$ 43.23 per hundredweight, **[\*\*4]** as established by DACO and as previously offered by the PRSC.

By September 2001, CAPR had sold all the Mercedita inventory and was unable to supply the local demand for refined sugar. Due to the lack of refined sugar, Able and another distributor, in agreement with DACO, imported refined sugar required for local consumption, with the expectation that CAPR would later import raw sugar, refine it, and resume the previous distributor system. Because the cost of the imported refined sugar was higher than the price established by DACO, DACO issued an order which allowed the importers to sell the refined sugar to other distributors and wholesalers at a higher price than had been previously permitted by regulation. The new, higher price for distributors was \$ 46.10 per hundredweight; distributors sold to wholesalers at the price of \$ 48.54 per hundredweight. This order was vacated in January of 2002, and the lower prices were reinstated.

CAPR, having sold all of its inventory of refined sugar, needed a new source of supply if it wished to continue in the business. **[\*59]** It chose to import raw sugar to refine. In a one-time purchase, CAPR imported approximately 12,000 tons of raw sugar into Puerto **[\*\*5]** Rico which it refined at its Mercedita facility. There is no evidence of any further importation of raw sugar by CAPR. Able attempted to buy refined sugar from CAPR (apparently refined from this one-time importation of raw sugar) at the distributors' price (\$ 43.23 per hundredweight), but on December 26, 2001, CAPR notified Able that it was cutting distributors from its sales strategy and would no longer be selling to distributors. Instead, CAPR would be selling directly to wholesalers and retailers: if Able wanted to buy CAPR's refined sugar, it could do so at the wholesalers' price (not the lower distributors' price). Unfortunately for Able, this price was also the maximum price that Able could, by law, sell to its clients.

Thus CAPR moved from being a supplier to Able, which was a distributor, to being a direct competitor to Able, with CAPR also acting as a distributor and selling directly to wholesalers. Both CAPR and Able sold directly to wholesalers and retailers, all of which were local Puerto Rico entities. One wholesaler, Tropical, purchased refined sugar from CAPR for export.

In an effort to make a profit and compete with CAPR, from January to February of 2002, Able imported **[\*\*6]** from Florida refined sugar at a cost of \$ 44.63 per hundredweight under the trademark "Florida Crystal." In conformance with DACO guidelines, Able anticipated selling the sugar to wholesale clients at \$ 47.54 per hundredweight.

Shortly thereafter, CAPR reduced the price of the sugar it had refined for sale to wholesalers from \$ 47.54 to \$ 45.10 per hundredweight. This was the beginning of the alleged period of predatory pricing. Able was forced to reduce its price as well to compete with CAPR.

At the end of April 2002, CAPR again reduced its price to wholesalers, this time to \$ 43.30 per hundredweight. This lower price was not enough to cover CAPR's costs, which consisted of the costs of refining the raw sugar, the sale of the now-refined sugar, and the excise tax of \$ 14.00 per hundredweight which CAPR was obligated to pay to the Puerto Rico Department of the Treasury. Throughout the time that CAPR was lowering its prices, it did not pay this excise tax as required by law.

Despite Able's efforts to compete with CAPR, it lost a number of its clients and its market share was reduced by between forty and fifty percent. The district court found that other distributors were eliminated **[\*\*7]** from the market as a result of CAPR's pricing.<sup>2</sup> In September 2002, CAPR exhausted its inventories and did not purchase any additional raw sugar. There is no further evidence in the record as to whether CAPR has remained in the business of selling refined sugar to wholesalers after it had exhausted the inventory of sugar it had refined from the one-time import of the 12,000 tons of raw sugar.

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<sup>2</sup>CAPR does point out that Able's chairman admitted at trial that the other two and five pound bag sugar distributors ceased operations on January 1, 2002, prior to the alleged predatory pricing period from February of 2002 to September of 2002. The district court's finding, however, has no bearing on whether or not there is subject matter jurisdiction; we merely note the discrepancy.

Able filed the verified complaint on May 22, 2002 averring its version of the facts and alleging that CAPR engaged in "predatory pricing" in violation of the Robinson-Patman Act, [15 U.S.C. § 13](#). Specifically, Able stated: [\[\\*\\*8\]](#)

**[\*60]** Defendant's practice consists of distributing sugar at prices lower than the costs of its inventory. The objective of said pricing structure is to eliminate Able Sales from the market, to allow CAPR to prevail upon the market as the sole sugar distributor in Puerto Rico. . . . [This] practice will then enable [CAPR] to recoup the losses sustained during its current scheme of predatory pricing.

On June 5, 2002, the summons, a copy of the verified complaint, and Able's first set of interrogatories and requests for production were served on CAPR. On August 9, 2002, after two extensions of time, CAPR filed an answer. After CAPR's continual failure to comply with discovery orders, the district court, pursuant to an Order of October 28, 2003, struck CAPR's answer to the complaint and its affirmative defenses. CAPR does not appeal this order.

On November 12 and 13, 2003, a bench trial was held before the district judge. At trial, Able presented documentary evidence, testimony of the Chairman of the Board of Able Sales, and an expert who testified as to Able's damages. CAPR was given an opportunity to present evidence and to cross examine witnesses. CAPR declined to present [\[\\*\\*9\]](#) evidence, but did cross examine witnesses.

Having stricken the defendant's answers and affirmative defenses from the record, the court determined that CAPR engaged in primary line price discrimination in contravention of the Robinson-Patman Act. The court stated, "this case clearly entails a primary-line price discrimination, in which CAPR imported raw sugar from sources outside of Puerto Rico, refined it at the Mercedita Refinery, and sold the refined sugar at below cost so as to eliminate its competitors."

CAPR challenged the court's subject matter jurisdiction, contending the "in commerce" requirement was not satisfied. The court found that it did have subject matter jurisdiction based on either CAPR's importation of raw sugar which it found remained in the flow of commerce or Able's importation of refined sugar.<sup>3</sup>

## **[\*\*10] II.**

Price discrimination is made unlawful by [§ 2\(a\) of the Clayton Act](#), as amended by the Robinson-Patman Act, which provides:

**HN1** It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality . . . where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them . . . .

[15 U.S.C. § 13\(a\)](#); see [Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 219-20, 125 L. Ed. 2d 168, 113 S. Ct. 2578 \(1993\)](#). **HN2** The statute encompasses two different types of violations: primary line violations and secondary line violations. Primary line violations are directed at injuring competition with the discriminating seller's direct competitors, whereas secondary line violations are directed at injuring competition among the discriminating seller's customers. [\[\\*\\*11\]](#) See [I\\*611 Coastal Fuels of P.R., Inc. v. Caribbean Petroleum Corp., 79 F.3d 182, 188 \(1st Cir. 1996\)](#); IA Areeda & Hovenkamp, [Antitrust Law](#) P 267c, at 329-30 (2d ed. 2000). In this case, the district court found that CAPR had committed a primary line violation by engaging in predatory pricing.<sup>4</sup>

<sup>3</sup> In a footnote, the district court referenced the transaction between Tropical and CAPR as a basis for subject matter jurisdiction and stated "CAPR did sell refined sugar for exportation."

<sup>4</sup> **HN3** In general, primary line violations involve a claim by the injured party that "[a] business rival has priced its products in an unfair manner with an object to eliminate or retard competition and thereby gain and exercise control over prices in the

[\*\*12] Whether the district court has subject matter jurisdiction over these types of violations is largely determined by the Supreme Court's decision construing § 2(a) of the Robinson-Patman Act, [15 U.S.C. § 13\(a\)](#), in [Gulf Oil Corp. v. Copp Paving Co., 419 U.S. 186, 42 L. Ed. 2d 378, 95 S. Ct. 392 \(1974\)](#). *Gulf Oil*, which involved a secondary line violation, held, as all parties agree, that [HN4](#) [§ 2(a) of the Robinson-Patman Act] did not extend jurisdiction to the full extent of Congress's constitutional power granted by the [Commerce Clause](#). *Id.* at 199-200. The Court stated:

The distinct "in commerce" language . . . appears to denote only persons or activities within the flow of interstate commerce . . . . The jurisdictional requirements of these provisions cannot be satisfied merely by showing that allegedly anticompetitive acquisitions and activities affect commerce.

[Id. at 195](#). To satisfy the "in commerce" requirement, one of the discriminatory sales must cross a state line. See [Id. at 195](#); [Coastal Fuels, 79 F.3d at 190](#). As this requirement is jurisdictional, [\*\*13] see [Gulf Oil, 419 U.S. at 195](#), the burden to prove the interstate character of the sales is on the party asserting subject matter jurisdiction. See [Bull HN Info. Sys. v. Hutson, 229 F.3d 321, 328 \(1st Cir. 2000\)](#) (the party asserting jurisdiction has the burden of proving it).

In an effort to meet this burden, Able points to three transactions which it argues satisfy the "in commerce" requirement of [§ 2\(a\)](#): (1) CAPR's importation of raw sugar into Puerto Rico for refinement and sale; (2) Able's importation of refined sugar from Florida; and (3) CAPR's sale of refined sugar to Tropical with the knowledge that Tropical planned to export this sugar.

#### A. Focus on Plaintiff's Activities

We first reject Able's argument that the "in commerce" element may be satisfied by reviewing the interstate activities of the *plaintiff*, whether or not the defendant has acted "in commerce." Specifically, Able argues that it imports refined sugar from Florida for sale in Puerto Rico, and this transaction crosses state lines. We disagree that the plaintiff's sales can be used to satisfy the "in commerce" requirement of [§ 2\(a\) of the Robinson-Patman Act](#) [\*\*14].

[HN5](#) [Following the language of the statute, the Supreme Court in *Gulf Oil* held<sup>5</sup> that in order to satisfy the "in commerce" requirement of the [§ 2\(a\) of the Robinson-Patman Act](#), the *defendant's* activities must satisfy the following test:

[\*62] Unless it appears . . . that the [defendant's] alleged exclusive-dealing arrangements and discriminatory sales occur in the course of its interstate activities . . . and . . . that at least one of [defendant's] allegedly discriminatory sales was made in interstate commerce . . . , plaintiff's claims must fail.

[Gulf Oil, 419 U.S. at 195](#).<sup>6</sup> In other words, "if one of the discriminatory sales is 'in commerce,' the seller is engaged in commerce and discrimination has occurred in the course thereof." IA Areeda and Hovenkamp, [Antitrust Law](#) P

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relevant market." [Brooke Group, 509 U.S. at 222](#); see also III Areeda & Hovenkamp, [Antitrust Law](#) P 745e, at 477 (2d ed. 2002). We express no view as to whether the district court correctly determined that the facts alleged by Able establish a primary line violation of [§ 2\(a\) of the Robinson-Patman Act](#). This issue has not been raised on appeal. The only question before us is whether the "in commerce" requirement of the Robinson-Patman Act is satisfied.

<sup>5</sup> We have excluded language concerning the requirements as to [§ 7 of the Clayton Act](#), as no [§ 7](#) allegations are made here.

<sup>6</sup> To support the finding that Able's transactions could satisfy the "in commerce" requirement, the district court erroneously read language in *Gulf Oil* that states, " [§ 2\(a\)](#) applies where at least one of the two transactions which, when compared, generate a discrimination . . . crosses a state line." [Gulf Oil, 419 U.S. at 200](#) (internal citation and quotation marks omitted). *Gulf Oil* involved

267c, at 329 (2d ed. 2000). The activities which must meet the in commerce requirements are the sales by the defendant seller.

[\*\*15] A focus on the defendant's sales is consistent with Congressional purpose. As the Supreme Court stated in *Standard Oil Co. v. FTC*, 340 U.S. 231, 95 L. Ed. 239, 71 S. Ct. 240, 47 F.T.C. 1766 (1951), "the recognized purpose of the Robinson-Patman Act [is] to reach the operations of large interstate businesses in competition with small local concerns." *Id. at 237-38*. Congress was concerned with predatory pricing by defendants who engaged in interstate commerce, not by those who acted purely locally. See *Gulf Oil*, 419 U.S. at 200-01 (reading the clear language of § 2 to exclude from the reach of the statute "a multitude of local activities that hitherto have been left to state and local regulation").

To impose liability on a defendant seller for activities within the sole control of a plaintiff competitor would itself be anti-competitive, and contrary to the purposes of the Robinson-Patman Act. A defendant seller must be able to know when it is subject to Robinson-Patman Act liability in order to conform its behavior to the law. We focus therefore only on the defendant's behavior. We reject the argument that the sales activity of the plaintiff, Able's [\*\*16] importation of refined sugar from Florida, can be the basis for satisfying the "in commerce" jurisdictional requirement of the statute.

#### *B. Defendant's Alleged Interstate Transactions*

##### *1. CAPR's Importation of Raw Sugar Across State Lines*

Able argues that even though CAPR's sales of refined sugar did not cross state lines, these sales satisfy the "in commerce" requirement because CAPR imported 12,000 tons of raw sugar,<sup>7</sup> and CAPR's refinement in Puerto Rico of this imported sugar did not remove the sugar from the "flow of commerce." This is an aspect of the doctrine concerned with the "flow backward" [\*63] into interstate transactions in raw materials." IA Areeda & Hovenkamp, *Antitrust Law* P 267b, at 324 (2d ed. 2000).

[\*\*17] Whatever the present contours of the in the "flow of commerce" doctrine under the Robinson-Patman Act, it certainly does not apply when there are material differences between the product imported and the product sold after undergoing processing. The fact that the raw materials were imported into Puerto Rico does not necessarily mean that the "in commerce" requirement of § 2(a) of the Robinson-Patman Act is met. See *Belliston v. Texaco, Inc.*, 455 F.2d 175, 180 (5th Cir. 1972) (The production of gasoline from crude oil is a "highly complex process" which interrupts the flow of commerce). Indeed the "flow of commerce" ends when these raw materials or goods are "transformed in a material way." See IA Areeda & Hovenkamp, *Antitrust Law* P 267b, at 324 (2d ed. 2000).

CAPR argues that the imported raw sugar was transformed in such a material way when it underwent refining into refined sugar. CAPR states that the raw sugar was "extensively processed within Puerto Rico, resulting in an alteration of the nature of the product" and that the refinement process "extracts molasses and other non-sugar minerals [from] the raw sugar."

We agree that the refinement of [\*\*18] raw sugar into refined sugar has transformed this product so that it cannot be fairly said to continue to be in the flow of commerce. This case is distinguishable from cases where courts have found the flow of commerce was not interrupted. This is not a case in which the same product was temporarily stored in the state of ultimate sale. See, e.g., *Standard Oil Co.*, 340 U.S. at 237-38 (temporary storage of gasoline

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a secondary line violation which requires, among other things, the discriminating seller to sell to one buyer (the favored buyer) at a lower price than to another buyer (the disfavored buyer). The two transactions to be compared, as this court's opinion in *Coastal Fuels* explained, are "either the sale to the favored buyer or the sale to the buyer allegedly discriminated against." *Coastal Fuels*, 79 F.3d at 189. In either a primary line violation or a secondary line violation, it is the sales by the defendant which are the focus.

<sup>7</sup> CAPR suggests in its reply brief that the one-time importation of raw sugar cannot satisfy the "in commerce" requirement of § 2(a) because CAPR did not regularly import products from across state lines and there was not a "constant flow" of raw sugar into Puerto Rico. We express no view on the validity of this argument.

does not deprive the gasoline of its interstate characteristic). Nor is it a case in which the resulting sold product was essentially the same as the imported product. See, e.g., [Dean Milk Co. v. FTC, 395 F.2d 696, 715 \(7th Cir. 1968\)](#); [Foremost Dairies, Inc. v. FTC, 348 F.2d 674, 678 \(5th Cir. 1965\)](#) (both holding that the processing of milk imported from out of state before local resale is not enough to remove the milk from the flow of commerce).

Despite stating that the refinement of sugar involves "negligible processing" and that the processes involved in this case are similar to those involved in the processing of milk as in the examples given above, the plaintiff does not seriously dispute CAPR's claim [\*\*19] as to the nature of the refinement process.<sup>8</sup> Accordingly Able has not met its burden of showing that the imported raw sugar remained in the flow of commerce. This transaction does not satisfy the "in commerce" requirement.

## 2. CAPR's Sale to Tropical for Export

In contrast with Able's previous argument concerned with backward interstate movement of materials, Able makes a forward flow argument as its final argument. See IA Areeda & Hovenkamp, [Antitrust Law](#) P 267b, at 324 (2d ed. 2000). Whether CAPR's sale of sugar to Tropical, knowing that Tropical planned to export the sugar, can satisfy the "in commerce" requirement [\*\*20] is a more complex question.

[\*64] From the 2002 sales summary, it appears that CAPR apparently made six sales of an indeterminate number of two pound bags of refined sugar and four sales of five pound bags of refined sugar to Tropical in 2002. Two of those sales were in the \$ 43 to \$ 46 range per hundredweight, and the rest were in the \$ 30 range. A notation next to the sales to Tropical suggests that those sales received a special discount because Tropical intended to export the sugar, presumably outside of Puerto Rico. These sales were likely discounted because CAPR does not have to pay an excise tax on such sales, as explained by Able's counsel.<sup>9</sup>

[\*\*21] We take Able's argument to be a permutation of the "flow of commerce" theory: the initial sale between CAPR and Able took place intrastate, but the goods remained in the "flow of commerce" because they were to be exported by Tropical and CAPR's knowledge of that puts the goods into the flow of commerce. The interstate activity of the buyer is therefore attributed back to CAPR, the intrastate seller, under the theory.

This forward flow theory may be arguable on certain facts. Cases under statutes based on the full scope of Congress' constitutional commerce power over certain types of intrastate transactions have suggested "so far as the [intrastate] sales are for shipment to other States or to foreign countries, it is idle to contend that they are not sales in interstate or foreign commerce and subject to congressional regulation." [Curran v. Wallace, 306 U.S. 1, 10, 83 L. Ed. 441, 59 S. Ct. 379 \(1939\)](#) (challenging the [Tobacco Inspection Act of 1935](#)); see also [United States v. Rock Royal Co-Op., 307 U.S. 533, 568-69, 83 L. Ed. 1446, 59 S. Ct. 993 \(1939\)](#) (challenging the Secretary's regulation of the handling of milk in the New York metropolitan area under the Agricultural Marketing Agreement Act of 1937 [\*\*22]). But of course, the scope of the "in commerce" clause of the Robinson-Patman Act is less than the constitutional reach.

While [Gulf Oil](#) held that a mere nexus to interstate commerce was insufficient, it did not decide whether some intermediate definitions of "in commerce" to capture the "practical consequences" of a discriminatory sale on national markets might be within Congressional intent. [Gulf Oil, 419 U.S. at 199](#). Indeed the Court specifically noted the absence of two claims: that the defendant made interstate sales or was "otherwise directly involved in national

<sup>8</sup> The district court did not make a specific finding as to whether the refinement process interrupted the flow of commerce. In response to CAPR's argument that it did, the district court stated, "even if the CAPR's refined sugar is not considered to be in the flow of commerce, Able Sales' refined sugar, which does not undergo any processing, is undeniably within the flow of commerce."

<sup>9</sup> We do not understand Able to say it could not buy from CAPR at the same price Tropical did for sugar, whether intended for export or not. Nor does Able say that it and Tropical compete with each other to export sugar from Puerto Rico. We understand Able's argument to be based on an overall theory of predatory pricing, that CAPR artificially lowered its price in order to drive Able, its competitor in the distribution of sugar, out of business.

markets" or that the "local market . . . is an integral part of the interstate market in other component commodities or products." *Id. at 195-96.*

But the record before us does not establish and indeed the plaintiff does not argue that either of those situations apply. Ultimately, Able fails to prove that the "flow of commerce" test is satisfied. The only evidence that Able points to concerning the sale from CAPR to Tropical is a sales summary of the sale to Tropical which has the notation, "special price for exportation of sugar, plus taxes," and [\*\*23] a statement made by Able's trial counsel to the district court that "among the sales that [CAPR] was able to execute during that year, one of their clients, Tropical Distributors, was sold sugar at a special price because he was going to export sugar."

[\*65] For several reasons this evidence is insufficient to prove that the sale was "in commerce." *HN6* The flow of commerce is thought to end when the goods "are stored in a [seller's] warehouse or storage facility for general inventory purposes," subject to an exception for when the goods are purchased and then stored in the seller's warehouse in response to a particular customer's needs. See *Zoslaw v. MCA Distributing Corp., 693 F.2d 870, 878 (9th Cir. 1982)*. That exception does not apply here. There is no evidence that CAPR's sale to Tropical was anything other than final, with Tropical taking possession of the sugar. Indeed, there is no evidence whether Tropical actually ever exported the sugar. But what Tropical, an independent company, intended to do with the sugar, in these circumstances, is not germane to the "in commerce" inquiry.

While there is evidence of negotiation over price and that CAPR expected that Tropical [\*\*24] would export the sugar, there is no evidence that CAPR exercised any control of the management, business, or distribution decisions of Tropical. *HN7* In cases where the "flow of commerce" doctrine applied, the same entity has engaged in both the intrastate and interstate transaction. See, e.g., *Standard Oil, 340 U.S. at 237* (intrastate sale was in the flow of commerce; both the intrastate and interstate transactions were conducted by the same entity); *Foremost Dairies, 348 F.2d at 676-77* (same). And courts have held that to the extent that the purchasers are independent distributors in their pricing and marketing decisions, the "flow of commerce" is interrupted by the sale of the product. See *Zoslaw, 693 F.2d at 880*; cf., *Acme Refrigeration of Baton Rouge, Inc. v. Whirlpool Corp., 785 F.2d 1240, 1243-44 (5th Cir. 1986)* (a subsidiary's sales could not be imputed to its parent company if the parent company did not "control" the subsidiary).

*HN8* In a situation where a wholly independent buyer purchases from the defendant seller, and there is no evidence of collusion or control between the seller and the independent [\*\*25] buyer,<sup>10</sup> the flow of commerce has ended and the intrastate seller cannot be held to have been made "in commerce" as a result of the subsequent interstate sale made by the independent buyer.

### III.

We hold that the district court did not have subject matter jurisdiction over this suit as CAPR's allegedly discriminatory sales were not "in commerce." We **reverse** the decision of the district court, set aside the award of damages against CAPR, and remand with instructions to dismiss the case for lack of jurisdiction. Costs are awarded to CAPR.

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<sup>10</sup> Areeda also warns against reliance on a party's intentions, as opposed to actions, except to cover the situations of "evasions calculated to keep illegal activities entirely intrastate while employing the channels of interstate commerce." IA Areeda & Hovenkamp, *Antitrust Law* P 267 b, at 324-327 (2d ed. 2000).



## In re Polyester Staple Antitrust Litig.

United States District Court for the Western District of North Carolina, Charlotte Division

May 6, 2005, Decided; May 9, 2005, Filed

MDL DOCKET NO: 3:03CV1516 ALL CASES

### **Reporter**

2005 U.S. Dist. LEXIS 47179 \*; 2005 WL 6457181

### **IN RE POLYESTER STAPLE ANTITRUST LITIGATION**

**Subsequent History:** Motion granted by, in part, Motion denied by, in part, Sanctions allowed by, in part, Motion granted by [In re Polyester Staple Antitrust Litig., 2005 U.S. Dist. LEXIS 40565 \(W.D.N.C., Sept. 7, 2005\)](#)

**Prior History:** [In re Polyester Staple Antitrust Litig., 2004 U.S. Dist. LEXIS 32281 \(W.D.N.C., Feb. 5, 2004\)](#)

## **Core Terms**

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purchasers, discovery, documents, yarn, indirect, conspiracy, poly-cotton, antitrust, polyester, staple, downstream, damages, manufactured, prices, customers, open-end, cotton

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**Judges:** Richard L. Voorhees, United States District Judge.

**Opinion by:** Richard L. Voorhees

## Opinion

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**ORDER GRANTING IN PART AND DENYING IN PART DEFENDANTS' MOTION TO COMPEL PARKDALE AND AVONDALE TO PRODUCE DOCUMENTS RELATED TO ALLEGED POLYESTER-COTTON YARN PRICE-FIXING CONSPIRACY**

**THIS MATTER** comes before the Court on Motion To Compel Plaintiffs Parkdale America, LLC and Parkdale Mills, Inc. ("Parkdale") and Plaintiff Avondale Mills, Inc. ("Avondale") to produce discovery, filed by Defendants Nan Ya Plastics Corporation, America ("Nan Ya America"), Wellman, Inc. ("Wellman"), and Arteva Specialties S.a'.r.l. d/b/a/ KoSa, now named INVISTA [**\*9**] S.a'.r.l.; Arteva Services, S.a'.r.l.; and Koch Industries, Inc. ("KoSa").<sup>1</sup> (Documents # 222, # 223) Plaintiffs Parkdale and Avondale have both responded to Defendants' motion, Defendants submitted reply briefs, and all of the parties have now submitted supplemental filings and, in some cases, related correspondence. (Documents ## 226-230; # 240, # 241, # 245) On January 6, 2005, the United States ("Government") also filed an amicus brief under seal. (Documents # 224, # 225)

On January 27th and 28th of 2005, Plaintiffs Parkdale and Avondale filed Motions To Strike the Declaration of Richard T. Rapp, which was filed as an attachment to KoSa's reply brief. (3:03CV1516 / Documents # 231, # 232, # 234 and # 238; 3:03CV296 / Document # 31) KoSa opposes Plaintiffs' motions.<sup>2</sup>

## I. Relevant Background

These [**\*10**] cases arise out of allegations by individual and class plaintiffs that beginning as early as 1995, and continuing at least through 2001, Defendants and their alleged co-conspirators agreed, combined and conspired with each other to fix, raise, maintain and / or stabilize the price of polyester staple and to allocate markets and / or customers for the sale of polyester staple in the United States.<sup>3</sup> (Consol. Am. Compl. at 2.) Plaintiffs collectively allege that as a result of Defendants' unlawful conduct and conspiracy, Plaintiffs paid artificially inflated prices for polyester staple fiber ("PSF"). Plaintiffs primarily assert that Defendants violated Sections 4 and 16 of the Clayton Act, [15 U.S.C. §§ 15](#) and [26](#), and Section 1 of the Sherman Act, [15 U.S.C. § 1](#).

Some of the Plaintiffs in this litigation allegedly made direct purchases of PSF from the Defendants while other Plaintiffs made indirect purchases of PSF.<sup>4</sup> In some instances, Plaintiffs allege that they made both direct and indirect purchases. In fact, Avondale and Parkdale are considered both direct and [**\*11**] indirect purchasers of PSF.<sup>5</sup> (Avondale's Second Am. Compl., P3) (Parkdale's Compl., P3, 8, 55, 63) There is yet another category of Plaintiffs in this case that claim to be indirect purchasers of PSF as a result of having purchased yarn containing PSF. Of this group, Plaintiff Springs Industries expressly alleges it purchased yarn containing PSF directly from Parkdale.<sup>6</sup> (Defendants' Exh. D / Springs Industries' Compl., P8) In addition to their prayers for relief as direct purchasers,

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<sup>1</sup> The Nan Ya Defendants (Nan Ya Taiwan, Nan Ya America and Robert Bradley Dutton) recently settled claims against them with all Non-Class Plaintiffs, including Parkdale and Avondale. Although Nan Ya America has not notified the Court that it no longer seeks to compel production from Parkdale and / or Avondale, presumably this issue is moot as to these parties.

<sup>2</sup> Wellman does not rely on the Rapp Declaration.

<sup>3</sup> Polyester staple is an essential raw material for many kinds of textiles and is also used to make a wide range of products.

<sup>4</sup> An indirect purchase of PSF may occur if Plaintiff purchased PSF from a third-party (not a Defendant in this action) or if Plaintiff purchased a product containing PSF rather than the raw material.

<sup>5</sup> Avondale and Parkdale seek monetary damages as indirect purchasers under state law, [N.C. Gen. Stat. § 75-1.1](#). (Avondale's Second Am. Compl., PP3,80; Parkdale Compl., PP63,64)

<sup>6</sup> Plaintiff National Textiles allegedly made indirect purchases of PSF "in finished yarn products manufactured by certain defendants" and "purchased [**\*12**] yarn that incorporated PSF manufactured by one or more defendants." (Defendants' Exh. E / National Textiles' Compl., PP3, 8,29) WestPoint Stevens' Complaint alleges it "purchased products containing PSF from third parties during the Conspiracy period." (Defendants' Exh. F / West Point Stevens' First Am. Compl., P3). Russell alleges it "purchased yarn that contained PSF manufactured and sold by defendants. . ." (Defendants' Exh. G / Russell's Compl., PP3, 8, 29). Dan River "purchased PSF in finished yarn products and fabric containing PSF manufactured by certain defendants . . ." (Unidentified Defendants' Exh. / Dan River's Compl., PP3,8,29).

many of these individual or non-class PSF Indirect Purchaser Plaintiffs (also direct purchasers of poly-cotton yarn) also seek redress, including monetary damages, pursuant to state law.<sup>7</sup>

In November 2004, Defendants first requested discovery from Plaintiffs Parkdale and Avondale related to an investigation into an alleged conspiracy to violate the antitrust laws in the spun yarn industry. Plaintiffs objected to Defendants' request. On February 11, 2004, Unifi, Inc., which along with Parkdale Mills, Inc., owns Parkdale America, LLC, issued a press release stating that "Parkdale participated in activities with competitors in the [\*13] markets for open-end and air-jet cotton and polycotton yarns used in the manufacture of hosiery and other garments that may have resulted in violations of U.S. antitrust laws," and that Parkdale "voluntarily disclosed the activities to the U.S. Department of Justice Antitrust Division . . . and that DOJ has launched an investigation of the activities. . ." (Defendants' Exhibit B / Press Release, *Unifi, Inc., Equity Affiliate Informs Unifi of Pending Investigation* (Feb. 11, 2004)). The record does not reflect whether the DOJ's leniency or amnesty program has come into play relative to any potential criminal prosecution of Parkdale.<sup>8</sup>

According to KoSa, Avondale has received a subpoena from the Department of Justice in connection with the poly-cotton yarn ("PCY") investigation and is an "obvious [\*14] focus" given its status as one of the largest open-end spun yarn spinners in North America. (2/16/05 Letter from Edward B. Davis).

In April 2004, class action suits were commenced against Parkdale and Avondale, among others, alleging violations of the antitrust laws, namely, conspiring to fix, raise, maintain or stabilize prices for open-end and air-jet cotton and polycotton yarns.<sup>9</sup> (Defendants' Exhibit C) These civil actions are now consolidated in the Middle District of North Carolina before The Honorable James Beaty, Jr., pursuant to the order of the Judicial Panel on Multidistrict Litigation.<sup>10</sup> (See MDL 1622 In Re Cotton Yarn Antitrust Litigation). The PCY conspiracy allegedly existed from approximately February 12, 2000 to April 2004. Thus, if proven, the PSF and PCY conspiracies overlapped from approximately February 12, 2000 to April 2001. Defendants assert that some of the larger manufacturer Plaintiffs in this case have claims against Parkdale and Avondale in the PCY litigation that overlap with their claims for damages in this PSF litigation. (Defendants' Exh. D)

In a previous Order, dated February 15, 2004, this Court ruled in favor of Plaintiffs in denying Defendants' request to obtain from Plaintiffs "downstream discovery" (or "downstream data"). Downstream discovery consists primarily of Plaintiffs' production costs and profit data for each end-use or product that was manufactured incorporating polyester staple. This Court noted that "Defendants do not purport to seek the information in order to oppose Plaintiffs' calculation of damages." (2/15/04 Order at 5, n.4) The Court also recognized that downstream data may be relevant as to damages claims made by Indirect Purchasers, but found Defendants' request unduly burdensome.<sup>11</sup> (*Id.* at 6.)

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<sup>7</sup> The Indirect Purchaser Class does not seek monetary damages. (Delta Clothing's Am. Compl., 3:02CV503-V)

<sup>8</sup> At least one individual, a former vice president of sales for the now defunct North Carolina-based yarn spinner company Harriet & Henderson Yarns, Inc., has agreed to enter a guilty plea in the Eastern District of North Carolina. This individual admitted participation in the alleged conspiracy to violate the antitrust laws within the spun yarn industry. (See Press Release, DOJ, (Feb. 10, 2005)).

<sup>9</sup> Polyester staple can be either spun by itself into yarn or blended with cotton and spun into yarn.

<sup>10</sup> In the polyester [\*15] cotton yarn ("PCY") civil litigation, the Direct Purchaser Class Plaintiffs define yarn as follows:

"Yarn" means open-end, air jet cotton and / or poly-cotton yarn, which is textured yarn utilized in connection with the manufacture of home furnishings, apparel and industrial fabrics, automotive, upholstery, hosiery, and sewing thread, and is produced through the yarn spinning process."

(Defendants' Exhibit C, P5 at 2.)

<sup>11</sup> The undersigned did not reach the issue regarding Indirect Purchasers' ability to recover [\*16] monetary damages under North Carolina law. (*Id.* at 6, n.6)

## II. FED. R. CIV. P. 26(b)

*Rule 26(b)(1) of the Federal Rules of Civil Procedure* provides that, "[p]arties may obtain discovery regarding any matter, not privileged, that is relevant to the claim or defense of any party. . ." *FED. R. CIV. P. 26(b)(1)*. "Relevant information need not be admissible at the trial if the discovery appears reasonably calculated to lead to the discovery of admissible evidence." *Id.* However, discovery may be limited by the Court if it finds that, "the burden or expense of the proposed discovery outweighs its likely benefit, taking into account the needs of the case, the amount in controversy, the parties' resources, the importance of the issues at stake in the litigation, and the importance of the proposed discovery in resolving the issues." *FED. R. CIV. P. 26(b)(2)(iii)*.

## III. Analysis

### A. Plaintiffs' Motions To Strike Affidavit Of Richard T. Rapp

Regarding Plaintiffs' motions to strike, the Court will deny Parkdale's and Avondale's motions. *Rule 6(d) of the Federal Rules of Civil Procedure* requires that "[w]hen a motion is supported by affidavit, the affidavit shall be served with the motion." *FED R. CIV. P. 6(d)*(emphasis [\*17] added). However, *Rule 6(d)* does not preclude the filing of an affidavit in support of a reply. *McGinnis v. Southeast Anesthesia Associates, P.A.*, 161 F.R.D. 41 (W.D.N.C.1995)(denying motion to strike where affidavit supported reply and striking affidavit would conflict with *Rule 6(d)*'s ultimate objective of resolving the motion on its merits). Notwithstanding KoSa's alleged violation of any procedural rules, namely, *FED R. CIV. P. 6(d)* and *L.R. 7.1(B)*, Plaintiffs cannot demonstrate any prejudice sustained as a result of the declaration. Plaintiffs had an opportunity, via the instant motion to strike, to address their concerns. Moreover, to grant Plaintiffs' motion would be inconsistent with federal policy favoring disposition based upon the merits of the underlying issue.

### B. Defendants' Motion To Compel Production Of Documents

Defendants' motion seeks production of materials relating to an investigation by the United States Department of Justice ("DOJ") into Parkdale's and Avondale's alleged involvement in a PCY price-fixing conspiracy.<sup>12</sup> Specifically, Defendants propounded the following discovery request to Parkdale and Avondale:

Request for Production No. 1: All documents relating [\*18] to any inquiry or investigation by the United States Department of Justice, any other governmental agency, federal or state, or any grand jury, relating to the pricing, distribution, purchase, or sale of open-end and / or jet cotton and / or poly-cotton yarn, or any other product manufactured by you an input of which includes polyester staple, including, but not limited to, all documents made available by you to any of these agencies, all documents you produced in response to any subpoena, informal request or otherwise, and all documents relating to any communication between you and any of these agencies.

(Defendants' Exhibit A at 4.) Thus, the nature of Defendants' request is essentially the same as the earlier request to produce downstream discovery in that PCY is an "end-use" of PSF.<sup>13</sup> The Court now addresses each of Defendants' legal arguments.

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<sup>12</sup> The United States opposes Defendants' motion to compel with respect to the documents disclosed in connection with its ongoing criminal investigation being conducted by the Antitrust Division of the United States Justice Department within the Eastern District of North Carolina. According to the Government, compelling production of documents [\*19] as requested within Defendants' motion would "compromise the integrity and secrecy of the grand jury investigation." (Gvmt.'s Amicus Brief, at 1.)

<sup>13</sup> In an attempt to distinguish PCY from any other end-use, Defendants suggest that, for purposes of textile applications, polyester cotton yarn is an "alternative" for polyester staple. Apparently, some of the larger textile manufacturers are capable of

Defendants first contend that the information is relevant to rebut any inference that communication amongst competitors necessarily means that the parties are engaging in an illegal conspiracy. [\*20] Defendants do not need to obtain documents exchanged between Parkdale and Avondale in order to establish this point as the law unequivocally requires more than "mere contacts and communications." [Cooper v. Forsyth County Hosp. Auth., Inc.](#), [789 F.2d 278, 281 \(4th Cir.1986\)](#).

Next, to the extent Defendants characterize this request for production as necessary to their "defense" to Plaintiffs' Sherman Act claims, the Court rejects Defendants' argument. In a *per se* price fixing case under the Sherman Antitrust Act, [15 U.S.C. § 1](#), once liability is proven, there is no affirmative defense. [Hanover Shoe v. United Shoe Machinery Corp.](#), [392 U.S. 481, 489, 88 S. Ct. 2224, 20 L. Ed. 2d 1231 \(1968\)](#) (direct injury or impact may be presumed in antitrust cases involving a conspiracy to fix prices or allocate customers); [Illinois Brick Co. v. Illinois](#), [431 U.S. 720, 724-25, 97 S. Ct. 2061, 52 L. Ed. 2d 707 \(1977\)](#).

Defendants further contend that the information sought is relevant to impact and damages issues. To the extent Defendants' argument relates to direct purchasers, the Court need not address this aspect of Defendants' motion because the Court's February 5, 2004 ruling adequately dealt with this contention. Notably, Defendant KoSa's affiant qualifies one of his [\*21] conclusions regarding the consequences of the poly-cotton yarn conspiracy on Direct Purchasers by first stating, "If the law permits it, the calculation of damages for these direct customers would have to account not only for overcharges on polyester staple but also for the potential benefits these same customers derived from the coordinated price increases in polyester-cotton yarn." (Rapp Affidavit, at 6.) The law does not permit a defendant to assert a "pass-on" defense as Rapp suggests. [Hanover Shoe](#), [392 U.S. at 489, 494](#) (as a general rule, a direct purchaser is injured within the meaning of Section 4 of the Clayton Act by the full amount of the overcharge paid by it notwithstanding any passing-on of the illegal overcharge to its own customers or indirect purchasers); [Illinois Brick Co.](#), [431 U.S. at 745-46](#) (direct purchasers are injured and able to recover the full extent of the overcharge paid by them). The information sought has no relevance to the Direct Purchaser claims.

Defendants likewise contend that the documents they seek relate directly to the indirect purchaser claims brought by a number of Non-Class Plaintiffs. Indeed, this Court previously found that PSF end-uses (PSF [\*22] products sold "downstream") only become relevant if indirect purchasers are allowed to seek monetary damages under state law. For purposes of resolving the instant motion, the Court presumes this to be the case.<sup>14</sup>

Having defined the potential relevance of the information sought as limited to Indirect Purchasers' damages claims, the Court now considers whether the burden or expense of the proposed discovery outweighs its likely benefit.

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purchasing polyester staple and spinning their own yarn while some textile manufacturers out-source all of their yarn-spinning. (Defendant's Brief, at 3, 6.) Defendants contend that Springs and others were able to avoid the alleged PSF price increases by shifting their purchases to PCY. (Suppl. Mem. at 2.) Even so, the ability to "shift" or reduce PSF purchases to another product would merely reduce the amount of damages that particular PSF purchaser was entitled to recover as the result of any alleged overcharge for actual purchases. (2/15/04 Order, at 5.) The Court does not find this argument persuasive.

<sup>14</sup> Defendants apparently concede that indirect purchasers are entitled to monetary damages under the laws of certain states. Whether indirect purchasers are entitled to monetary damages for antitrust violations in North Carolina, and the extent of damages that may be recoverable by indirect purchasers, are issues that have not been fully briefed by the parties. The current state of North Carolina law is unclear. Compare [Hyde v. Abbott Laboratories, Inc.](#), [123 N.C.App. 572, 473 S.E.2d 680 \(1996\)](#); [N.C. Gen. Stat. § 75-16](#); [Adams v. Aventis, S.A.](#), [2003 NCBC 7, 2003 WL 22015384 \(N.C. Super. 2003\)](#); and [Crouch v. Crompton Corp.](#), [2004 NCBC 7, 2004 WL 2414027, \\*12 \(N.C. Super. 2004\)](#) ("There is no definitive decision from the North Carolina Supreme Court ruling upon the issue of indirect purchaser standing in North Carolina, nor is there a clear legislative history.")

In some of the states that are deemed Illinois Brick "repeater" states, indirect purchasers are allowed to recover the full extent [\*23] of the illegal overcharge just as a direct purchaser would. *Report of the Indirect Purchaser Task Force: Section of Antitrust Law* American Bar Association, 63 ANTITRUST L.J. 993 (Spring 1995). If that were the case in each of the states relevant here, the Court's analysis would be the same for both indirect and direct purchasers. In Hyde, however, the North Carolina Court of Appeals contemplated that indirect purchaser plaintiffs would be tasked with paring out the amount of illegal overcharge that was passed on to indirect purchasers. [Hyde, 123 N.C.App. at 584](#); [Crouch, 2004 NCBC 7, 2004 WL 2414027](#).

Defendants' current request is more discrete in that Defendants seek information from only two of the Plaintiffs - Parkdale and Avondale. However, Defendants' request is also overly broad to the extent that it encompasses information regarding products that do not contain any PSF. As propounded, Defendants' request may strain Parkdale's and Avondale's resources. Defendants seek [\*24] data regarding "any other product manufactured by you an input of which includes polyester staple." Discovery related to the passing on of any added costs from the alleged PCY conspiracy could very well be expensive and inefficient.

The Court does not have sufficient information at this time to evaluate whether the amount in controversy regarding the indirect purchaser claims at issue weighs in favor or against Defendants' request. The fact that the indirect purchaser claims are remote - twice removed from the alleged PSF conspiracy that is the subject of this litigation - leads the undersigned to believe the damages at issue may ultimately be relatively inconsequential.

In terms of the importance of the issues at stake, and the importance of the proposed discovery in resolving these issues, the Court recognizes that Defendants are entitled to challenge or rebut the amount of damages sought by indirect purchasers. As a practical matter, this presents an almost insurmountable obstacle in terms of determining what percentage of illegal pass-on is attributable to the respective alleged conspiracies. [Crouch, 2004 NCBC 7, 2004 WL 2414027, \\*18](#) ("The cost of obtaining information relevant to pass through [\*25] of added costs from antitrust violations and investigating the pricing decisions made in the distribution chain is high.") For these reasons, the likely benefit of the proposed discovery is negligible at best.

Finally, it is problematic that Defendants seek to investigate issues that are not squarely before this Court but rather are the subject of proceedings before the Middle District of North Carolina. The Court is hesitant to authorize even circumscribed discovery beyond the PSF market. The Indirect Purchaser Plaintiffs have already produced some downstream discovery. (2/15/04 Order, at 6.) Defendants also assert that Avondale has agreed to supplement its production with respect to product substitutability. Nonetheless, Wellman argues that PCY sellers such as Parkdale and Avondale possess relevant information regarding the cause of any illegal pass-on, namely, involvement in an alleged poly-cotton yarn price-fixing conspiracy, that could not have been produced by PCY purchasers. This point is well taken. Nonetheless, the undersigned does not intend to conduct a "mini-trial" on the issues presented in the pending PCY litigation. For the reasons stated herein,

**IT [\*26] IS HEREBY ORDERED THAT** Defendants' Motion To Compel is hereby **GRANTED in part and DENIED in part:**

- 1) Defendants' Motion To Compel is **GRANTED** to the extent Defendants seek documents relating to the pricing, distribution, purchase, or sale of poly-cotton yarn. In other words, Defendants will be allowed to discover information related to Avondale's and Parkdale's sales of PCY to existing Indirect Purchaser Plaintiffs in 3:03CV1516;
- 2) Defendants' Motion To Compel is hereby **DENIED** in all other respects, including Defendants request for Plaintiffs Parkdale and Avondale to produce documents related to open-end or air-jet cotton yarn, documents relating to communications between Parkdale and Avondale and "any other product manufactured by you an input of which includes polyester staple, including, but not limited to, all documents made available by you to any of these agencies, all documents you produced in response to any subpoena, information request or otherwise, and all documents relating to any communication between you and any of these agencies"; and
- 3) Plaintiffs' Motion To Strike is **DENIED**.

**Signed: May 6, 2005**

/s/ Richard L. Voorhees

Richard L. Voorhees

United States District Judge

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## JES Props., Inc. v. USA Equestrian, Inc.

United States District Court for the Middle District of Florida, Tampa Division

May 9, 2005, Decided ; May 9, 2005, Filed

Case No. 8:02-cv-1585-T-24MAP

### **Reporter**

2005 U.S. Dist. LEXIS 43122 \*; 2005 WL 1126665

JES PROPERTIES, INC. d/b/a CYPRESS TRAILS FARM, a Florida Corporation, and MICHAEL W. GALLAGHER, Plaintiffs, -vs- USA EQUESTRIAN, INC. (formerly the American Horse Show Association), et al., Defendants.

**Subsequent History:** Costs and fees proceeding at, Motions ruled upon by [JES Props., Inc. v. USA Equestrian, Inc., 432 F. Supp. 2d 1283, 2006 U.S. Dist. LEXIS 32581 \(M.D. Fla., 2006\)](#)

Affirmed by [JES Props. v. USA Equestrian, Inc., 458 F.3d 1224, 2006 U.S. App. LEXIS 19429 \(11th Cir. Fla., Aug. 2, 2006\)](#)

**Prior History:** [JES Props., Inc. v. USA Equestrian, Inc., 2003 U.S. Dist. LEXIS 20633 \(M.D. Fla., Oct. 10, 2003\)](#)

## **Core Terms**

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Mileage, Promoter, relevant market, sport, competitions, horse show, equestrian, antitrust, monopolization, Defendants', amateur sports, Sherman Act, anti trust law, monopoly, anticompetitive, waivers, jumper, amended complaint, requests, hunter, Federation, conspiracy, horses, practices, athletes, summary judgment motion, amateur, rule of reason, summary judgment, governing body

**Counsel:** [\*1] For JES Properties, Inc., a Florida corporation doing business as Cypress Trails Farm, Michael W. Gallagher, Plaintiff Anna-Katrina S. Christakis, Jason B. Hirsh, John L. Ropiequet, Michael R. Tuoff, Robert D. Butters, Arnstein & Lehr LLP, Chicago, IL; Robin S. Trupp, Arnstein & Lehr LLP, Tampa, FL.

For Dave Burton, also known as Dave Burton, Sr., also known as Dave E. Burton, also known as Dave E. Burton, Sr., Burton & Sons, Inc., Littlewood Fences, Inc., David Burton, also known as David Burton, Jr., also known as David E. Burton, also known as David E. Burton, Jr., Defendants: Charlotte D. Gage, Stanley Howard Eleff, Trenam Kemker, Tampa, FL US.

For Bob Bell, Classic Co., Ltd., Defendants: William Charles Hughes, Law Office of Brent G. Siegel, P.A., Gainesville, FL.

For Kernan Hodges, also known as George H. Hodges, Jr., Defendant:David Thomas Knight, Hill, Ward & Henderson, P.A., Tampa, FL.

For United States Equestrian Federation, Inc., Defendant: Christopher Lee Griffin, James Maxwell Landis, Jon P. Tasso, Foley & Lardner, Tampa, FL.

For Rose View Stables, Ltd., Thomas E. Struzzieri, Horse Shown in the Sun, Inc., Linda S. Aldrich, Fox Lea Farm, Inc. [\*2] , Defendants: Julie S. Sneed, Richard George Salazar, Fowler, White, Boggs & Banker, P.A., Tampa, FL US.

Michael Nachwalter, Mediator, Pro se, Kenny, Nachwalter, Seymour, Arnold, Critchlow & Spector, P.A., Miami, FL.

For Keith D Bartz, Movant: Jon P. Tasso, Foley & Lardner, Tampa, FL.

For North Florida Hunter & Jumper Assoc., Inc., Defendant: Donald A. Mihokovich, Ruden, McClosky, Smith, Schuster & Russell, P.A., Tampa, FL.

For USA Equestrian Trust, formerly known as USA Equestrian, Inc., formerly known as American Horse Show Assoc., Defendant: Chris S. Coutroulis, Samuel J. Salario, Jr., Carlton Fields, P.A., Tampa, FL; George Hunter Gibbons, Michael P. Murphy, Richard Roger Garland, Dickinson and Gibbons, P.A., Sarasota, FL.

For Eugene R. Mische, Defendant: Edward J. Comey, Thomas M. Wood, Shumaker, Loop & Kendrick, LLP, Tampa, FL; Thomas T. Steele, Law Offices of Thomas T. Steele, P.A., Tampa, FL US; William J. Berman, Berman, Rosenbach, P.C., Morristown, NJ.

For Stadium Jumping Inc., Defendant: Edward J. Comey, Thomas M. Wood, Shumaker, Loop & Kendrick, LLP, Tampa, FL; Thomas T. Steel, Law Offices of Thomas T. Steele, P.A., Tampa, FL US; William J. [\*3] Berman, Berman, Rosenbach, P.C., Morristown, NJ; Richard George Salazar, Fowler, White, Boggs & Bunker, P.A., Tampa, FL US.

**Judges:** SUSAN C. BUCKLEW, United States District Judge.

**Opinion by:** SUSAN C. BUCKLEW

## **Opinion**

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### **ORDER**

This cause comes before the Court for consideration of the following motions: Defendant United States Equestrian Federation, Inc.'s ("USEF") Motion for Summary Judgment and Request for Oral Argument (Doc. No. 287); Defendants', David E. Burton, Sr., David E. Burton, Jr., Burton and Sons, Inc. and Littlewood Fences, Inc. (collectively, "the Burton Defendants"), Motion for Summary Judgment (Doc. No. 290); Defendants', Thomas Struzzieri ("Struzzieri"), Horse Shows in the Sun, Inc. ("HITS") and Rose View Stables, Ltd. ("Rose View Stables") (collectively "the HITS Defendants"), Motion for Summary Judgment (Doc. No. 292) and Defendants, Stadium Jumping, Inc. ("Stadium Jumping") and Eugene R. Mische ("Mische") (collectively, "the Stadium Jumping Defendants"), Motion for Entry of Final Summary Judgment (Doc. No. 294).<sup>1</sup> The Court shall refer to the Burton Defendants, the HITS Defendants and the Stadium Jumping Defendants collectively as the "Promoter Defendants." With leave [\*4] of the Court, Plaintiffs filed a Combined Response to Defendants' Summary Judgment Motions (Doc. No. 317) (hereinafter "Response to Motions for Summary Judgment"). With leave of the Court, USEF filed a Reply Brief on the Limited Issue of Antitrust Immunity (Doc. No. 343) and Plaintiffs filed a Sur-Reply to USEF's Reply on the Limited Issue of Antitrust Immunity (Doc. No. 344).

### **I. Procedural History**

On August 29, 2002, Plaintiffs filed a three-count Complaint which raised claims of unreasonable [\*5] restraint of trade under [section 1 of the Sherman Act](#) (Count I), monopolization and attempted monopolization under [section 2 of the Sherman Act](#) (Count II), and claims of conduct, practices and activities which have the likelihood of substantially lessening competition under [section 7](#) of the Clayton Act (Count III). Upon Defendants' motions this Court dismissed the Complaint, but granted Plaintiffs leave to amend (Doc. No. 39).

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<sup>1</sup> The Court notes that the only other remaining Defendants, Linda S. Aldrich and Fox Lea Farm, Inc. did not file dispositive motions. Several Defendants, USA Equestrian Trust, Inc., f/k/a USA Equestrian, Inc. ("USAEE") (formerly The American Horse Shows Association, Inc. ("AHSAA")), Bob Bell, Classic Company Ltd., Kernan Hodges a/k/a Mrs. George H. Hodges, Jr. and North Florida Hunter & Jumper Association, Inc. apparently settled with the Plaintiffs and have been dismissed from the case (Doc. Nos. 195, 261, 267 and 350).

On April 18, 2003, Plaintiffs filed a nine-count Amended Complaint (Doc. No. 42) in which they alleged claims for violation of Section 1 of the Sherman Act, violation of Section 2 of the Sherman Act, violation of Florida's Antitrust Act and violation of the Florida Deceptive and Unfair Trade Practices Act. In the Amended Complaint, Plaintiffs also added an additional Defendant, North Florida Hunter & Jumper Association, Inc. ("NFHJA"). On October 10, 2003, this Court denied Defendants' Motions to Dismiss the First Amended Complaint (Doc. No. 59).<sup>2</sup>

[\*6] On December 19, 2003, Plaintiffs sought leave to file a fourteen count Second Amended Complaint to add Eugene R. Mische, Stadium Jumping, Inc., Thomas E. Struzzieri, Horse Shows in the Sun, Inc., Linda S. Aldridge, Fox Lea Farm, Inc., and United States Equestrian Federation, Inc. ("USEF") as additional defendants (Doc. No. 77). As Defendants did not oppose this second amendment, the Court granted Plaintiffs leave to file a Second Amended Complaint (Doc. No. 81). In the Second Amended Complaint, Plaintiffs again alleged claims for violation of Section 1 of the Sherman Act, violation of Section 2 of the Sherman Act, violation of Florida's Antitrust Act and violation of the Florida Deceptive and Unfair Trade Practices Act.

Almost a year later, on December 16, 2004, Plaintiffs sought leave to file a Third Amended Complaint to add Roseview Stables Ltd. as an additional defendant (Doc. No. 250). Again Defendants did not oppose this third amendment, and the Court granted Plaintiffs leave to file a Third Amended Complaint (Doc. No. 257). In the Third Amended Complaint, Plaintiffs allege that the rules of USAE and USEF, more specifically, the "Mileage Rule,"<sup>3</sup> and Defendants' alleged refusal [\*7] to waive application of that rule violate section 1 of the Sherman Act (Count I). Counts II - IV raise claims of monopolization, attempted monopolization, and conspiracy to monopolize in violation of section 2 of the Sherman Act. Counts V-VIII raise claims of violations of the Florida Antitrust Act, FLA. STAT. §§ 542.18 and 542.19. Count IX alleges violations of the Florida Deceptive and Unfair Trade Practices Act. USEF, the Burton Defendants, the HITS Defendants and the Stadium Jumping Defendants now move for summary judgment as to all counts of the Third Amended Complaint.

## **II. Factual Background**

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[\*8] This antitrust case arises from an unusual factual situation involving the sanctioning of hunter and jumper horse show competitions in the state of Florida during the winter months. USEF, a New York not-for-profit corporation, is the current<sup>5</sup> national governing body ("NGB") for equestrian sport in the United States under the Ted Stevens Olympics and Amateur Sports Act ("Amateur Sports Act" or "ASA"), 36 U.S.C. §§ 220501 et seq. (Doc. No. 289, Exh. 1, Long Decl., P 3 and Doc. No. 317, Exh. H, O'Connor Dep. p. 23). USEF has over 80,000 members in 27 breeds and disciplines. (Doc. No. 305). USEF is not a promoter, operator, or manager of horse shows. (Doc. No. 289, Exh. 1, Long Decl., P 17). USEF did not exist prior to 2003 and has been the NGB for equestrian sport in the United States since June 2004. (Doc. No. 289, Exh. 1, Long Decl., P 4). USEF is a separate legal entity from USAE with its own ownership and management. (Doc. No. 289, Exh. 1, Long Decl., P 8). Due in part to a delay in the

<sup>2</sup> The Court notes that as to Plaintiff Gallagher, the Court granted without prejudice the Burton Defendants' Motion to Dismiss the First Amended Complaint since Plaintiff Gallagher did not allege compliance with "the Federation procedures and did not plead he sought a waiver of the Mileage Rule from the Burton Defendants" (Doc. No. 59).

<sup>3</sup> The Mileage Rule provides, in part, that in all States other than Maine, New Hampshire, Vermont, Connecticut, Rhode Island, New Jersey, New York and Pennsylvania, horse shows offering "A" rated hunter and jumper events must be held at least 250 miles apart on the same date. The Mileage Rule may be waived by a conflicting horse show promoter.

<sup>4</sup> The Court will not restate the entire factual background of this case. Instead, the Court incorporates by reference the factual background as outlined in the Court's Order granting the Burton Defendants, the Federation, the Bell Defendants and Defendant Hodges' Motions to Dismiss (Doc. No. 39) and the Court's Order denying Defendants' Motion to Dismiss the First Amended Complaint (Doc. No. 59).

<sup>5</sup> Replacing former NGB, USA Equestrian, Inc. ("USAE"), formerly known as the American Horse Show Association ("AHSA"). In its previous Orders, the Court referred to USAE as the Federation for that period prior to December 1, 2003.

Internal Revenue Service's recognizing USEF's not-for-profit status, which is a requirement under the Amateur Sports Act for all NGBs, USEF entered into a Management and [\*9] License Agreement ("Agreement") with USAE. Under this Agreement, USEF carried out USAE's obligations as the NGB from December 2003 through May 2004, including processing applications for the current equestrian competition year (2005) on behalf of USAE. (Doc. No. 289, Exh. 1, Long. Decl., P 5).

USEF, and predecessor NGBs, promulgated a variety of rules, including rules that sanction hunter and jumper horse shows as "Recognized Competitions." <sup>6</sup> (Doc. No. 305, GR208, pp. GR11 - GR12). These rules are embodied in the 2005 USEF Rule Book. (Doc. No. 305). Each Promoter Defendant agrees to abide by the rules as a condition of membership. (Doc. No. 305, GR210, pp. GR12 - GR13). Recognized Competitions enjoy privileges not available to other competitions. (Doc. No. 305, GR209, p. GR12). [\*10] Plaintiffs allege that Recognized Competitions provide unique benefits to competitors and those who put on horse shows which are only available by repeat participation at such USEF-sanctioned shows. Plaintiffs further allege that horse show promoters can benefit economically from holding Recognized Competitions. (Doc. No. 317, Exh. K, Weiland Decl., PP 15 and 16). The Mileage Rule which governs Recognized Competitions for hunter and jumper competitions rated "A" and above <sup>7</sup> ("A-Rated Shows") was implemented in 1975. (Doc. No. 317, Exh. I, Balch Dep. p. 100).

In its current form, the Mileage Rule, for hunter and jumper Recognized Competitions in Group 2 states (which includes Florida), provides a "250-mile radius for competitions with any of the same A rated sections, or unrated Jumper sections and classes with total prize money of \$ 10,000 or more." (Doc. No. 305, GR214(2), [\*11] p. GR16). In the 1980's the Mileage Rule applicable to the New England and Middle Atlantic states was reduced to a 125 miles radius. (Doc. No. 305, GR214(1), pp. GR15 - GR16; Doc. No. 317, Exh. L, Swann Decl., P 8 and Doc. No. 317, Exh. L, Long Dep. p. 99). Lesser mileage distances apply for "B" and "C" rated horse shows. (Doc. No. 305, GR214(2), pp. GR15 - GR16). USEF General Rule 214(7) <sup>8</sup>, which controlled the sanctioning of new A-Rated Shows during the course of the present litigation and is part of the Mileage Rule, stated in relevant part:

New competitions offering "A" rated hunter or jumper divisions or sections will not be recognized on dates conflicting with those of any other Recognized Competitions within the applicable distance specified by this rule which offers A rated hunter or jumper divisions or sections, regardless of class scheduling . . . The mileage restrictions . . . will not prevent two Hunter/Jumper competitions from being approved if the two competitions have different competition managements and the competition with priority gives written permission, to be renewed annually, and the mileage distance between the competitions is at least 10 miles.

[\*12] (Doc. No. 305, GR214(7), pp. GR16 - GR17).

USEF initially adopted the rules of the Federation as its own. (Doc. No. 289, Exh. 1, Long Decl., P 9). In January 2004, the USEF Board created a task force to study the Mileage Rule and related rules, and recommend appropriate changes, if any. (Doc. No. 289, Exh. 1, Long Decl., P 10). In January 2005, USEF's Board passed several rule changes (the "January 2005 rule changes") <sup>9</sup>, including but not limited to: 1) giving USEF ultimate control over the granting or denying of waivers under the Mileage Rule, and 2) enacting a "license agreement" regime under which USEF has the right to refuse to renew applications of now-established competitions if such competitions fail to satisfy certain objective standards. (Doc. No. 289, Exh. 1, Long Decl., P 11 and Doc. No. 344, Exh. A.). By way of example, although the Mileage Rule previously provided that a promoter of a horse show could, in its sole discretion, waive an objection to the holding of another similarly [\*13] rated horse show within the applicable mileage restriction, new General Rule 213 provides, in relevant part: "The Federation shall reserve the right to have final approval on the granting or denying of waivers and will not delegate this responsibility to any other entities or parties." (Doc. No. 289, Exh. 1, Long Decl., Exh. C thereto and Doc. No. 344, Exh. A thereto). No

<sup>6</sup> The Court notes that in their Third Amended Complaint the Plaintiffs utilize the term "Recognized Horse Shows."

<sup>7</sup> "A" or "AA."

<sup>8</sup> Now amended.

<sup>9</sup> Effective May 1, 2005.

mileage restrictions apply to a horse show promoter who wishes to hold a horse show that is "unrated," i.e., not sanctioned by the USEF. (Doc. No. 286, Struzzieri Decl., P 4).

In their Third Amended Complaint, Plaintiffs define the relevant product market as "[h]unter and jumper equestrian competitions recognized by the Federation as hunter and jumper competitions 'A' rated and above." Third Am. Compl. P 151. They also define the relevant geographic market as the state of Florida between December 1 and March 31 of each year (the "Winter Months"). Third Am. Compl. PP 154 - 158. Therefore, the Relevant Market is defined [\*14] as A-Rated Shows in the state of Florida during the Winter Months. Third Am. Compl. P 159.<sup>10</sup>

Plaintiffs are horse show promoters. Dr. Douglas Weiland ("Weiland"), the principal of Plaintiff JES Properties, Inc. ("JES"), began holding unrecognized horse shows at his Cypress Trails Farm facility in Odessa, Florida in 1998. (Doc. No. 317, Exh. K, Weiland Decl. PP 3 and 4). Weiland registered JES with USAE in 2000 and began to conduct Recognized Competitions during the summer months since no other promoters had conflicting dates in those months. (Doc. No. 317, Exh. K, Weiland Decl., P 4). Weiland held six A-Rated Shows at Cypress Trails Farm in the summers of 2001 and [\*15] 2002,<sup>11</sup> and held 25 unrated shows between 1998 and 2003. (Doc. No. 317, Exh. K, Weiland Decl., P 11). Weiland intended to run A-Rated Shows in the Relevant Market if it was possible to do so. (Doc. No. 317, Exh. K, Weiland Decl., P 14). However JES was unable to obtain dates for A-Rated Shows in the Relevant Market due to the application of the Mileage Rule by the NGB and JES' inability to obtain waivers from the Promoter Defendants who controlled the dates. (Doc. No. 317, Exh. K, Weiland Decl., PP 21 - 23). JES was actually unable to hold horse shows at the Cypress Trails Farm after 2003 due to zoning regulations. (Doc. No. 317, Exh. K, Weiland Decl., P 24). However, Weiland alleges he would have conducted shows at other properties had he been able to obtain entry into the Relevant Market (Doc. No. 317, Exh. K, Weiland Decl., P 25).

Plaintiff Gallagher ("Gallagher") conducted both A-Rated [\*16] and unrated shows in the Tallahassee area. (Doc. No. 317, Exh. O, Gallagher Decl. PP 8 - 10). Gallagher alleges he has experience developing an equestrian facility in the Tallahassee area and has been approached about developing additional facilities and "residential communities surrounding them." (Doc. No. 317, Exh. O, Gallagher Decl. P 11). Gallagher also has attempted to promote A-Rated Shows in the Relevant Market, but has been unable to obtain dates for A-Rated Shows in the Relevant Market due to the application of the Mileage Rule by the NGB and Gallagher's inability to obtain waivers from the Promoter Defendants who controlled the dates. (Doc. No. 317, Exh. O, Gallagher Decl., PP 12 and 13). Gallagher alleges that he has the financial backing needed to promote and manage A-Rated Shows. (Doc. No. 317, Exh. O, Gallagher Decl., P 14).

The Burton Defendants conduct A-Rated Shows. (Doc. No. 291, Exh. A., Burton, Sr. Dep. Vol. I p.141; Exb. B., Burton, Jr. Dep. p. 113). None of the Burton Defendants were involved in the adoption of the Mileage Rule or related rules. (Doc. No. 291, Exh. A, Burton, Sr. Dep. Vol. II pp. 12 -13; Exh. B., Burton, Jr. Dep. p. 130). Cypress Trails Farm [\*17]<sup>12</sup> unsuccessfully sought waivers of the Mileage Rule from each of the Burton Defendants. (Doc. No. 291). Gallagher unsuccessfully sought waivers of the Mileage Rule from each of the Burton Defendants. (Doc. No. 291). The decisions by each of the Burton Defendants not to grant waivers of the Mileage Rule were unilateral decisions. (Doc. No. 291, Exh. A, Burton, Sr. Dep. Vol. II pp. 52-68 and 77-79; Exh. B, Burton, Jr. Dep. pp.186 - 197).

Defendant Thomas E. Struzzieri ("Struzzieri") is the sole owner of Horse Shows in the Sun, Inc. ("HITS") and Rose View Stables, Ltd. ("Rose View Stables")(collectively "the HITS Defendants"). (Doc. No. 286, Struzzieri Decl., P 2). From 1998 through late 2002, Struzzieri was a member of the board of directors of USAE. He was one of approximately 64 board members. (Doc. No. 286, Struzzieri Decl., P 11). In January 2005, Struzzieri became a

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<sup>10</sup> For the limited purpose of ruling on Defendants' summary judgment motions this Court will accept that Plaintiffs' definition of the Relevant Market is correct. However, the Court notes that the Burton Defendants and HITS Defendants argue that the relevant product market should not be "A" rated hunter and jumper shows (Doc. Nos. 291 and 292).

<sup>11</sup> The Court notes that it is unclear from the record whether Weiland held six A-Rated Shows each summer or in total.

<sup>12</sup> JES d/b/a Cypress Trails Farm.

board member of USEF. (Doc. No. 289, Long Decl., P 13). From 1990 to the present, Struzzieri has been a [\*18] member of the Competition Management Committee for USAE and USEF. (Doc. No. 286, Struzzieri Decl., PP 12 and 14).

Since 1981 the HITS Defendants have been holding and promoting horse shows throughout the United States, including shows in California, Arizona, Florida, New York, Virginia and Massachusetts. (Doc. No. 286, Struzzieri Decl., P 2). For each of the last three (3) years, the HITS Defendants have held seven (7) hunter/jumper shows in the state of Florida at a facility in Ocala, Florida. Of these seven (7) shows, five (5) were A-Rated Shows held on consecutive weeks in February and March. The other two (2) horse shows were "unrated" hunter/jumper shows held in January. (Doc. No. 286, Struzzieri Decl., P 5). Except for the five (5) week period during the months of February and March, the HITS Defendants do not hold any USEF sanctioned horse shows in the state of Florida.

In 2003, the HITS Defendants received a Mileage Rule waiver request from Weiland, on behalf of JES.<sup>13</sup> This was the first request for a waiver that the HITS Defendants had ever received from JES. (Doc. No. 286, Struzzieri Decl., P 7). JES failed to provide the HITS Defendants with specific details regarding [\*19] the location of the contemplated show, and the waivers were not only for 2004 but for all years thereafter; therefore, the HITS Defendants did not provide JES with the waiver of the Mileage Rule. (Doc. No. 286, Struzzieri Decl., P 7). The HITS Defendants received a similar request from Gallagher and similarly did not provide Gallagher with the waiver. (Doc. No. 286, Struzzieri Decl., P 8). In 2004, the HITS Defendants again received waiver requests from Plaintiffs for show dates in February and March of 2005. The HITS Defendants again decided not to grant such requests based upon the fact that the Plaintiffs had filed this lawsuit against the HITS Defendants (Doc. No. 286, Struzzieri Decl., P 17).

Defendant Stadium Jumping first received a Mileage Rule waiver request from JES in May 2003. [\*20]<sup>14</sup> (Doc. No. 293, Mische Decl., P 2). On May 12, 2003, Defendant Stadium Jumping responded to JES by denying JES' waiver request. (Doc. No. 293, Mische Decl., P 3). Defendant Stadium Jumping elected not to respond to subsequent waiver requests received from JES. (Doc. No. 293, Mische Decl., PP 6, 9 and 12). Defendant Stadium Jumping received similar requests from Gallagher and similarly did not provide Gallagher with waivers or respond to his requests. (Doc. No. 293, Mische Decl., PP 8, 9 and 12). Defendant Stadium Jumping's decisions not to grant waivers of the Mileage Rule, or respond to Plaintiffs' requests, were unilateral decisions. (Doc. No. 293, Mische Decl., PP 4, 6, 9, and 12).

Defendant Eugene R. Mische ("Mische") personally, or in [\*21] the name of Defendant Stadium Jumping, has been a member of USEF and its predecessor organizations for more than thirty (30) years. Mische states that other than a *de minimis* role based on his being a member of USEF, he had no actual role in the institution or development of the Mileage Rule. (Doc. No. 293, Mische Decl., P 13). Mische further claims that in the past, Defendant Stadium Jumping has granted Mileage Rule waivers to promoters, including Defendant Horse Shows in the Sun and Defendant Burtons & Sons, Inc. These waivers "were granted by Stadium Jumping without being conditioned on giving, or not giving, any future 'waivers' or permissions to those promoters or any other promoters who might make such requests in the future." (Doc. No. 293, Mische Decl., P 14).

The Promoter Defendants do not control or dictate USEF policies and rules. (Doc. No. 289, Exh.1, Long Decl., P 15 and Doc. No. 293, Mische Decl., P 15). Rather, the power to make and change USEF rules is placed by USEF's bylaws with USEF's fifty-four member Board of Directors. (Doc. No. 305, pp. ix - x). Of the fifty-four Board of Directors members, only ten (two of whom are athlete seats mandated by the Amateur [\*22] Sports Act), represent the hunter and/or jumper communities. (Doc. No. 305, pp. x - xi and Doc. No. 289, Long Decl., P 13). Only Defendant Struzzieri is currently a board member of USEF. (Doc. No. 289, Long. Decl., P 13). Furthermore, USEF

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<sup>13</sup> The dates that were subject to JES' request were February 4-8, 2004, February 11 - 15, 2004, February 18 - 22, 2004, February 25 - 29, 2004, March 3-7, 2004 and March 10 - 14, 2004. (Doc. No. 286, Struzzieri Decl., P 7).

<sup>14</sup> The dates that were subject to JES' request were February 5-9, 2003, February 12 - 16, 2003, February 19 - 23, 2004, February 26 - March 3, 2003, March 5-9, 2003, March 13 - 16, 2003, March 19 - 23, 2003 and March 25 - 29, 2004 (Doc. No. 293, Mische Decl., Exh. A).

committees, such as the Competition Management committee, have no power to make or change USEF rules but can only make recommendations for rule changes to the Board of Directors. (Doc. No. 305, p. xxix; Doc. No. 289, Long Decl., P 14 and Doc. No. 286, Struzzieri Decl., P 14).

### **III. Standard of Review**

Summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that the moving party is entitled to judgment as a matter of law." [Fed. R. Civ. P. 56\(c\)](#). The moving party bears the initial burden of showing the Court, by reference to materials on file, that there are no genuine issues of material fact that should be decided at trial. See [Celotex Corp. v. Catrett, 477 U.S. 317, 106 S. Ct. 2548, 91 L. Ed. 2d 265 \(1986\)](#). A moving party discharges its burden on a motion for summary judgment by "showing" or "pointing out" to the Court that there is an [\*23] absence of evidence to support the non-moving party's case. [Id. at 325](#). [Rule 56](#) permits the moving party to discharge its burden with or without supporting affidavits and to move for summary judgment on the case as a whole or on any claim. See [id.](#) When a moving party has discharged its burden, the non-moving party must then "go beyond the pleadings," and by its own affidavits, or by "depositions, answers to interrogatories, and admissions on file," designate specific facts showing there is a genuine issue for trial. [Id. at 324](#).

In determining whether the moving party has met its burden of establishing that there is no genuine issue as to any material fact and that it is entitled to judgment as a matter of law, the Court must draw inferences from the evidence in the light most favorable to the non-movant and resolve all reasonable doubts in that party's favor. See [Samples on behalf of Samples v. City of Atlanta, 846 F.2d 1328, 1330 \(11th Cir. 1988\)](#). The Eleventh Circuit has explained the reasonableness standard:

In deciding whether an inference is reasonable, the Court must "cull the universe of possible inferences from [\*24] the facts established by weighing each against the abstract standard of reasonableness." [citation omitted]. The opposing party's inferences need not be more probable than those inferences in favor of the movant to create a factual dispute, so long as they reasonably may be drawn from the facts. When more than one inference reasonably can be drawn, it is for the trier of fact to determine the proper one.

[WSB-TV v. Lee, 842 F.2d 1266, 1270 \(11th Cir. 1988\)](#).

Thus, if a reasonable fact finder evaluating the evidence could draw more than one inference from the facts, and if that inference introduces a genuine issue of material fact, then the court should not grant the summary judgment motion. See [Augusta Iron & Steel Works v. Employers Ins. of Wausau, 835 F.2d 855, 856 \(11th Cir. 1988\)](#). A dispute about a material fact is "genuine" if the "evidence is such that a reasonable jury could return a verdict for the non-moving party." [Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 \(1986\)](#). The inquiry is "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so [\*25] one-sided that one party must prevail as a matter of law." [Id. at 251-52](#).

### **IV. Discussion**

The question before this Court is whether there are grounds for relief under the antitrust laws based upon the alleged anticompetitive impact of the Promoter Defendants' adherence to the rules promulgated by the national governing body of equestrian sport in the United States. Plaintiffs have asserted claims against the Promoter Defendants and USEF based upon Plaintiffs' inability to obtain permission to hold or promote A-Rated Shows in Florida between December 1 and March 31. The crux of Plaintiffs' claims is that the Promoter Defendants illegally use USEF's rules to insulate themselves from economic competition in the horse show industry. Specifically, as a result of the Promoter Defendants' adherence to USEF's rules, Plaintiffs argue that "at least one incumbent promoter of an A-Rated Show exists for every winter weekend in Florida, preventing any other promoters from entering the market and engaging in head-to-head competition within the 250-mile radius" (Doc. No. 317). By way

of example, Plaintiffs contend that "the 250 mile radius prevents A-Rated Shows from [\*26] being held in the Tampa, Orlando or Jacksonville metro areas if a similar show is being held in the Palm Beach County area, unless the incumbent promoter grants a waiver" (Doc. No. 317). Plaintiffs refer to the Promoter Defendants' alleged illegal conduct as granting them "perfect and permanent serial monopolies for their protected dates" (Doc. No. 317).

### **1. Ted Stevens Olympics and Amateur Sports Act, 36 U.S.C. §§ 220501 et seq.**

USEF argues that it is exempt from antitrust liability for the subject Mileage Rule under the Ted Stevens Olympics and Amateur Sports Act, 36 U.S.C. §§ 220501 et seq. (the "Amateur Sports Act" or "ASA"). The Promoter Defendants all contend that since USEF enjoys antitrust implied immunity in connection with the establishment and enforcement of the Mileage Rule, they should likewise be immune from antitrust liability for exercising their right not to waive the application of the rule. Plaintiffs respond that there is no support in the case law for such an expansive view of implied antitrust immunity. Plaintiffs further contend that while USEF may be the NGB for equestrian sport, the Mileage Rule [\*27] is not necessary for any of the core functions of the NGB and serves no legitimate purpose.

The Amateur Sports Act was enacted "to correct the disorganization and serious factional disputes that seemed to plague amateur sports in the United States." San Francisco Arts & Athletics, Inc. v. United States Olympic Comm'n, 483 U.S. 522, 544, 107 S. Ct. 2971, 97 L. Ed. 2d 427 (1987)(citations omitted). Under the Amateur Sports Act, the United States Olympic Commission ("USOC") is authorized to recognize one NGB for each sport included in the program of the Olympic Games. As the recognized NGB for equestrian sport in the United States, USEF is mandated to regulate the sport. The Amateur Sports Act provides in relevant part:

- (a) Authority.--For the sport that it governs, a national governing body may --
  - (1) represent the United States in the appropriate international sport federation;
  - (2) establish national goals and encourage the attainment of those goals;
  - (3) serve as the coordinating body for amateur athletic activity in the United States; . . .
  - (6) recommend to the corporation <sup>15</sup> individuals and teams to represent the United States in the Olympic Games [\*28] . . .

### 36 U.S.C. § 220523.

For the sport that it governs, a national governing body shall --

- (1) develop interest and participation throughout the United States and be responsible to the persons and amateur sports organizations it represents;
- (2) minimize, through coordination with other amateur sports organizations, conflicts in the scheduling of all practices and competitions . . .

### 36 U.S.C. § 220524.

To the extent that courts have considered antitrust challenges to rules defining professional sports activities, the rulemaking authorities have been given considerable discretion to achieve their sporting objectives, in the absence of any demonstrated market foreclosure. See Brookins v. Int'l Motor Contest Ass'n, 219 F.3d 849, 853 (8th Cir. 2000). While the Amateur Sports Act does not expressly exempt amateur sports activities from the antitrust laws, courts have found implied antitrust [\*29] immunity. See Behagen v. Amateur Basketball Ass'n of the United States, 884 F.2d 524 (1989). USEF argues that because § 220524(2) of the Amateur Sports Act confers on USEF an obligation to minimize scheduling conflicts, USEF is entitled to antitrust immunity with respect to the Mileage Rule. This Court Agrees.

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<sup>15</sup> The USOC.

In Behagen, a former amateur basketball player, Ronald Behagen ("Behagen") lost his amateur eligibility status <sup>16</sup> after playing professional basketball for a second time. The ABA/USA, the NGB for basketball, had enacted a player eligibility rule that provided that an athlete could reclaim amateur status only once after playing professional basketball. When Behagen's amateur status was not reinstated, he brought suit alleging in part that the player eligibility rule constituted an illegal group boycott under section 1 of the Sherman Antitrust Act ("Sherman Act"). See Behagen, 884 F.2d at 527. The Tenth Circuit reversed a jury verdict in favor of Behagen on the Sherman Act claim. In finding the player eligibility rule exempt from the coverage of the federal antitrust laws, the Court stated "[t]he defendants' actions in this case were [\*30] clearly within the scope of activity directed by Congress, and were necessary to implement Congress' intent with regard to the governance of amateur athletics." Id. The Court further stated that "the monolithic control exerted by an NGB over its amateur sport is a direct result of the congressional intent expressed in the Amateur Sports Act." Id. at 528.

As the NGB for equestrian sport in the United States, USEF performs many functions including the promulgation of scheduling and competition rules such as are at issue in the present case. The Amateur Sports Act requires USEF, as the NGB for equestrian sport, to coordinate amateur equestrian activity in the United [\*31] States and to minimize scheduling conflicts. See 36 U.S.C. §§ 220524(2) and 220523(a)(3). Plaintiffs concede that USEF promotes the equestrian sport, including the publication of rules and standards for participation, rider and animal safety and judging at competitive shows. Third Am. Compl. P 35. At the very heart of Plaintiffs' lawsuit is their desire to have A-Rated Shows in the Relevant Market sanctioned by USEF and have the ability to utilize the rules of USEF.

Scheduling is central to the governing of any sport. USEF argues that "the Mileage Rule is a scheduling rule that minimizes conflicts between recognized competitions." (Doc. No. 288). USEF further contends that use of mileage as a calendar coordinating means, especially where horses are concerned, "is a very good and objective way of doing it." (Doc. No. 289, Exh. 5, Balch Dep., pp. 83 - 84). Plaintiffs do not dispute that the Mileage Rule minimizes scheduling conflicts between competitions, rather, Plaintiffs contend that the Mileage Rule has anticompetitive effects. However, USEF's Mileage Rule and its enforcement thereof, is exactly the type of action which the Amateur Sports Act directs, [\*32] that is, "the monolithic control of an amateur sport by the NGB for that sport." Id. at 529.

In Eleven Line Inc v. North Texas State Soccer Ass'n, 213 F.3d 198 (5th Cir. 2000), one of the few cases examining antitrust liability under the Amateur Sports Act, the Court rejected the application of the implied immunity doctrine and distinguished the facts of the case from Behagen. However the Eleven Line court based its rejection in large part upon the fact that the United States Soccer Federation ("USSF"), the national governing body, had not issued the rule in question or explicitly approved of it. The Eleven Line court acknowledged that "[a]lthough the facts of this case do not support an implied exemption from the antitrust laws, an implied exemption would be appropriate in many other situations." Eleven Line, 213 F.3d at 204. In the case before this Court, USEF as the national governing body of equestrian sport, specifically approved of the Mileage Rule and was aware of its consequences, i.e., that it may preclude a promoter from obtaining a Recognized Competition on a desired date.

Plaintiffs urge this Court to [\*33] consider the history of the Mileage Rule, and its waiver provision <sup>17</sup>, to determine if there might be a less exclusionary means to carry out the scheduling purpose of the Amateur Sports Act. This approach ignores the existing federal case law on implied immunity under the Amateur Sports Act which

<sup>16</sup> In order for an American to play basketball in amateur competition outside of the United States, the player is required to qualify as an amateur by receiving a travel permit from the Amateur Basketball Association of the United States ("ABA/USA") and a license from the Federation Internationale de Basketball Amateur ("FIBA")

<sup>17</sup> With respect to Plaintiffs' argument that the Mileage Rule does not minimize scheduling conflicts since it permits a promoter to "waive" a mileage conflict, this Court notes that under the January 2005 rule changes, USEF has ultimate control over all waivers (Doc. No. 289, Exh. 1, Long Decl., Exh. C thereto). Furthermore, to the extent Plaintiffs argue that under the January 2005 rule changes, the only modification is that USEF must give prior approval to "the incumbent promoters' veto power," this bolsters the presumption that the Mileage Rule is necessary. Specifically, incumbent promoters may not "dispense" with the Mileage Rule simply because it suits their purposes.

acknowledges that a national governing body may exert monolithic control, i.e., Behagen and Eleven Line. This Court finds that like the player eligibility rule exempted under Behagen, the Mileage Rule should be exempted and Plaintiffs' antitrust claims against USEF should be barred since USEF's Mileage Rule minimizes scheduling conflicts and implements Congress' intent with regard to the governance of amateur athletics. Likewise, Plaintiffs' claims against the Promoter Defendants are barred based upon their membership in USEF and/or conduct in compliance with, and pursuant to, the rules and regulations of USEF. In summary, Defendants are entitled to summary judgment on all of Plaintiffs' claims under the doctrine of implied immunity.

#### **[\*34] 2. Standing**

The HITS Defendants and Stadium Jumping Defendants contend<sup>18</sup> [\*35] that Plaintiffs lack standing to bring the claims asserted in the Third Amended Complaint because they have not suffered the type of injury to business or property contemplated by the Sherman Act. Plaintiff JES<sup>19</sup> responds that it does have standing since it "attempted to enter the Relevant Market for many years" and that "each attempt was precluded by application of the Mileage Rule." Standing is a question of law for the Court to decide. See Todorov v. DCH Healthcare Authority, 921 F.2d 1438, 1448 (11th Cir. 1991). "Antitrust standing is best understood in a general sense as a search for the proper plaintiff to enforce the antitrust laws." Id. The Eleventh Circuit has identified a two-pronged approach to determine whether a plaintiff has antitrust standing. To be a proper party, a plaintiff must have suffered an antitrust injury and must be an efficient enforcer of the antitrust laws. See id. at 1449; see also Levine v. Central Florida Medical Affiliates, Inc., 864 F. Supp. 1175, 1178 (M.D. Fla. 1994).

##### **a. Antitrust Injury**

Antitrust injury is defined as:

injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful. The injury should reflect anticompetitive effect either of the violation or of anticompetitive effects made possible by the violation. It should be, in short, the type of loss that the claimed violation would be likely to cause.

*Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977)*. That is, an antitrust plaintiff must show that his own injury coincides with the public detriment tending to result from the alleged violation. See Todorov, 921 F.2d at 1450; see also Amey, Inc. v. Gulf Abstract & Title, Inc., 758 F.2d 1486, 1493 (11th Cir. 1985).

In the case before this Court, Gallagher seeks the profits that he claims he would have made promoting A-Rated Shows [\*36] during the period within which he was precluded from conducting such shows by reason of the Mileage Rule and the Promoter Defendants' failure to waive the Mileage Rule. JES likewise seeks the profits it claims that it would have made in promoting A-Rated Shows during the period within which it was precluded from conducting such shows. Additionally, JES and Gallagher seek the profits they claim they would have made on housing developments they would have built had they not been precluded from holding A-Rated Shows in the Relevant Market. Plaintiffs further allege that they are harmed by the Mileage Rule in that they cannot offer greater than \$ 10,000 in prize money at the unrated shows that the Mileage Rule restricts them to in the Relevant Market.

In essence, Plaintiffs complain of injury largely to themselves not injury that inures to the public detriment. This is not antitrust injury. The antitrust laws were enacted for the protection of competition, not the competitors. See *Brunswick, 429 U.S. at 488*. In their Response to the Motions for Summary Judgment, Plaintiffs allege the Mileage Rule has caused harm to competition because it has (1) reduced the number of [\*37] A-Rated Shows in the Relevant Market, (2) increased the costs of participation in the incumbent shows, and (3) blocked potential new

<sup>18</sup> The Burton Defendants join in this argument.

<sup>19</sup> Plaintiffs' Response to Motions for Summary Judgment incorrectly states that Defendants do not challenge Plaintiff Gallagher's standing to sue.

entrants from holding competing shows. (Doc. No. 317, Exh. R, McAnneny Expert Report, filed under seal (S-2)). There are few specific facts in the record to support these allegations, especially the allegation that the Mileage Rule has increased the costs of participation in the incumbent shows. See Evers v. General Motors Corp., 770 F.2d 984, 986 (11th Cir. 1985). Furthermore, the only examples of "potential new entrants" who have been blocked from holding competing shows are the Plaintiffs themselves. Lastly, while arguably the application of the Mileage Rule may have limited the number of A-Rated Shows in the Relevant Market, it is undisputed that there were at least 26 A-Rated Shows in the Relevant Market in 2004. (Doc. No. 317, Exh. R, McAnneny Expert Report, filed under seal (S-2)).

Furthermore, Plaintiffs allege damages equal to the profits they would have garnered had they been able to share in the Promoter Defendants' alleged monopoly profits. This is not antitrust injury. See Todorov, 921 F.2d at 1453. Lastly, [\*38] as to Plaintiffs' contention that they are entitled to profits they claim they would have made on housing developments, these damages are simply too remote and speculative to serve as a basis for any antitrust injury. In summary, since Plaintiffs have not shown they suffered antitrust injury, they have no standing to assert their claims.

### **b. Efficient Enforcement of Antitrust Laws**

To establish that it is an efficient enforcer of the antitrust laws, a plaintiff must meet the target area test. "The target area test requires that an antitrust plaintiff both 'prove that he is within the sector of the economy endangered by a breakdown of competitive conditions in a particular industry' and that he is 'the target against which anticompetitive activity is directed.'" Florida Seed Co. v. Monsanto Co., 105 F.3d 1372, 1374 (11th Cir. 1997)(quoting National Indep. Theatre Exhibitors, Inc. v. Buena Vista Distribution Co., 748 F.2d 602, 608 (11th Cir. 1984)).

Since the Court has found that Plaintiffs suffered no antitrust injury, it need not and will not address whether Plaintiffs would be efficient enforcers of the antitrust laws under the second prong [\*39] of the standing analysis.

### **3. Section 1 of the Sherman Act, 15 U.S.C. § 1 (Count I)**

Section 1 of the Sherman Act provides, in pertinent part, that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal." 15 U.S.C. § 1. Broadly speaking, irrespective of the type of activity challenged, certain elements must be established to prove a violation of section 1: (1) that an agreement exists between two or more entities and (2) that the agreement unreasonably restrains trade. See Torodov, 921 F.2d at 1455; see also Boczar v. Manatee Hospitals & Health Systems, Inc., 731 F. Supp 1042, 1046 (M.D. Fla. 1990); Weight-Rite Golf Corporation, et al. v. United States Golf Association, 766 F. Supp. 1104, 1108 (M.D. Fla. 1991); Tucci v. Smoothie King Franchises, Inc., 215 F. Supp. 2d 1295, 1301 (M.D. Fla. 2002). As discussed below, the Court finds that Plaintiffs have failed to establish either of the elements necessary to prove a violation [\*40] of section 1 of the Sherman Act.

#### **a. Contract, Combination or Conspiracy**

The threshold element of a section 1 claim is "concerted activity." Mere unilateral conduct is not violative of section 1. See Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 768, 104 S. Ct. 2731, 81 L. Ed. 2d 628 (1984); see also Levine v. Central Fla. Medical Affiliates, 72 F.3d 1538, 1545. Section 1 of the Sherman Act does not prohibit independent business decisions but only prohibits concerted action and, thus, requires some agreement, express or implied, between two or more persons. See Moecker v. Honeywell Int'l, Inc., 144 F. Supp. 2d 1291, 1300 (M.D. Fla. 2001)(citing Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 761, 104 S. Ct. 1464, 79 L. Ed. 2d 775 (1984)). It is well settled in the Eleventh Circuit that evidence of parallel business behavior, or even conscious parallelism, does not without more<sup>20</sup>, constitute concerted activity. See City of Tuscaloosa v. Harcros Chemicals, Inc., 158 F.3d 548, 570 (11th Cir. 1998).

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<sup>20</sup> At times referred to as "plus factors."

[\*41] The Promoter Defendants claim that Plaintiffs cannot demonstrate that the Promoter Defendants acted collusively in refusing to grant Plaintiffs' requests for waiver of the Mileage Rule. The Court agrees that there is no record evidence that the Promoter Defendants' refusals to waive the Mileage Rule as to Plaintiffs' proposed A-Rated Shows were anything other than unilateral acts. "The threshold requirement of every conspiracy claim, under both section 1 and section 2, is an agreement to restrain trade. To prove that such an agreement exists between two or more persons, a plaintiff must demonstrate 'a unity of purpose or a common design and understanding, or a meeting of minds in an unlawful arrangement.'" Seagood Trading Com. v. Jerrico, Inc., 924 F.2d 1555, 1573 (11th Cir. 1991)(quoting American Tobacco Co. v. United States, 328 U.S. 781, 810, 66 S. Ct. 1125, 90 L. Ed. 1575 (1946)). This Court recognizes that it will only be the rare case in which a plaintiff can establish the existence of a conspiracy by showing an explicit agreement and that most conspiracies are inferred "from the behavior of the alleged conspirators." See id. However, antitrust law limits [\*42] the range of permissible inferences from circumstantial or ambiguous evidence in a section 1 case. See City of Tuscaloosa, 158 F.3d at 570. To prove a conspiracy, the circumstantial evidence must reasonably tend to exclude the possibility that the alleged conspirators acted independently. See Seagood, 924 F.2d at 1574.

With respect to Plaintiffs' contention that the record is "replete" with evidence of written agreements between the HITS Defendants and Stadium Jumping Defendants in which these Promoter Defendants continually agree to grant each other waivers of the Mileage Rule, this Court cannot infer from these agreements any conspiracy or "meeting of the mind" to exclude Plaintiffs from promoting A-Rated Shows in the Relevant Market. Plaintiffs further contend that the NGB "held up their end of the bargain," and participated in the purported conspiracy, by assisting these Promoter Defendants over the years in the implementation of their agreement and denying any conflicting date applications from other promoters pursuant to the Mileage Rule. (Doc. No. 317). However, Plaintiffs concede that the Stadium Jumping Defendants have from time to time [\*43] granted Mileage Rule waivers to other longstanding horse show promoters in the Relevant Market. (Doc. No. 317, Exh. C). Plaintiffs further concede that "there is no direct evidence of collusion" among the HITS Defendants and Stadium Jumping Defendants in reaching their specific decisions to deny the Plaintiffs' waiver requests. (Doc. No. 317).

Here the evidence Plaintiffs rely upon for the proposition that this Court should infer a conspiracy only demonstrates that the HITS Defendants and the Stadium Jumping Defendants chose to do business with one another. Furthermore, the evidence establishes that over the years the Stadium Jumping Defendants apparently opted to do business with Kernan Hodges and at least one of the Burton Defendants. As to the Promoter Defendants, "[i]t is well established that a party 'may choose with whom he will do business and with whom he will not do business' and that this behavior referred to as 'exclusive dealing,' will not give rise to liability absent a showing of actual competitive injury." See Seagood, 924 F.2d at 1567 (citing Construction Aggregate Transp., Inc. v. Florida Rock Indus., Inc., 710 F.2d 752, 772-73 (1983)). [\*44] Additionally, the conduct of the NGB amounts to little more than enforcing its own rules and minimizing scheduling conflicts as it is required to do.

Here Plaintiffs have presented no credible evidence by which this Court could find a conspiracy. Circumstantial evidence in this case is insufficient to implicate the Promoter Defendants in an agreement to exclude Plaintiffs from promotion of A-Rated Shows in the Relevant Market. This is especially true since each Promoter Defendant, at most, admittedly only has control of a limited number of weekend dates in the alleged Relevant Market and has no control over the remaining dates. Furthermore, in denying the Plaintiffs' waiver requests, the Promoter Defendants complied with the rules of the NGB. Therefore, an agreement between the Defendants has not been established.

### **b. Unreasonable Restraint of Trade**

Even if Plaintiffs were able to demonstrate concerted activity on the part of Defendants, not every agreement that restrains competition will violate the Sherman Act. The Supreme Court has determined that section 1 prohibits only those agreements that *unreasonably* restrain competition. See National Collegiate Athletic Ass'n v. Board of Regents of University of Oklahoma, 468 U.S. 85, 98, 104 S. Ct. 2948, 82 L. Ed. 2d 70 (1984); [\*45] see also Levine, 72 F.3d at 1545 (citing Standard Oil Co. v. United States, 221 U.S. 1, 58, 64, 31 S. Ct. 502, 55 L. Ed. 619 (1911)). To determine whether an agreement unreasonably restrains trade, courts have applied the rule of reason analysis and the *per se* analysis. See Boczar, 731 F. Supp. at 1046. That is, "[a] restraint may be violative of the Sherman Act because it is solely a naked restraint of trade so offensive to competition as to be unreasonable *per*

se, or because it runs afoul of the more detailed rule of reason inquiry." *Retina Associates, P.A. v. Southern Baptist Hospital of Florida et al.*, 105 F.3d 1376, 1381 (11th Cir. 1997)(citing *F.T.C. v. Indiana Fed'n of Dentists*, 476 U.S. 447, 458, 106 S. Ct. 2009, 90 L. Ed. 2d 445 (1986)). Plaintiffs contend that the application of the Mileage Rule by the Promoter Defendants as members of the NGB, in failing to grant waiver requests to the Plaintiffs, requires this Court to undertake a *per se* analysis. This Court disagrees and finds the rule of reason analysis is applicable to Plaintiffs' claims.

#### **i. Is the Mileage Rule *Per Se* Unreasonable?**

Per *se* [\*46] illegality is limited to four categories of trade restraints: (1) horizontal and vertical price fixing; (2) horizontal market divisions; (3) group boycotts or concerted refusals to deal; and (4) tying arrangements. See *Moecker*, 144 F. Supp. 2d at 1301 (citing *Seagood Trading*, 924 F.2d at 1567). Plaintiffs allege that through the use of the Federation's prize level restriction within the Mileage Rule, Defendants have fixed, depressed and standardized the amount of money that may be awarded at Recognized Horse Shows resulting in illegal price-fixing that is a *per se* violation of *section 1*. Third Am. Compl. P 203. Plaintiffs also allege that the agreement of the Promoter Defendants to enforce the Mileage Rule is a horizontal allocation of markets that is a *per se* violation of *section 1*. Third Am. Compl. P 204. Plaintiffs further allege that "the activity of the Defendants to cause the Federation to deny permission to Plaintiffs to compete in the Relevant Market constitutes an illegal boycott that is a *per se* violation" of *section 1*. Third Am. Compl. P 205.

However, in the Eleventh Circuit, "[t]he presumption in cases brought under *section 1* of the [\*47] Sherman Act is that the rule-of-reason standard applies." *Seagood*, 924 F.2d at 1567. Furthermore, there is substantial case law rejecting a *per se* approach in examining the action taken by sporting associations. See *NCAA*, 468 U.S. at 100-01; see also *Cha-Car, Inc. v. Calder Race Course, Inc.*, 752 F.2d 609, 613 (11th Cir. 1985); *Hatley v. American Quarter Horse Ass'n*, 552 F.2d 646, 652-53 (5th Cir. 1977); *Martin v. American Kennel Club, Inc.*, 697 F. Supp. 997, 1000 (N.D. Ill. 1988). Since under a *per se* analysis there is no inquiry into possible justifications for the challenged restraint, the *per se* doctrine should not be extended to restraints that are of ambiguous effect. See *Cha-Car*, 752 F.2d at 612-13.

"The decision to apply the *per se* rule turns on 'whether the practice facially appears to be one that would always or almost always tend to restrict competition and decrease output.'" *Northwest Wholesale Stationers, Inc. v. Pacific Stationery & Printing Co.*, 472 U.S. 284, 289-90, 105 S. Ct. 2613, 86 L. Ed. 2d 202 (1985)(quoting *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.* 441 U.S. 1, 19-20, 99 S. Ct. 1551, 60 L. Ed. 2d 1 (1979)). [\*48] The Mileage Rule as promulgated by USEF, including its prize money requirement, and application thereof by the Promoter Defendants, is not a practice which facially appears to be one that would always or almost always tend to restrict competition.

Therefore, the Court finds that Plaintiffs have failed to establish *per se* violations of the Sherman Act and a "rule of reason" analysis should be applied. Specifically, despite Plaintiffs' efforts to couch Defendants' conduct in terms of traditionally *per se* illegal activities, the field of sports is one "in which horizontal restraints on competition are essential if the product is to be available at all." See *NCAA*, 468 U.S. at 101. That is, the self-regulation which is present here by virtue of the operation of the NGB for equestrian sport exempts Defendants' conduct from *per se* analysis. See *Cha-Car*, 752 F.2d at 614 n.9.

#### **ii. Is the Mileage Rule Unreasonable Under the Rule of Reason?**

"Under Eleventh Circuit case law, alleged Section One agreements analyzed under the rule of reason require a plaintiff 'to prove (1) the anticompetitive effect of the defendant's conduct on the relevant market, [\*49] and (2) that the defendant's conduct had no pro-competitive benefit or justification.'" *Spanish Broadcasting System of Florida, Inc. v. Clear Channel Communications, Inc.*, 376 F.3d 1065, 1071 (11th Cir. 2004) (quoting *Levine*, 72 F.3d at 1551); see also *Retina Associates*, 105 F.3d at 1383 (requires proof that defendant's conduct had an anticompetitive effect in the relevant market, either by establishing actual anticompetitive effect or potential for genuine anticompetitive effect in defined geographic and product markets, and that no pro-competitive rationale would justify conduct).

The burden of proving an unjustified anticompetitive effect is on the Plaintiffs. See [Seagood, 924 at 1570](#). However, since the Defendants do not specifically address whether the alleged violative conduct has restrained competition in the Relevant Market, for purposes of its rule of reason analysis, this Court will presume without finding that Plaintiffs have demonstrated an anticompetitive effect in the Relevant Market. The Court must then determine whether the Defendants' conduct had any pro-competitive benefit or justification. At the heart of [\*50] this inquiry is the Mileage Rule itself.

Under the rule of reason analysis, this Court must evaluate the challenged rule in light of the factual context of the particular industry, the history of the restraint, and the reason for its imposition<sup>21</sup> in order to determine whether its anticompetitive effects outweigh its pro-competitive benefits. See [National Society of Professional Engineers v. United States, 435 U.S. 679, 98 S. Ct. 1355, 55 L. Ed. 2d 637 \(1978\)](#); see also [Cooney v. American Horse Shows Ass'n, 495 F. Supp. 424, 431 \(S.D.N.Y. 1980\)](#). The record before this Court demonstrates the reasonableness of the Mileage Rule.

Plaintiffs suggest that the Mileage Rule has no purpose other than to effect some sort of elaborate scheme whereby they are precluded from acquiring their desired dates to promote A-Rated Shows in the Relevant Market. Specifically, Plaintiffs contend "[t]he Mileage Rule [\*51] has no purpose other than to insure that incumbent promoters of shows covered by the Mileage Rule do not face any competition within a 250 mile radius, unless they are willing in the exercise of their unfettered discretion to tolerate a new entrant by granting a waiver from the Mileage Rule's monopoly grant." Plaintiffs' assertion is not supported by the evidence before this Court.

The Mileage Rule has several pro-competitive functions relating to equestrian sport. As discussed above, the Mileage Rule is an effective way to minimize scheduling conflicts. USEF's Mission Statement states, in relevant part:

As the National Governing Body (NGB) of Equestrian Sport in the United States we will inspire, encourage interest in, and regulate equestrian competition by ensuring the safety and well-being of the horses . . . promote the pursuit of excellence in equestrian sport from junior and grass roots programs to Olympic Games . . . [t]o accomplish this mission, our members and staff, working together will:

- (3) Protect and support the welfare of horses by inspecting, monitoring and testing to deter use of forbidden substances and other cruel, unsafe and/or unsportsmanlike [\*52] practices and by adopting and enforcing rules to prohibit such practices . . .
- (6) Provide the strongest possible U.S. representation internationally . . .
- (12) Serve as the coordinating body for equestrian activity in the United States . . .
- (13) Coordinate the calendar of competitions . . . and provide for varying levels of regional and national competition in a wide variety of disciplines to increase the breadth and depth of the sport throughout the country . . .

(Doc. No. 305, pp. i-ii). The Mileage Rule aids USEF in ensuring horses and United States athletes can compete at the highest levels both in the United States and internationally. Specifically, the Mileage Rule disperses hunter and jumper competitions geographically, thereby making it more likely that the best athletes and horses will compete against one another. (Doc. No. 289, Exh. 2, O'Connor Decl., P 6, Doc. No. 289, Exh. 5, Balch Dep., pp. 111 - 112 and Doc. No. 289, Exh. 4, Long Dep., pp. 64 - 65). A-Rated Shows attract the best athletes and horses. However, not a large number of horses and athletes can compete at the highest levels. If there were numerous A-Rated Shows in close geographic [\*53] proximity on the same days, as might occur without the Mileage Rule, it is less likely that the best horses and athletes would compete against each other as the top horses and athletes would instead be dispersed among those A-Rated Shows. (Doc. No. 289, Exh. 2, O'Connor Decl., P 6).

Furthermore, the Mileage Rule promotes the health and welfare of the horses by removing incentives for horse owners to overuse their horses by chasing "points" and prize money on the same or proximate days at multiple competitions in the same geographic area. (Doc. No. 289, Exh. 2, O'Connor Decl., P 7, Doc. No. 289, Exh. 5, Balch

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<sup>21</sup> There is no evidence before this Court as to why the Mileage Rule was originally implemented.

Dep., pp. 112 - 113, 133 - 137 and Doc. No. 289, Exh. 3, O'Connor Dep., pp. 51 - 52). Lastly, the Mileage Rule aids USEF in fostering the development of equestrian sport across the United States, not just in former regional centers such as the Northeast. (Doc. No. 289, Exh. 5, Balch Dep., p. 111).

USEF, as the NGB for equestrian sport, utilizes the Mileage Rule to achieve several pro-competitive functions. There is no evidence in the record that in denying the Plaintiffs' waiver requests, the Promoter Defendants as members did any more than abide by USEF's rules in operating [\*54] their respective horse shows. Furthermore, under the January 2005 rule changes, the Promoter Defendants will not have "unfettered discretion" to waive the Mileage Rule because USEF "shall determine whether it is in the best interest of the sport to either deny or grant the waiver and under what terms and conditions such waiver shall be given." (Doc. No. 344, Exh. A, GR213). Therefore, applying the rule of reason, the Court finds that under the facts of this case the Mileage Rule does not result in an unreasonable restraint of trade.

#### **4. Section 2 of the Sherman Act, 15 U.S.C. § 2 (Counts II - IV)**

Section 2 of the Sherman Act is directed against "[e]very person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States." [15 U.S.C. § 2](#). Broadly speaking, there are three distinct violations actionable under section 2 of the Sherman Act: (1) monopolization; (2) attempt to monopolize; and (3) conspiracy to monopolize. In their Third Amended Complaint, Plaintiffs allege all three violations.

As an initial matter under [\*55] the Court's section 2 analysis, USEF argues that it is entitled to summary judgment on Counts II - IV, as well as the related Florida state law claims (Counts VI, VII, VII, and IX (in part)), since it is not a competitor in the relevant market and because Plaintiffs' "shared monopoly" theory is unsupported by the facts and law. This Court agrees that USEF is not a competitor in the Relevant Market. According to Plaintiffs, the Relevant Market is A-Rated Shows in the state of Florida during the winter months. It is undisputed that USEF is the NGB for equestrian sport in the United States and not a horse show promoter, operator or manager in this alleged market (Doc. No. 289, Long Decl., P 17). Nor is there any credible evidence in the record that the Promoter Defendants control or influence USEF. Since USEF does not compete in the Relevant Market, USEF is entitled to summary judgment on Plaintiffs' section 2 claims based upon the argument that it does not compete in the Relevant Market. See [Aquatherm Industries, Inc. v Florida Power & Light Company, 145 F.3d 1258, 1261 \(11th Cir. 1998\)](#); see also [Spanish Broadcasting System, 376 F.3d at 1075](#). The Court [\*56] will address Plaintiffs' "shared monopoly" theory of liability in greater detail below.

Plaintiffs claim that Defendants have used USEF's protected status as a NGB to "create a series of monopolies" in the Relevant Product Market. The Court finds that Plaintiffs have failed to present evidentiary support for the elements of their claims for monopolization offenses under section 2 of the Sherman Act.

##### **i. Monopolization (Count II)**

To establish a claim for monopolization, plaintiffs must demonstrate that Defendants: (1) possessed monopoly power in the relevant market and (2) willfully acquired or maintained that power, as distinguished from growth or development as consequence of superior product, business, acumen, or historic accident. See [Morris Communications Corp. v. PGA Tour, Inc., 364 F.3d 1288, 1293-94 \(11th Cir. 2004\)](#)(citing [United States v. Grinnell Corp., 384 U.S. 563, 570-71, 86 S. Ct. 1698, 16 L. Ed. 2d 778 \(1966\)](#)). "Monopoly power" is defined as "the power to control prices or exclude competition in the relevant market." [United States v. E.I. duPont de Nemours & Co., 351 U.S. 377, 391, 76 S. Ct. 994, 100 L. Ed. 1264 \(1956\)](#).

Under a "shared monopoly" theory, [\*57] Plaintiffs have alleged Defendants possess market power. Specifically, with respect to their monopolization claim under section 2 of the Sherman Act, Plaintiffs allege that "[t]he Federation, together with the non-Federation Defendants and/or other unnamed coconspirators, possess monopoly power in the Relevant Market due to their control over available dates for Recognized Horse Shows under the Federation Rules." Third Am. Compl. P 220. The record evidence does not demonstrate that any individual Defendant had the power to control prices or exclude competition from the market. Rather, at most, the Promoter

Defendants possess what Plaintiffs have termed a "perfect and permanent serial" monopoly. This is not sufficient to establish a claim for monopolization under [section 2](#) of the Sherman Act.

The Eleventh Circuit has not directly addressed whether claims based on a "shared monopoly" may constitute a violation of [section 2](#) of the Sherman Act. In October 2003, in denying the then Defendants' <sup>22</sup> motions to dismiss Plaintiffs' amended complaint, this Court found that "the concept of a 'shared monopoly' cannot be excluded at this juncture" (Doc. No. 59). At the summary judgment stage, [\*58] however, the Court declines to accept the concept of a shared monopoly as a basis for [section 2](#) liability under Plaintiffs' claims for monopolization and attempted monopolization. Only [section 2](#)'s conspiracy to monopolize claim targets concerted action. See [Carpet Group, Int'l v. Oriental Rug Importers Ass'n](#), 256 F. Supp. 2d 249, 283- 85 (D. NJ 2003); see also [ID Security Systems, Inc. v. Checkpoint Systems, Inc.](#), 249 F. Supp. 2d 622, 649 (E.D. Pa. 2003).

Even if this Court were to accept the concept of a shared monopoly, Plaintiffs have failed to set forth facts sufficient to establish that USEF and the Promoter Defendants share monopoly power in the Relevant Market. Here we have a small Relevant Market, i.e., the state of Florida, in which numerous entities [\*59] promote anywhere from 26 to 31 A-Rated Shows during the approximately seventeen (17) weeks that make up the winter months. There is no evidence before this Court that any of the individual Promoter Defendants expanded or combined their limited "perfect and permanent serial" monopolies to achieve market power in the Relevant Market.

## ii. Attempted Monopolization (Count III)

To establish a claim for attempted monopolization, plaintiffs must demonstrate: "(1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." [Spectrum Sports, Inc. v. McQuillan](#), 506 U.S. 447, 456, 113 S. Ct. 884, 122 L. Ed. 2d 247 (1993). "Anticompetitive conduct is 'the use of monopoly power, however lawfully acquired, to foreclose competition, to gain a competitive advantage, or to destroy a competitor.'" [Covad Communications Co. v. BellSouth Corp.](#), 299 F.3d 1272, 1283 (11th Cir. 2002), vacated on other grounds, 540 U.S. 1147, 124 S. Ct. 1143, 157 L. Ed. 2d 1040 (2004), quoting [United States v. Griffith](#), 334 U.S. 100, 107, 68 S. Ct. 941, 92 L. Ed. 1236 (1848)). "Proof of the intent element [\*60] requires proof of 'a specific intent to destroy competition or build a monopoly.'" See [Retina Associates](#), 105 F.3d at 1385 (quoting [Times-Picayune Publishing Co. v. United States](#), 345 U.S. 594, 73 S. Ct. 872, 97 L. Ed. 1277 (1953)). Plaintiffs allege that Promoter Defendants together have prevented competition from new Recognized Competitions because entities who submit timely applications to hold Recognized Competitions, accompanied by the applicable fees, do not have the same access to dates for Recognized Competitions as existing promoters and managers. The Court declines to accept the concept of a shared monopoly as a basis for [section 2](#) liability under Plaintiffs' claim for attempted monopolization. Furthermore, Plaintiffs have failed to demonstrate that the Promoter Defendants engaged in predatory or anticompetitive conduct when they unilaterally refused to grant Plaintiffs' waiver requests. There is also insufficient evidence from which a jury could find that any of the Promoter Defendants acted with a "specific intent to monopolize" when they unilaterally opted to adhere to the USEF rules. Lastly, Plaintiffs do not point to any record evidence supporting [\*61] an inference that the Promoter Defendants' unilateral conduct created a "dangerous probability" that they would succeed in achieving a monopoly.

## iii. Conspiracy to Monopolize (Count IV)

To establish a claim for conspiracy to monopolize, plaintiffs must prove "(1) concerted action deliberately entered into with the specific intent of achieving a monopoly; and (2) the commission of at least one act in furtherance of the conspiracy." [Moecker](#), 144 F. Supp. 2d. at 1310 (quoting [Todorov](#), 921 F.2d at 1460 n.5). See also ABA Section of [Antitrust Law](#), [Antitrust Law](#) Developments, p. 308 (5th ed. 2002); [Thompson v. Metropolitan Multi-List](#), 934 F.2d 1566, 1582 (11th Cir. 1991). A claim for conspiracy to monopolize does not require a showing of monopoly power. See [Levine](#), 72 F.3d at 1555.

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<sup>22</sup> David E. Burton, Sr., David E. Burton, Jr., Burtons and Sons, Inc., Littlewood Fences, Inc., Kernan Hodges, USA Equestrian, Inc., Bob Bell, Classic Company, Ltd. and North Florida Hunter & Jumper Association, Inc.

Since the most Plaintiffs can establish is that an individual promoter may have a "serial monopoly" for its protected dates, which make up only a portion of the total number of dates available for A-Rated Shows in the Relevant Market, no jury could find that an individual promoter acted with a specific intent to monopolize the Relevant [\*62] Market. See Feldman v. Jackson Mem'l Hosp., 571 F. Supp. 1000, 1010 - 11 (S.D. Fla. 1983). Furthermore, as discussed above in relation to section 1, the evidence before this Court does not demonstrate that the Promoter Defendants acted in knowing concert or "conspired" when they individually refused to grant the Plaintiffs' requested waivers of the Mileage Rule.

### **5. Florida Antitrust Act, FLA. STAT. §§ 542.18 and 542.19 (Counts V - VIII)**

The Florida Antitrust Act provides that "[e]very contract, combination, or conspiracy in restraint of trade or commerce in this state is unlawful." FLA. STAT. § 542.18 (2002). Furthermore, "[i]t is unlawful for any person to monopolize, attempt to monopolize, or combine or conspire with any other person or persons to monopolize any part of trade or commerce in this state." Flat. Stat. § 542.19 (2002). "Federal and Florida antitrust laws are analyzed under the same rules and case law." All Care Nursing Service, Inc. v. High Tech Staffing Services, Inc., 135 F.3d 740, 745 n.11 (11th Cir. 1998). "[T]he Florida legislature has, in effect, adopted as the law of Florida the body of antitrust law developed [\*63] by the federal courts under the Sherman Act. St. Petersburg Yacht Charters, Inc. v. Morgan Yacht, Inc., 457 So. 2d 1028, 1032 (Fla. 2nd DCA 1984). Therefore, for the same reasons this Court has found no violation of the Federal antitrust laws, this Court finds that Plaintiffs have failed to establish the elements of a violation of FLA. STAT. §§ 542.18 and 542.19.

### **6. Florida Deceptive and Unfair Trade Practices Act, FLA. STAT. §§ 501.201 et seq. (Count IX)**

Count IX alleges violations of the Florida Deceptive and Unfair Trade Practices Act ("FDUTPA"). FLA. STAT. § 501.201 et seq. FDUTPA provides that unfair methods of competition, unconscionable acts or practices, and unfair or deceptive acts or practices in the conduct of any trade or commerce are unlawful. FLA. STAT. § 501.204(1). Sub-section 501.203(3) provides that a violation of the Federal Trade Commission Act constitutes a violation of FDUTPA. The law also provides that in construing this provision, great weight should be given to the interpretations of the Federal Trade Commission and the federal courts relating to § 5(a)(1) of the Federal Trade Commission Act. FLA. STAT. § 501.202. Unquestionably, [\*64] antitrust claims fall within § 5(a)(1) of the Federal Trade Commission Act. See Indiana Fed'n of Dentists, 476 U.S. at 454-55. Plaintiffs' FDUTPA claim is based on the same allegations as their antitrust claims.<sup>23</sup> Third Am. Compl. P 262. Therefore, for the same reasons this Court has found no violation of the Federal antitrust laws, this Court finds that Plaintiffs have failed to establish the elements of a violation of FLA. STAT. § 501.201 et seq.

### **IV. Conclusion**

The Court finds that under the facts of this case there are no grounds under which Plaintiffs are entitled to relief under the antitrust law. See First National Bank of Arizona v. Cities Service Co., 391 U.S. 253, 288, 88 S. Ct. 1575, 20 L. Ed. 2d 569 - 89, 391 U.S. 253, 88 S. Ct. 1575, 20 L. Ed. 2d 569 (1968). Accordingly, it is **ORDERED AND ADJUDGED** that:

- (1) Defendant United States Equestrian Federation, Inc.'s ("USEF") Motion for Summary Judgment (Doc. [\*65] No. 287) is **GRANTED**. USEF's Request for Oral Argument is **DENIED**.
- (2) Defendants', David E. Burton, Sr., David E. Burton, Jr., Burtons and Sons, Inc. and Littlewood Fences, Inc. (collectively, "the Burton Defendants"), Motion for Summary Judgment is (Doc. No. 290) is **GRANTED**.
- (3) Defendants', Thomas Struzzieri ("Struzzieri"), Horse Shows in the Sun, Inc. ("HITS") and Rose View Stables, Ltd. ("Rose View Stables")(collectively "the HITS Defendants"), Motion for Summary Judgment (Doc. No. 292) is **GRANTED**.

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<sup>23</sup> Plaintiffs concede that their FDUTPA claims "survive" or "fall" with their antitrust claims.

(4) Defendants', Stadium Jumping, Inc. ("Stadium Jumping") and Eugene R. Mische ("Mische)(collectively, "the Stadium Jumping Defendants"), Motion for Entry of Final Summary Judgment (Doc. No. 294) is **GRANTED**.

Defendants', Stadium Jumping, Inc. ("Stadium Jumping") and Eugene R. Mische ("Mische)(collectively, "the Stadium Jumping Defendants"), Request for Oral Argument (Doc. No. 295) is **DENIED**.

(5) Since the Court has found Plaintiffs' claims are barred by the Defendants' implied immunity, all claims against Defendants Linda S. Aldrich and Fox Lea Farms, Inc. shall be dismissed.

(6) The Pretrial Conference in the above-captioned **[\*66]** matter which was previously scheduled for Friday, May 13, 2005, at 8:30 a.m. is hereby cancelled.

(7) The Clerk is directed to enter judgment in favor of Defendants United States Equestrian Federation, Inc., David E. Burton, Sr., David E. Burton, Jr., Burton and Sons, Inc., Littlewood Fences, Inc., Thomas Struzzieri, Horse Shows in the Sun, Inc., Rose View Stables, Ltd., Stadium Jumping, Inc. and Eugene R. Mische and **CLOSE** this case.

**DONE AND ORDERED** at Tampa, Florida, this 9th day of May, 2005.

/s/

SUSAN C. BUCKLEW

United States District Judge

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## S. Coast Cab Co. v. City of Anaheim

United States District Court for the Central District of California, Southern Division

May 16, 2005, Decided; May 17, 2005, Filed

Case No. SA CV 99-416-GLT (ANx)

**Reporter**

2005 U.S. Dist. LEXIS 63364 \*

SOUTH COAST CAB CO., INC. et al., Plaintiffs, vs. CITY OF ANAHEIM et al., Defendants.

**Prior History:** [S. Coast Cab Co. v. City of Anaheim, 2005 U.S. App. LEXIS 7652 \(9th Cir. Cal., May 2, 2005\)](#)

### **Core Terms**

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cause of action, state court, franchise, Antitrust, damages, first amended complaint, merits, issue preclusion, parties, state case, relitigating, litigated, claim preclusion, violations, injunctive relief, motion to dismiss, permit system, permits, counter-motion, ordinance, taxicab, partial summary judgment, substantive due process, permitting process, prevents, courts, first cause, allegations, entitlement, rights

**Counsel:** [\*1] For John M Wolfe, Chapter 7 Trustee, Savvas Roditis, husband and wife, Irene Roditis, husband and wife, Plaintiffs: Maryann Cazzell, LEAD ATTORNEY, Cazzell and Associates, Santa Ana, CA USA.

For Hme Enterprises Inc, Real Party in Interest Plaintiff, Real Party in Interest Plaintiff: Jesse S Finlayson, LEAD ATTORNEY, Finlayson Toffer Roosevelt & Lilly LLP, Irvine, CA USA; Michael Raymond Williams, LEAD ATTORNEY, Finlayson Williams Toffer Roosevelt and Lilly LLP, Irvine, CA USA.

For The City of Anaheim, a Charter City, Richard Larochelle, individually and as a Code Enforcement officer on behalf of The City of Anaheim, John Poole, individually and as the Code Enforcement Manager on behalf of The City of Anaheim, Defendants: Moses W Johnson, IV, LEAD ATTORNEY, Anaheim City Attorneys Office, Anaheim, CA USA.

**Judges:** GARY L. TAYLOR, UNITED STATES DISTRICT JUDGE.

**Opinion by:** GARY L. TAYLOR

### **Opinion**

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ORDER ON (1) DEFENDANTS' MOTION TO DISMISS, (2) PLAINTIFFS' COUNTER-MOTION FOR PARTIAL SUMMARY JUDGMENT

Defendants' motion to dismiss is GRANTED IN PART. Plaintiffs' counter-motion for partial summary judgment is GRANTED IN PART.

**I. BACKGROUND**

Plaintiffs South Coast Cab Co. and its owners, Savvas and Irene Roditis, brought this federal [\*2] case and a state case challenging the City of Anaheim's procedure for permitting taxicab businesses in Anaheim and its later taxicab franchise system. The state case has now concluded. This Court recently reopened the federal case and granted

leave to amend the Complaint. Plaintiffs filed a First Amended Complaint, which Defendants now move to dismiss on the grounds of claim preclusion and issue preclusion.<sup>1</sup>

The First Amended Complaint contains five causes of action: (1) under [42 U.S.C. § 1983](#), substantive due process violations resulting from (a) the permitting process, (b) the "need or necessity" standard for obtaining a permit, (c) the process of changing from a permit system to a franchise system, (d) the franchise system itself; (2) under [§ 1983](#), procedural due process violations resulting from the permitting process; (3) under [§ 1983](#), equal protection violations resulting from disparate treatment during the permitting process and the creation and implementation of the franchise system, due to the individual Plaintiffs' Greek origin and the sex of the President of South Coast Cab Co.; (4) violations of the Sherman Antitrust Act entitling Plaintiffs to damages and injunctive relief; (5) under the Sherman Antitrust [[\\*3](#)] Act, violations of the "law of the case" and the spirit and intent of the Sherman Antitrust Act resulting from the City's intention to take away Plaintiffs' remaining 30 taxicab permits.

Defendants argue the state courts decided all of the issues raised in the First Amended Complaint. Plaintiffs filed a counter-motion for partial summary judgment, seeking a declaration they are entitled to damages as a result of the state court's finding the permit ordinance was unconstitutionally vague.

## II. DISCUSSION

The Court has carefully reviewed the First Amended Complaint, the six versions of the complaint in the state case, and the seven opinions of the state trial and appellate courts, which the parties provided to the Court.<sup>2</sup> Claim preclusion and issue preclusion prevent many, but not all, of Plaintiffs' claims from being litigated in this case.

### A. Legal Standards

Claim preclusion means "a valid final adjudication of a claim precludes a second action on that claim or any part of it." [Baker v. Gen. Motors Corp., 522 U.S. 222, 233 n.5 \(1998\)](#). It also applies to a claim that was not litigated but "should have been advanced in an earlier suit." [United Parcel Serv. v. Cal. Pub. Utils. Comm'n, 77 F.3d 1178, 1185 \(9th Cir. 1996\)](#) (quoting [Migra v. Warren City Sch. Dist. Bd. of Educ., 465 U.S. 75, 77 n.1, 104 S. Ct. 892, 79 L. Ed. 2d 56 \(1984\)](#)).

This federal Court must give claim preclusive effect to a state court judgment "whenever the courts [[\\*4](#)] of the State from which the judgment emerged would do so." [Id. at 1184-85](#) (quoting [Allen v. McCurry, 449 U.S. 90, 96, 101 S. Ct. 411, 66 L. Ed. 2d 308 \(1980\)](#)). California courts apply claim preclusion when "(1) the decision in the prior proceeding is final and on the merits; (2) the present proceeding is on the same cause of action as the prior proceedings; and (3) the parties in the present proceeding or parties in privity with them were parties to the prior proceeding." [Fed'n of Hillside & Canyon Ass'n v. City of Los Angeles, 126 Cal. App. 4th 1180, 1202, 24 Cal. Rptr. 3d 543 \(Ct. App. 2004\)](#). Claim preclusion "bars the litigation of not only issues that were actually litigated but also issues that could have been litigated." [Id.](#)

"Collateral estoppel, or issue preclusion, prevents parties from relitigating an issue of fact or law if the same issue was determined in prior litigation." [Resolution Trust Corp. v. Keating, 186 F.3d 1110, 1114 \(9th Cir. 1999\)](#); see also [United Parcel Serv., 77 F.3d at 1185](#) ("Issue preclusion, or collateral estoppel, 'refers to the effect of a judgment in foreclosing relitigation of a matter that has been litigated and decided.'") (quoting [Migra, 465 U.S. at 77 n.1](#)).

Federal courts apply issue preclusion to state court judgments "whenever the courts of the State from which the judgment emerged would do so." [United Parcel Serv., 77 F.3d at 1184-85](#) (quoting [Allen, 449 U.S. at 96](#)). California courts apply issue preclusion when "(1) the issue decided in the prior case is identical with the one now presented;

<sup>1</sup> Defendants also move to dismiss under [England v. Louisiana State Board of Medical Examiners, 375 U.S. 411, 84 S. Ct. 461, 11 L. Ed. 2d 440 \(1964\)](#). The Court considered this contention in the April 11, 2005 Order and will not reconsider it here.

<sup>2</sup> The Court grants Defendants' requests for judicial notice of these and other documents. It is appropriate to refer to documents outside the pleadings on this motion to dismiss. To determine claim and issue preclusion, the Court must refer to the previous decisions of the state courts. Also, neither party objects to the Court referring to state court documents.

(2) there was a final judgment on the merits in [\*5] the prior case; and (3) the party to be estopped was a party to the prior adjudication." Stoltz *v. Bank of Am., 15 Cal. App. 4th 217, 222, 19 Cal. Rptr. 2d 19 (Ct. App. 1993)*.

For purposes of both claim and issue preclusion, the parties agree they were also parties to the state case. The parties also agree the judgment in the state case is now final.

#### B. First Cause of Action

Plaintiffs' first cause of action seeks damages and injunctive relief under [§ 1983](#) for a substantive due process violation. The facts supporting the cause of action involve unfairness in the taxicab permitting process, the vague "need or necessity" standard for obtaining a permit, the process of changing from a permit system to a franchise system, and the franchise system itself.

The facts alleged regarding the permitting process, which are summarized in paragraph 78, lines 11-20 of the First Amended Complaint, all were alleged in the state complaints. Both the original complaint and the first amended complaint in the state case claimed a violation of substantive due process under the U.S. Constitution, which is the same cause of action raised here. The state court dismissed the due process cause of action. *South Coast Cab Co. v. City of Anaheim*, No. G026197, at \*18 (Cal. Ct. App. Dec. 19, 2000) (affirming [\*6] the dismissal of the due process cause of action). Plaintiffs agree the state court found no due process violation in the implementation of the permit system. (Pls.' Opp'n at 20:14-17.) The state decision is final and was on the merits. Claim preclusion bars relitigation of this claim.

As for the "need or necessity" standard for obtaining permits, summarized in paragraph 79 of the First Amended Complaint, this issue also was decided by the state court. Plaintiffs' second amended complaint in the state case raised the same facts as part of a writ of administrative mandamus cause of action.<sup>3</sup> The state court granted this cause of action because it found the permit ordinance unconstitutionally vague. *South Coast Cab Co.*, No. G026197, at \*18 (ordering the trial court to enter judgment in South Coast Cab's favor on the second amended complaint). This decision is final and on the merits. As discussed below on Plaintiffs' counter-motion for summary judgment, the decision has claim preclusive effect in this case. The Court will not relitigate the allegations in paragraph 79 of the First Amended Complaint or the constitutionality of the "need or necessity" standard for obtaining permits.

Turning [\*7] to the allegations surrounding the franchise system, the causes of action and issues raised by Plaintiffs already have been decided by the state courts. All of the facts Plaintiffs allege, summarized in paragraph 78 of the First Amended Complaint, also were alleged in the third amended complaint or the verified second supplemental complaint in the state case. The state court rejected all of Plaintiffs' contentions. In April 2003, the appellate court rejected any constitutional cause of action Plaintiffs could allege with respect to the franchise system. *South Coast Cab Co. v. City of Anaheim*, No. G030551, [2003 Cal. App. Unpub. LEXIS 3844, at \\*14-23 \(Cal. Ct. App. Apr. 17, 2003\)](#). The court found no legal basis for striking down the franchise ordinance or exempting Plaintiffs from the ordinance. *Id.* at \*2.

In December 2004, the state appellate court affirmed the dismissal of "all claims brought against the City of Anaheim by South Coast Cab Company." *South Coast Cab Co. v. City of Anaheim*, Nos. G031608 & G034127, [2004 Cal. App. Unpub. LEXIS 11789, at \\*2 \(Cal. Ct. App. Dec. 27, 2004\)](#). This included affirming a November 2002 summary judgment decision by the trial court in the City's favor, which was directed to the "various constitutional claims" relating to the franchise alleged in the 2002 verified second supplement complaint. *Id.* at \*12. After [\*8] the November 2002 summary judgment and the December 2004 decision, the state courts had "ruled substantively on all causes of action which had either survived [the December 2000 opinion] or which had been asserted afterwards." *South Coast Cab Co. v. City of Anaheim*, No. G032823, [2004 Cal. App. Unpub. LEXIS 2365, at \\*14 \(Cal. Ct. App. Mar. 15, 2004\)](#).

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<sup>3</sup> Plaintiffs also alleged the same facts in the first amended complaint as part of a substantive due process cause of action. Claim preclusion bars relitigation of a substantive due process cause of action based on these facts because, as discussed above, the state court rejected due process claims relating to the permit process.

Plaintiffs argue the state decisions regarding the franchise system were based on Plaintiffs' failure to exhaust administrative remedies. Because exhaustion of administrative remedies is not required under [§ 1983](#), Plaintiffs contend the state decisions do not preclude this Court from considering constitutional challenges to the franchise system.

The Court disagrees. First, the 2002 verified second supplemental complaint raised the same cause of action as Plaintiffs' substantive due process challenge in this case. Although not called a "substantive due process" cause of action, it alleged the franchise ordinance, the process of selecting franchisees, and the implementation of the franchise was "unconstitutional on its face or as implemented." The complaint alleged Plaintiffs would be deprived of their vested property rights. This alleges a substantive due process cause of action, and it appears the state courts construed [\*9] is as such. The state courts rejected the cause of action. Claim preclusion prevents relitigation of the cause of action in this case.<sup>4</sup>

Also, a fair reading of the state court opinions shows they did not rely on failure to exhaust administrative remedies when rejecting Plaintiffs' constitutional challenge to the franchise system. Although the December 2004 state decision refers to exhaustion of administrative remedies, it also refers repeatedly to the April 2003 decision, which considered the constitutionality of the franchise system. The April 2003 decision found there was no causation between the franchise system and Plaintiffs' inability to operate a taxicab business in Anaheim because Plaintiffs did not apply for a franchise. Causation is required in a [§ 1983](#) claim: "Every person who . . . subjects, or causes to be subjected, any citizen . . . to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured . . ." [42 U.S.C. § 1983 \(2003\)](#) (emphasis added). The state court found any deprivation of Plaintiffs' rights was not caused by Defendants. This precludes relitigation of the issue of causation in this case. Plaintiffs may not [\*10] litigate their [§ 1983](#) challenge to the franchise system in this Court.

In sum, all of Plaintiffs' substantive due process allegations regarding the permit system and the franchise system have already been decided by the state courts. The first cause of action is DISMISSED with prejudice.

#### C. Second Cause of Action

Plaintiffs' second cause of action is for damages and injunctive relief under [§ 1983](#) for procedural due process violations. The facts supporting the cause of action relate to the permit procedure. Plaintiffs raised these facts in the first amended complaint in the state case, alleging a procedural due process violation under the U.S. Constitution. This is the same cause of action now alleged in this case. The state court rejected this claim on the merits: "The due process claims . . . were necessarily predicated on the impropriety of the permit denials as such . . . Therefore the demurrer was properly sustained without leave to amend as to those claims." [South Coast Cab Co., No. G026197](#), at \*8. Plaintiffs agree the state court found "*under the permit system, there was no due process violation.*" (Pls.' Opp'n at 20:14.) The parties do not dispute this decision is final. Claim preclusion [\*11] prevents Plaintiffs from relitigating the procedural due process cause of action in this Court. The second cause of action is DISMISSED with prejudice.

#### D. Third Cause of Action

Plaintiffs' third cause of action seeks damages and injunctive relief under [§ 1983](#) for equal protection violations. The supporting facts allege that, because Plaintiffs are of Greek origin and the president of South Coast Cab is a woman, Defendants discriminated against them during the permitting process and during the creation and implementation of the franchise system.

The record shows the state court thoroughly explored and decided the issue of disparate treatment. Plaintiffs raised the same issue in the state case through a cause of action under the California Unruh Civil Rights Act. The first cause of action in the first amended complaint alleged discriminatory treatment due to national origin and sex in

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<sup>4</sup> To the extent Plaintiffs believe the state courts erroneously relied on failure to exhaust administrative remedies in connection with the substantive due process cause of action, that would be the subject of an appeal within the state court system, not relitigation by this federal Court. This Court does not review state court decisions.

connection with the permit process. The first cause of action in the third amended complaint alleged the right to "equal protection under the laws . . . of the United States of America" in connection with the permit process and the franchise system. These are the same issues of fact and law Plaintiffs now allege [\*12] in this federal case.

The state courts granted a demurrer without leave to amend as to the Unruh Civil Rights Act claims. South Coast Cab did not challenge the sustaining of the demurrs. South Coast Cab Co. v. LaRochelle, No. G030079, [2003 Cal. App. Unpub. LEXIS 3841, at \\*6 \(Cal. Ct. App. Apr. 17, 2003\)](#).

In a separate opinion, the state court concluded Plaintiffs could not show disparate treatment in connection with the franchise system. See South Coast Cab Co., No. G030551, at \*17, 14-23 ("[W]e have examined the record very critically to determine whether the franchise system was subtly structured in such a way as to deter South Coast Cab from applying for a franchise."); see also South Coast Cab Co., Nos. G031608 & G034127, at \*11-15. The court concluded, "the record is remarkably free of anything that shows any animus toward South Coast Cab." South Coast Cab Co., No. G030551, at \*16. Issue preclusion prevents Plaintiffs from relitigating their equal protection claims.

Plaintiffs' third cause of action is DISMISSED with prejudice.

#### E. Fourth Cause of Action

Plaintiffs' fourth cause of action seeks damages and an injunction under the Sherman Antitrust Act, apparently in connection with both the permit process and the franchise system. As discussed in this [\*13] Court's April 11, 2005 Order, the Sherman Antitrust Act claim in the state court did not result in a final judgment on the merits because the state court did not have jurisdiction to hear the claim. Claim preclusion and issue preclusion do not apply.

Defendants move to dismiss the claim on the merits, arguing municipalities and their employees are immune from damages under the Sherman Antitrust Act. Plaintiffs state they did not construe Defendants' motion as a motion on the merits, and they did not respond on the merits. (Pls.' Opp'n at 2:4-12.) Their confusion is understandable because Defendants' motion presented no analysis of this issue, simply quoting lengthy portions of the state court decisions. (Defs.' Mot. at 22:6-25:22.) Nonetheless, Defendants state they are moving to dismiss on the merits. (Defs.' Reply at 1:13-17.) Because the parties argued the merits of the federal antitrust claim in the state case, because the state court made findings on the claim (albeit without jurisdiction to do so), because the merits of the damages claim appear to be clear from the face of federal antitrust laws themselves, and in the interest of advancing this prolonged litigation as quickly [\*14] as possible, the Court considers the merits of the motion to dismiss the Sherman Antitrust Act claim.

As for damages under the Sherman Antitrust Act, the Clayton Act, another federal antitrust law, incorporates the Sherman Antitrust Act into its definition of "antitrust laws." [35 U.S.C. § 12\(a\) \(Supp. 2005\)](#). In § 15, the Clayton Act states injured parties may recover damages under the "antitrust laws." Id. § 15(a) (1997). However, the Local Government Antitrust Act of 1984, states damages under § 15 of the Clayton Act may not be recovered "from any local government, or official or employee thereof acting in an official capacity." Id. § 35(a). Therefore, damages may not be recovered from local governments or officials under the Sherman Antitrust Act.

Plaintiffs attempt to avoid this rule by claiming "Defendants lost any anti-trust immunity by acting outside of any protected 'state action.'" (First Am. Compl. ¶ 90.) Issue preclusion prevents Plaintiffs from prevailing on this claim. The state court already considered whether the individual Defendants, Richard LaRochelle and John Poole, acted in their official capacities. The court concluded they did. South Coast Cab Co., No. G030079, at \*8-11. This Court will not relitigate whether [\*15] these Defendants acted in an official capacity.

Plaintiffs also claim they are entitled to damages under § 1983 for a violation of the Sherman Antitrust Act. Defendants do not really discuss whether Plaintiffs may recover § 1983 damages if the City violated the Sherman Antitrust Act. Plaintiffs may proceed on this theory for now, and a further motion may be brought by either party.

Turning to the request for injunctive relief under the Sherman Antitrust Act, Defendants do not show why the claim should be dismissed on the merits. The state court recognized injunctive relief may be available against the City.

South Coast Cab Co., No. G030079, at \*7 ("The federal statute does impliedly allow *injunctive* relief against cities."). This appears to be correct, given the Ninth Circuit's holding the Sherman Antitrust Act "applies to local governments as well as individuals and businesses." [A-1 Ambulance Serv. v. County of Monterey, 90 F.3d 333, 335 \(9th Cir. 1996\)](#). Defendants have not stated why they are immune from this general rule under the "state action immunity doctrine" or some other doctrine. See id.

Defendants' motion to dismiss the fourth cause of action is DENIED.<sup>5</sup>

#### F. Fifth Cause of Action

Plaintiffs' fifth cause of action also seeks injunctive relief under the Sherman Antitrust [\*16] Act. Here, Plaintiffs allege Defendants' stated intent to take away South Coast Cab's remaining 30 taxicab permits by May 31, 2006 violates the "law of the case," the spirit and intent of the December 2000 state court opinion, and the spirit and intent of section 1 of the Sherman Antitrust Act.

Because the fourth cause of action does not specify which facts form the basis for the cause of action, it is not apparent how the fifth cause of action is different from the fourth. Any violation of the "spirit and intent" of the Sherman Antitrust Act is adequately alleged in the fourth cause of action.

As to whether the franchise system violates the "law of the case" and the spirit and intent of the December 2000 state court opinion, issue preclusion prevents Plaintiffs from relitigating these issues. The state court considered and rejected these allegations:

One cannot extract from the [December 2000] opinion, as South Coast Cab has tended to do throughout these proceedings, an entitlement to permits sufficient to withstand an otherwise legitimate change from a permit system to a franchise system. The "spirit" of the opinion — a theme to which South Coast Cab often returns was that South Coast Cab should [\*17] have been given the permits it applied for when it applied for them, not that those permits were forever immune to some revision of the city's taxicab permit laws.

South Coast Cab Co., No. G030551, at \*13; see also id. at \*11-14, 14 (rejecting the "law of the case" theory).

The fifth cause of action is DISMISSED with prejudice.

#### G. Plaintiffs' Counter-Motion for Partial Summary Judgment

Plaintiffs' counter-motion for partial summary judgment essentially seeks a declaration stating a holding of the state court has preclusive effect in this case. Specifically, Plaintiffs ask the Court to find the state court's finding the permit system was unconstitutionally vague precludes this Court from finding otherwise and entitles Plaintiffs to damages.<sup>6</sup>

The Court finds the state court's finding has preclusive effect in this case. The December 2000 decision of the appellate court is final and was on the merits of the questions of the constitutionality of the permit ordinance and Plaintiffs' entitlement to the permits they applied for in April 1999. Paragraph 79 of Plaintiffs' First Amended Complaint raises these same issues. The state court holdings apply in this case. Plaintiffs also ask this Court to hold they are entitled [\*18] to damages under [§ 1983](#) as a result of this finding. The merits of this position have not been adequately briefed.<sup>7</sup> The Court does not decide this question. The parties may bring another motion or litigate

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<sup>5</sup> The Court does not rule on Defendants' contention the other taxicab franchisees are indispensable parties to an antitrust claim. The parties have not adequately briefed this issue.

<sup>6</sup> Defendants oppose the counter-motion procedurally, but not on the merits. Defendants have not shown they will be prejudiced if the Court considers the motion. The Court will consider the motion.

<sup>7</sup> For example, Plaintiffs assert their right to damages under [§ 1983](#) would stem from an equal protection violation. (Pls.' Opp'n at 3:23-4:9.) The state court did not find an equal protection violation, but found the permit ordinance was unconstitutionally vague.

whether Plaintiffs are entitled to damages and the amount of any damages. It appears Plaintiffs' first prayer for relief adequately claims entitlement to damages on this issue, and an amendment to the First Amended Complaint to add a new cause of action is likely not necessary. Still, the Court will consider a request for leave to amend the First Amended Complaint, if necessary.

**C. Conclusion**

The first, second, third, and fifth causes of action are DISMISSED WITH PREJUDICE. Given the procedural complexity of this case, it is worth noting this result is consistent with the April 11, 2005 Order. There, the Court found Plaintiffs had not litigated two [§ 1983](#) claims in state court: the damages claim pursuant to the finding the permit ordinance was unconstitutionally vague, and the damages claim for a violation of the Sherman Antitrust Act. (Apr. 11, 2005 Order at 6:4-10.) Without referring to the then-unfiled First Amended Complaint, the Court presumed Plaintiffs did not want to litigate [§ 1983](#) challenges [\*19] to the permit system or the franchise system. (Apr. 11, 2005 Order at 6:2-4.) Having now reviewed the First Amended Complaint, it is clear Plaintiffs do wish to litigate these claims. However, claim and issue preclusion bar them from doing so, a result the April 11, 2005 Order contemplated. (Apr. 11, 2005 Order at 6:24-27.)

**III. DISPOSITION**

Defendants' motion to dismiss is GRANTED IN PART. Plaintiffs' counter-motion for partial summary judgment is GRANTED IN PART.

DATED: May 16, 2005

/s/ Gary L. Taylor

GARY L. TAYLOR

UNITED STATES DISTRICT JUDGE

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## George Miller Brick Co., Inc. v. Stark Ceramics, Inc.

Supreme Court of New York, Monroe County

May 18, 2005, Decided

1995/01001

**Reporter**

9 Misc. 3d 151 \*; 801 N.Y.S.2d 120 \*\*; 2005 N.Y. Misc. LEXIS 1163 \*\*\*; 2005 NY Slip Op 25226 \*\*\*\*; 2005-2 Trade Cas. (CCH) P74,890

[\*\*\*\*1] George C. Miller Brick Co., Inc., Plaintiff, v. Stark Ceramics, Inc., Defendant.

**Prior History:** [George Miller Brick Co., Inc. v. Stark Ceramics, Inc., 2002 N.Y. Misc. LEXIS 2128 \(N.Y. Sup. Ct., May 20, 2002\)](#)

### **Core Terms**

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distributor, termination, bid, Brick, vertical, damages, contends, conspiracy, allegations, territorial, bifurcated, concerted action, supplier, treble, cases, price fixing, antitrust, reargument, summary judgment, anti trust law, response to interrogatory, antitrust action, manufacturer, rule of reason, resale price, reconsolidation, preclusion, products, retailer, motions

### **LexisNexis® Headnotes**

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Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **[HN1](#) [down arrow] Private Actions, Standing**

The *in pari delicto* defense is not applicable to certain New York private antitrust actions. A private antitrust action may be barred on the grounds of the plaintiff's own culpability only where: (1) as a direct result of his own actions, the plaintiff bears at least substantially equal responsibility for the violations he seeks to redress, and (2) preclusion of suit would not significantly interfere with the effective enforcement of the antitrust laws and protection of the public.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Legislation > Interpretation

Governments > Courts > Judicial Precedent

## **HN2** Public Enforcement, State Civil Actions

New York's Donnelly Act, [\*N.Y. Gen. Bus. Law § 340 et seq.\*](#), is construed in light of federal precedent and given a different interpretation only where state policy, differences in statutory language, or legislative history justify such a result.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > Sherman Act

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## **HN3** Price Fixing & Restraints of Trade, Vertical Restraints

Restraints imposed by agreement between competitors are denominated as horizontal restraints while those imposed by agreement between firms at different levels of distribution are vertical restraints. Under the Sherman Act, a vertical restraint of trade is not illegal per se unless it includes some agreement on price or price levels. Without an agreement as to a specific minimum price or price level, a vertical restraint is unlawful only if it fails a rule of reason analysis.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN4** Price Fixing & Restraints of Trade, Vertical Restraints

Neither the Sherman Act nor the Donnelly Act, [\*N.Y. Gen. Bus. Law § 340 et seq.\*](#), proscribes independent action. A one-sided practice is outside the scope of the Donnelly Act. Section 1 of the Sherman Act requires that there be a contract, combination or conspiracy, while the Donnelly Act requires a contract, agreement, arrangement or combination. [\*N.Y. Gen. Bus. Law § 340\(1\)\*](#).

Contracts Law > Types of Contracts > Lease Agreements > General Overview

Energy & Utilities Law > Oil & Petroleum Products > Gasoline Fuels > Gasoline Dealers & Distributors

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

9 Misc. 3d 151, \*151 N.Y.S.2d 120, \*\*120 2005 N.Y. Misc. LEXIS 1163, \*\*\*1163 2005 NY Slip Op 25226,  
■■■■■

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Leases & Licenses > Forfeiture Clauses

## [\*\*HN5\*\*](#) Types of Contracts, Lease Agreements

It long has been held under the Sherman Act that there is an actionable wrong whenever a restraint of trade or monopolistic practice has an impact on the market; and it matters not that the complainant may be only one merchant. The fact that a retailer can refuse to deal does not give the supplier immunity if the arrangement is one of those schemes condemned by the antitrust laws. Alleged concerted action involving a plaintiff knuckling under to pressure by the defendant to raise his prices can satisfy the concerted action requirement.

Antitrust & Trade Law > Regulated Practices > Private Actions > General Overview

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## [\*\*HN6\*\*](#) Regulated Practices, Private Actions

Preservation of the private antitrust action as an ever-present threat to deter anyone contemplating business behavior in violation of the **antitrust law** may outweigh any inequities that might result should a culpable plaintiff recover a windfall gain. Indeed, the United States Supreme Court has emphasized the inappropriateness of invoking broad common law barriers to relief where a private suit serves important public purposes.

Civil Procedure > Judicial Officers > Judges > Discretionary Powers

Governments > Courts > Judges

## [\*\*HN7\*\*](#) Judges, Discretionary Powers

The Supreme Court of New York has the inherent authority to control its own calendar provided that it does not exercise that discretion in a manner that conflicts with an existing legislative command. That control is authorized whether the trial justice is the original justice assigned to the case or the justice substituted for the original presiding justice.

Civil Procedure > ... > Methods of Discovery > Interrogatories > Format & Number of Interrogatories

Evidence > ... > Exemptions > Statements by Party Opponents > General Overview

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Methods of Discovery > Interrogatories > General Overview

Evidence > Types of Evidence > Judicial Admissions > General Overview

## [\*\*HN8\*\*](#) Interrogatories, Format & Number of Interrogatories

9 Misc. 3d 151, \*151 N.Y.S.2d 120, \*\*120 2005 N.Y. Misc. LEXIS 1163, \*\*\*1163 2005 NY Slip Op 25226,  
 ■■■■F

It is well settled that the response to an interrogatory is admissible as an admission of the respondent. However, because a response to an interrogatory is not a formal judicial admission, a response to an interrogatory is not binding and may be explained. It is for a trier of fact to determine the weight of the evidence in light of any explanation offered.

[Antitrust & Trade Law > ... > Private Actions > Costs & Attorney Fees > Clayton Act](#)

[Civil Procedure > ... > Jury Trials > Jury Instructions > Standard Instructions](#)

[Antitrust & Trade Law > ... > Private Actions > Costs & Attorney Fees > State Regulation](#)

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > Sherman Act > Remedies > General Overview](#)

[Antitrust & Trade Law > Sherman Act > Remedies > Damages](#)

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

[Civil Procedure > Pretrial Matters > Motions in Limine > General Overview](#)

[Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview](#)

[Civil Procedure > ... > Attorney Fees & Expenses > Basis of Recovery > Statutory Awards](#)

## **[HN9](#) [+] Costs & Attorney Fees, Clayton Act**

The Donnelly Act, [N.Y. Gen. Bus. Law § 340 et seq.](#), like the Sherman Act upon which it is modeled, requires the trebling of the damage award. [15 U.S.C.S. § 15](#); [N.Y. Gen. Bus. Law § 340\(5\)](#). The weight of federal authority prohibits any mention of the trebling requirement to the jury, because reference to treble damages and attorneys fees is irrelevant to the jury questions of liability and damages and may tend to confuse or prejudice a jury into reducing its eventual award, thus frustrating Congress's goal of deterring improper conduct by assessing treble damages and attorneys fees. Although the New York Supreme Court, Monroe County, can find no cases discussing this issue under the Donnelly Act, the court agrees with the rationale of the federal courts that have examined the issue.

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

[Civil Procedure > Trials > Separate Trials](#)

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

## **[HN10](#) [+] Private Actions, Remedies**

To be liable under the antitrust laws means that one has violated the antitrust laws and that violation has resulted in an injury to the business or property of the plaintiff, i.e., there was a fact of damage. Stated another way, to establish liability, a plaintiff must prove the existence of antitrust injury, which is to say, injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. A plaintiff must make some showing of actual injury attributable to something the antitrust laws were designed to prevent.

9 Misc. 3d 151, \*151 N.Y.S.2d 120, \*\*120 2005 N.Y. Misc. LEXIS 1163, \*\*\*1163 2005 NY Slip Op 25226,  
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Indeed, a treble-damage plaintiff may not recover for losses due to factors other than the defendant's antitrust violations. Thus, when an antitrust case has been bifurcated for trial, the plaintiff must establish during the liability portion of the trial that the violation caused him injury. This is true even in cases involving alleged per se violations.

Civil Procedure > Judgments > Relief From Judgments > Altering & Amending Judgments

Civil Procedure > Judgments > Preclusion of Judgments > Law of the Case

### **HN11** [blue] **Relief From Judgments, Altering & Amending Judgments**

Where a previous determination of a court on a particular issue was advisory only, it is subject to revision upon changed circumstances. [N.Y. C.P.L.R. 2221\(e\)\(2\)](#).

Civil Procedure > Pretrial Matters > Motions in Limine > General Overview

Civil Procedure > Judgments > Summary Judgment > Partial Summary Judgment

### **HN12** [blue] **Pretrial Matters, Motions in Limine**

Because a purported motion in limine, if granted, would not really limit the production of certain evidence, but rather, would effectively grant its proponents partial summary judgment on the critical substantive issue of what constitutes the opponents' causes of action, the proponents' motion, although labeled one in limine, actually is the functional equivalent of a motion for partial summary judgment dismissing the complaint.

Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > Timing of Motions & Responses

### **HN13** [blue] **Motions for Summary Judgment, Timing of Motions & Responses**

A summary judgment motion is precluded where it is filed more than 120 days after the note of issue is filed.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

Business & Corporate Law > Distributorships & Franchises > Termination > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### **HN14** [blue] **Price Fixing & Restraints of Trade, Vertical Restraints**

The Donnelly Act, [N.Y. Gen. Bus. Law § 340 et seq.](#), reaches competing distributors who conspire among themselves and with a supplier to terminate a fellow distributor for selling at a discount.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

### **HN15** [blue] **Price Fixing & Restraints of Trade, Vertical Restraints**

In **antitrust law**, resale price maintenance cases typically describe those situations where a manufacturer specifies a minimum price list for its product line and prohibits its distributors from underselling one another by lower than that price.

## **Headnotes/Summary**

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### **Headnotes**

#### **Monopolies -- Donnelly Act -- Vertical Price-Fixing Scheme -- "Concerted Action"**

1. Plaintiff, a terminated distributor of defendant's brick and tile products, was not precluded from recovering damages in a private antitrust action under the Donnelly Act ([General Business Law § 340 et seq.](#)) because of its own participation with defendant in an illegal bid-rigging and vertical price-fixing scheme in connection with the award of a construction contract. Plaintiff's allegation that it was economically coerced by defendant into submitting a noncompetitive bid for a public works project satisfied the "concerted action" requirement under the Donnelly Act, which applies to vertical restraint agreements, to state an actionable wrong without having to allege that other distributors were also involved in the conspiracy with defendant to restrain trade. Furthermore, in view of the allegations of vertical price-fixing, the "per se standard," rather than a rule of reason standard, was applicable to establish a Donnelly Act violation.

#### **Damages -- Treble Damages -- Donnelly Act Violation**

2. In a bifurcated private antitrust action under the Donnelly Act ([General Business Law § 340 et seq.](#)) in which plaintiff, a terminated distributor of defendant's brick and tile products, alleged that it was economically coerced by defendant into participating in an illegal bid-rigging and vertical price-fixing scheme in connection with the award of a construction contract, defendant was precluded from informing the jury that damages for a Donnelly Act violation would be trebled (see [General Business Law § 340 \[5\]](#)). Reference to treble damages would be irrelevant to the jury questions of liability and damages, and would only tend to confuse or prejudice the jury into reducing its eventual award.

#### **Monopolies -- Donnelly Act -- Vertical Price-Fixing Scheme -- Admissibility of Evidence of Distributor's Termination by Supplier during Liability Phase of Trial**

3. In a bifurcated private antitrust action under the Donnelly Act ([General Business Law § 340 et seq.](#)) in which plaintiff, a terminated distributor of defendant's brick and tile products, alleged that it was economically coerced by defendant into participating in an illegal bid-rigging and vertical price-fixing scheme in connection with the award of a construction contract, plaintiff was permitted to introduce evidence of its termination as a distributor of defendant's products during the liability portion of the trial. Since an "antitrust injury" was an element that had to be proven during the liability portion of the trial, evidence of plaintiff's termination was admissible during that phase of the trial to show such an antitrust injury.

**Counsel:** Charles W. Rogers, Rochester (*Mark Hannabury of counsel*), and Gates & Adams, Rochester (*Anthony J. Adams of counsel*), for plaintiff. Hiscock & Barclay, Rochester (*Thomas B. Cronmiller of counsel*), for defendant.

**Judges:** Kenneth R. Fisher, Justice Supreme Court.

**Opinion by:** Kenneth R. Fisher

## **Opinion**

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In 1995, plaintiff George C. Miller Brick Co., Inc., a distributor of brick and tile products, commenced this antitrust action under the [Donnelly Act](#) ([General Business Law § 340 et seq.](#)) against a supplier, defendant Stark Ceramics, Inc., seeking treble damages based on allegations of bid rigging and price fixing in April 1991 in connection with the award of a contract for [\*153] structural glazed facing tile on a construction project at the Albion Correctional Facility. The matter has been bifurcated for trial, the court (Stander, J.) having previously ordered separate trials on the issues of liability and damages.

Before the court are two motions brought by Miller. The first motion seeks an order (1) prohibiting Stark from putting on evidence or argument for the purpose of "explaining away" the response to interrogatory [\*\*\*2] No. 18 (c); (2) prohibiting Stark from advising the jury that damages for a [Donnelly Act](#) violation are trebled; and (3) allowing evidence during the liability portion of the trial of Miller's termination as a distributor of Stark's products. The second motion seeks an order reconsolidating the trial.

### Background

Miller was Stark's exclusive distributor in the Rochester area. John H. Black Co. was Stark's exclusive distributor in the Buffalo area, which includes the Albion Correctional Facility. This action is based on allegations that, after Miller was awarded the prison contract, it was pressured by Stark to relinquish the contract and to withdraw its bid so that, upon a rebidding, Black would be awarded the contract. Miller, fearful of losing its distributorship, cooperated with Stark on the condition that Black fix its price at \$ 109,000. Upon the rebidding, Miller then followed Stark's direction and submitted a bid six percent higher. After Black was awarded the contract, it demanded that Stark pay it \$ 4,000, representing the difference between Miller's [\*\*125] original bid and Black's subsequent bid. Stark made the payment to Black and then terminated Miller's distributorship, [\*\*\*3] allegedly because it blamed Miller for having to make the payment to Black. Miller claims damages arising from the loss of the contract and the termination of its distributorship.

Previously, it was determined by the Fourth Department that the action, as pleaded, alleges a [\*\*\*\*2] vertical price-fixing scheme that is a per se violation of the [Donnelly Act](#) (*Miller Brick Co. v Stark Ceramics*, 2 A.D.3d 1341, 1343, 770 N.Y.S.2d 235 [2003]; see [Business Elecs. Corp. v Sharp Elecs. Corp.](#), [485 U.S. 717, 735-736, 99 L. Ed. 2d 808, 108 S. Ct. 1515 \[1988\]](#)). The only remaining allegation of concerted action under the act involves a conspiracy between Miller, itself, and Stark,<sup>1</sup> distinguishing this case from [Monsanto Co. v Spray Rite Serv.](#) [[\\*1541 Corp. \(465 U.S. 752, 79 L. Ed. 2d 775, 104 S. Ct. 1464 \[1984\], reh denied 466 U.S. 994, 104 S. Ct. 2378, 80 L. Ed. 2d 850 \[1984\]\)](#)]. Although the only remaining allegation of concerted action involves Miller and Stark, there is an actionable wrong under the [Donnelly Act](#) because Miller alleges it was coerced to participate in the illicit scheme (see [Simpson v Union Oil Co. of Cal.](#), [377 U.S. 13, 12 L. Ed. 2d 98, 84 S. Ct. 1051 \[1964\], reh denied 377 U.S. 949, 84 S. Ct. 1349, 12 L. Ed. 2d 313 \[1964\]](#); [\*\*\*4] [Isaksen v Vermont Castings, Inc.](#), [825 F.2d 1158, 1162-1163 \[7th Cir 1987\]](#), cert denied 486 U.S. 1005, 100 L. Ed. 2d 193, 108 S. Ct. 1728 [1988]; [Ring v Spina](#), [148 F.2d 647 \[2d Cir 1945\]](#); [Rochez Bros., Inc. v North Am. Salt Co., Inc.](#), [1994 U.S. Dist. LEXIS 19421, \\*7, 1994 WL 735932, \\*3 \[US Dist Ct, WD Pa, Nov. 2, 1994\]](#)).<sup>2</sup> Moreover, [HN1](#) the "in pari delicto" defense is not applicable to private antitrust actions such as this (see [Perma Life Mufflers, Inc. v International Parts Corp.](#), [392 U.S. 134, 140, 20 L. Ed. 2d 982, 88 S. Ct. 1981 \[1968\]](#) overruled on other grounds by [Copperweld Corp. v Independence Tube Corp.](#), [467 U.S. 752, 765-766, 81 L. Ed. 2d 628, 104 S. Ct. 2731 \[1984\]](#); see also [Bindit Corp. v Inflight Adv.](#), [285 A.D.2d 309, 314, 731 N.Y.S.2d 43 \[2001\]](#)). A private antitrust action

<sup>1</sup> Although initially Black was named as a codefendant, in 1999 Black was granted summary judgment dismissing the action against it and thereafter the action was discontinued against Black.

<sup>2</sup> The [Donnelly Act](#) is "construed in light of Federal precedent and given a different interpretation only where State policy, differences in statutory language or the legislative history justify such a result" ([Anheuser-Busch, Inc. v Abrams](#), [71 N.Y.2d 327, 335, 520 N.E.2d 535, 525 N.Y.S.2d 816 \[1988\]](#); see [X.L.O. Concrete Corp. v Rivergate Corp.](#), [83 N.Y.2d 513, 518, 634 N.E.2d 158, 611 N.Y.S.2d 786 \[1994\]](#)).

"may be barred on the grounds of the plaintiff's own culpability only where (1) as a direct result of his own actions, the plaintiff bears at least substantially equal responsibility for the violations he seeks to redress, and (2) preclusion of suit would not significantly interfere with the effective enforcement of the [antitrust laws] and protection of the . . . public" ([Bateman Eichler, Hill Richards, Inc. v Berner, 472 U.S. 299, 310-311, 86 L. Ed. 2d 215, 105 S. Ct. 2622 \[1985\]](#)).

[\*\*\*5] Each of these holdings is explained below.

## [HN2](#)

### Vertical Restraint of Trade and Defendant's Monsanto Argument

In view of the implication in defendant's motion papers and its express position at oral argument that it will be entitled to a directed verdict at the end of plaintiff's case, and particularly in view of the court's remarks during oral argument that acceptance of defendant's *Monsanto* argument might indeed entitle it to judgment as a matter of law, the court [\*\*\*6] finds it necessary to elucidate the effect of the Appellate Division's decision that this is, [\*\*126] indeed, a vertical restraint of trade case, and to dispel any misconception. The following is also necessary to provide the [\*155] backdrop to the discretionary rulings below. [HN3](#) Restraints imposed by agreement between competitors are denominated as horizontal restraints while those imposed by agreement between firms at different levels of distribution are vertical restraints (see [Business Elecs. Corp. v Sharp Elecs. Corp., 485 U.S. 717, 730, 99 L. Ed. 2d 808, 108 S. Ct. 1515 \[1988\]](#)). It is beyond dispute that the alleged restraint in this case is vertical since it involves a restraint imposed by agreement between a supplier and a distributor.

Under the [Sherman Act](#), a vertical restraint of trade is not illegal per se unless it includes [\*\*\*3] some agreement on price or price levels ([485 U.S. at 735-736](#)). "Without an agreement as to a specific minimum price or price level, a vertical restraint is unlawful only if it fails a rule of reason analysis" ([Euromodas, Inc. v Zanella, Ltd., 368 F.3d 11, 21 \[1st Cir 2004\]](#)).

Commentary to the New York Pattern Jury Instructions suggests [\*\*\*7] that the rule is otherwise under the [Donnelly Act](#). The commentary clearly indicates that vertical price fixing is not a per se violation of the [Donnelly Act](#) but is subject to the rule of reason standard (2 NY PJI3d 532 [2005]). The cases cited in the comment, however, do not support that proposition. The issue in [Anheuser-Busch, Inc. v Abrams \(71 N.Y.2d 327, 520 N.E.2d 535, 525 N.Y.S.2d 816 \[1988\]\)](#) concerned the authority of the Attorney General under the [Donnelly Act](#) to investigate vertically imposed exclusive territorial dealerships ([71 N.Y.2d at 331](#)). The other case involved allegations of price discrimination, not price fixing ([State of New York v Mobil Oil Corp., 38 N.Y.2d 460, 463, 344 N.E.2d 357, 381 N.Y.S.2d 426 \[1976\]](#)).

In this case, there are allegations of vertical price fixing. When the matter was before the Fourth Department in December 2003, the issue was raised whether the per se standard or the rule of reason standard was applicable. The Fourth Department rejected defendant's contention that the rule of reason standard applied and held that "the per se standard is properly applied where, as here, price fixing is alleged" (2 A.D.3d 1341, 1343 [2003]). In support of that determination, the Court cited, [\*\*\*8] among other things, the United States Supreme Court's decision [Business Elecs.](#). Thus, it is the law of the case that this is a per se violation case arising under the [Donnelly Act](#).

### Concerted Action

[HN4](#) Neither the [Sherman Act](#) nor the [Donnelly Act](#) proscribe independent action (see [Monsanto Co. v Spray Rite Corp., 465 U.S. 752, 761, 79 L. Ed. 2d 775, 104 S. Ct. 1464 \[1984\]](#), *reh denied* 466 U.S. 994 [1984] [[Sherman Act](#)]; [State of New York v Mobil Oil Corp., 38 N.Y.2d 460, 464, 344 N.E.2d 357, 381 N.Y.S.2d 426 \[1976\]](#) ["a one-sided practice . . . is outside the scope of the [\*156] ([Donnelly Act](#)")]. [Section 1 of the Sherman Act](#) requires that there be a "contract, combination . . . or conspiracy" ([15 USC § 1](#)), while the [Donnelly Act](#) requires a "contract, agreement, arrangement or combination" ([General Business Law § 340 \[1\]](#)).

[1] In this case, summary judgment has been granted to Black dismissing the action against it. In its opposing papers here, defendant clearly implies that, under *Monsanto* and cases like it, plaintiff will not survive a motion for a directed verdict absent proof of an agreement between it and some other nonterminated distributor (such as Bock Brick Co. and Momack Building Materials) [\*\*\*9] to fix prices. Defendant, [\*\*127] however, misreads *Monsanto* in this regard.

In *Monsanto*, a terminated distributor brought an antitrust action against the manufacturer alleging that the manufacturer conspired with other distributors to fix prices. At trial, the plaintiff introduced evidence that it had been terminated by the defendant following complaints by other distributors regarding the plaintiff's price-cutting practices. On appeal from a verdict in favor of the plaintiff, the Seventh Circuit held that the evidence of the termination in response to the complaints was sufficient to raise an inference of concerted action, thus indicating "that an antitrust plaintiff can survive a motion for a directed verdict if it shows that a manufacturer terminated a price-cutting distributor in response to or following complaints by other distributors" ([465 U.S. at 759](#)). The Supreme Court disagreed, holding that such evidence alone is not sufficient to establish concerted action and that there must be additional "evidence that tends to exclude the possibility that the manufacturer and nonterminated distributors were acting independently" ([465 U.S. at 764](#)).

The present case is [\*\*\*10] different. There is no longer any allegation, as there was in [\*\*\*4] *Monsanto*, that defendant conspired with other distributors to fix prices. Plaintiff here, unlike the plaintiff in *Monsanto*, is alleging an illegal conspiracy between it and defendant to fix prices. Thus, while in *Monsanto* evidence of a conspiracy between the defendant and other distributors was critical to show concerted action, here it is not.

The fact that the only parties to the alleged illegal activity in this case are the plaintiff and the defendant does not preclude an action under the *Sherman Act*. HN5↑ It long has been held under the *Sherman Act* that "[t]here is actionable wrong whenever the restraint of trade or monopolistic practice has an impact on [\*157] the market; and it matters not that the complainant may be only one merchant" ([Simpson v United Oil Co. of Cal., 377 U.S. 13, 16, 12 L. Ed. 2d 98, 84 S. Ct. 1051 \[1964\]](#)). In *Simpson*, a retail gasoline dealer was required, by virtue of its lease and consignment agreement with its supplier, to sell gasoline at the price set by the supplier. When the retailer sold gas below the fixed price, the supplier refused to renew the retailer's lease [\*\*\*11] and terminated the consignment agreement. The retailer commenced an action under the *Sherman Act* against the supplier alleging that it had been economically coerced into the price-fixing scheme. The Supreme Court held that there was an actionable wrong under the *Sherman Act* and "[t]he fact that a retailer can refuse to deal does not give the supplier immunity if the arrangement is one of those schemes condemned by the antitrust laws" ([377 U.S. at 16](#); see [Ring v Spina, 148 F.2d 647 \[2d Cir 1945\]](#) [one constrained to enter into an illegal agreement under the *Sherman Act* by virtue of economic necessity is not precluded from recovering damages on ground that he himself was a participant in the unlawful combination]).

More recently, [Isaksen v Vermont Castings, Inc.](#)([825 F.2d 1158 \[7th Cir 1987, Posner, J.\]](#), cert denied 486 U.S. 1005, 100 L. Ed. 2d 193, 108 S. Ct. 1728 [1988]) held that it is of no moment under the *Sherman Act* that the only alleged concerted action involved the plaintiff and the defendant, since it was further alleged that the plaintiff was an involuntary participant ([825 F.2d at 1163](#)). The plaintiff in that case, like [\*\*\*12] here, was unable to allege that other distributors were involved in a conspiracy with the defendant. The Seventh Circuit, however, held that alleged concerted action involving the plaintiff "knuckling under to pressure [\*\*128] by [the defendant] to raise his prices" could satisfy the concerted action requirement of the *Sherman Act* ([825 F.2d at 1162](#)).

In another case, remarkably similar on its facts to the case at bar, a District Court held that the alleged "conspiracy between [the] plaintiff and . . . defendant may satisfy [the Sherman Act's] concerted action requirement" ([Rochez Bros., Inc. v North Am. Salt Co., Inc., 1994 U.S. Dist. LEXIS 19421, \\*7, 1994 WL 735932, \\*3 \[US Dist Ct, WD Pa, Nov. 2, 1994\]](#)). The plaintiff in that case, as here, alleged that it was coerced into submitting a noncompetitive bid for a public works project by implicit threats from its supplier. Moreover, like this case, the plaintiff alleged that, despite its compliance with defendant's order to bid noncompetitively, the defendant thereafter terminated its relationship with plaintiff.

[\*158] Since *Simpson*, the Supreme Court has rejected the application of the "in pari delicto" (of equal fault) defense in private antitrust actions [\*\*\*13] (*Perma Life Mufflers, Inc. v International Parts Corp.*, 392 U.S. 134, 140, 20 L. Ed. 2d 982, 88 S. Ct. 1981 [1968], overruled on other grounds by *Copperweld Corp. v Independence Tube Corp.*, 467 U.S. 752, 765-766, 81 L. Ed. 2d 628, 104 S. Ct. 2731 [1984]). The Court explained that HN6[<sup>1</sup>] preservation of the private antitrust action as "an ever-present threat to deter anyone contemplating business behavior in violation of the *antitrust law*" outweighed any inequities that might result should a culpable plaintiff recover a windfall gain (392 U.S. at 139). Indeed, the Court emphasized "'the inappropriateness of invoking broad common-law barriers to relief where a private suit serves important public [\*\*\*\*5] purposes'" (*Bateman Eichler, Hill Richards, Inc. v Berner*, 472 U.S. 299, 307, 86 L. Ed. 2d 215, 105 S. Ct. 2622 [1985], quoting 392 U.S. at 138). The Court, however, refused to decide whether "truly complete involvement and participation in a monopolistic scheme could ever be a basis, wholly apart from the idea of in pari delicto," to bar a plaintiff's cause of action (392 U.S. at 140). The Court appears to have answered that question in *Bateman*.

*Bateman* [\*\*\*14] arose in the context of a private action brought under the federal securities law. The Court clearly indicated, though, that the rule it announced in that case had broader application, including application to private antitrust actions. The Court held that:

"[A] private action for damages in these circumstances may be barred on the grounds of the plaintiff's own culpability only where (1) as a direct result of his own actions, the plaintiff bears at least substantially equal responsibility for the violations he seeks to redress, and (2) preclusion of suit would not significantly interfere with the effective enforcement of the [regulatory laws] and protection of the . . . public" (472 U.S. at 310-311).

Although the Second Department has held under *Perma Life* that a contracting defendant has standing to claim that its agreement violates the *Donnelly Act* (see *Bindit Corp. v Inflight Adv.*, 285 A.D.2d 309, 314, 731 N.Y.S.2d 43 [2001]), there are no reported cases specifically rejecting the in pari delicto defense, or adopting the standard set forth in *Bateman*, as a matter of state law. There appears to be no reason, however, why state antitrust cases should be treated [\*\*\*15] differently than federal antitrust cases in this regard (see *Anheuser-Busch*, 71 N.Y.2d at 335 [the *Donnelly Act* is "construed in light of Federal precedent and given a different [\*159] interpretation only where State policy, differences in statutory language or legislative history justify such a result"]).<sup>3</sup>

[\*\*129] With this background in mind, the court turns to the procedural history of the case, and plaintiff's motions.

#### Relevant Procedural History

In 1997, Miller brought a motion seeking, among other things, an order deeming the subject matter of a notice to admit dated May 2, 1997 to be established as true. The subject matter of the notice to admit was Stark's response to interrogatory No. 18 (c). In that interrogatory, Miller asked Stark to "[d]escribe the procedures which Miller . . . was supposed to follow with respect to the bidding on prison expansion projects both within and without its territory . . ." Stark responded:

"On the prison expansion project, [\*\*\*16] Stark distributors were permitted to bid if requested by the State, provided that such distributors included in their bids a factor for specification protection. A distributor who was granted an exclusive territory for a particular project would offer the product at the lowest bid price."

The court (Lunn, J.) denied the motion as it pertained to the notice to admit, indicating that because the responses to the interrogatories were verified and sworn as true, "[they] have already been admitted as true and may not be explained away at trial."

In November 1999, the court (Stander, J.) granted summary judgment to Stark and dismissed the second amended complaint against it. Upon reargument in May 2000, the court adhered to its earlier determination and again dismissed the second amended complaint against Stark. On appeal, however, the Fourth Department held that

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<sup>3</sup> See below, on motion for reargument.

there are triable issues of fact whether there was a violation of the *Donnelly Act* by Stark and thus that it was error to grant [\*\*\*\*6] Stark summary judgment (281 A.D.2d 960, 961, 722 N.Y.S.2d 679 [2001]).

In May 2002, as relevant here, the court (Stander, J.) bifurcated the trial at the request of Stark<sup>4</sup> and precluded Miller, during [\*\*\*17] the liability phase of the trial, from presenting evidence [\*160] of its termination as a distributor of Stark's products. Miller appealed but failed to brief the issue whether the court properly bifurcated the trial. The Fourth Department affirmed, holding that the part of the order dealing with the admissibility of evidence was not appealable and that Miller abandoned the bifurcation issue by not briefing it (*Miller Brick*, 2 A.D.3d at 1343).

### Present Motions

More than a year later, in September 2004, Miller brought the first [\*\*\*18] of the two motions now before the court. Miller contends that, by virtue of Justice Lunn's decision in 1997, it "is entitled to a motion in limine prohibiting [Stark] from introducing any evidence, or argument, the purpose of which is to explain away its response to interrogatory No. 18 (c)." Miller further contends, citing *HBE Leasing Corp. v Frank* (22 F.3d 41, 46 [2d Cir 1994]), that it is improper to inform a jury that damages for a *Donnelly Act* violation are trebled and thus "[Stark], or its attorneys . . . [should be precluded] from making any such reference during the course of the trial." Finally, Miller contends that, notwithstanding the previous order of the court (Stander, J.), it should be permitted to introduce evidence of its termination as [\*130] a distributor during the liability portion of the trial. In support of that contention, Miller cites its belief that the prior order bifurcated only the amount of damages from the fact of damage, and argues that the fact of damage is a necessary element of liability. Miller further argues that Stark's pretextual reasons for the termination are circumstantial evidence of an alleged agreement between Stark and its [\*\*\*19] other distributors to restrain trade.

Stark opposes the motion and cross-moves for costs. In its opposing papers dated January 3, 2005, Stark contends that the motion should be denied in its entirety because it is untimely in light of a scheduling order by Stander in May 2001. Stark also contends that the motion, insofar as it seeks reargument of that part of the May 2002 order limiting evidence during the liability portion of the trial, is untimely (see *CPLR 2221 (d)*). In the alternative, Stark opposes reargument because Miller's "understanding of bifurcation orders does not serve a cognizable basis for reargument" and because the claimed relevance of the evidence of the termination is spurious inasmuch as there are no [\*161] other alleged coconspirators. Stark additionally contends that, while it may not deny its response to interrogatory No. 18 (c), it may "offer proof to put the admission in context with other proof" and to explain its meaning. Finally, Stark asks this court to ignore federal law on the treble damages issue and to reexamine that issue in light of state law, as a court has done in another context in New Jersey (see *Wanetick v Gateway Mitsubishi*, 163 F.3d 71 N.J. 484, 494-495, 750 A.2d 79 [2000] [\*\*\*20] [there is "no compelling policy reason to justify shielding jurors from the consequences of their own actions in the jury box"]).

In the second of the two motions, dated January 13, 2005, Miller seeks an order "reconsolidating the trial of this action." Miller contends that it has become apparent since the prior order of the court that "bifurcation is unworkable . . . [because] the issues as to the existence of an agreement, the causation between any agreement and damages, and the amount of such damages, are inextricably intertwined in this case." Miller further contends that reconsolidation serves the interest of judicial economy because many of the witnesses in the two trials will be the same.

After receipt by the court of the second motion, Stark submitted supplemental papers dated January 15, 2005 more fully explaining its opposition to the first motion and indicating that, "in the event [Miller] does seek to reargue the motion with respect to bifurcation, it is respectfully requested that [Stark] be permitted an opportunity to fully respond to plaintiff's allegations and argument." In its supplemental papers, Stark contends that proof of the termination is irrelevant [\*\*\*21] and immaterial to the conspiracy alleged to have occurred months before April 1991

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<sup>4</sup> Stark contended that "the issues of damages and liability are completely unrelated. The existence of a price-fixing conspiracy has no bearing on the measure of damages purportedly sustained by [Miller] after its termination as a . . . distributor." According to Stark, bifurcation would "further judicial economy, promote juror understanding of the issues, and require shorter and less encompassing closing arguments and jury charges." Miller did not oppose bifurcation.

and that, in any event, such proof is inadmissible as a matter of law under [Monsanto](#) in the absence of proof that a nonterminated distributor participated in the alleged conspiracy. Finally, although conditionally requesting additional time to address the reconsolidation issue, Stark contends that bifurcation was proper because the issues of fact identified by the Fourth Department in its decision on summary judgment are separate and distinct from the issue of damages.

### Discussion

Initially, the court rejects Stark's contention that the prior scheduling order has any preclusive effect. [HN7](#)[] This court has the inherent authority to control its own calendar provided that it does not exercise that discretion in a manner that conflicts with [\*162] an existing legislative command [\*\*131] (see [Matter of Attorney Gen. of State of N.Y. v Firetow](#), 94 N.Y.2d 477, 490-491, 727 N.E.2d 1220, 706 N.Y.S.2d 666 [2000]; [People v Mezon](#), 80 N.Y.2d 155, 158-159, 603 N.E.2d 943, 589 N.Y.S.2d 838 [1992]). That control is authorized whether the trial justice is the original justice assigned to the case or, as here, the justice substituted for the original presiding justice [\*\*\*22] (see [Matter of Public Adm'r of County of N.Y. v Cohen](#), 221 A.D.2d 297, 298, 634 N.Y.S.2d 106 [1995]; see also [Wahrhaftig v Space Design Group](#), 33 A.D.2d 953, 306 N.Y.S.2d 863 [1970]).

Turning to the substance of the motions, the court grants that part of the first motion seeking an order prohibiting Stark from "explaining away" its verified response to interrogatory No. 18 (c) but only insofar as prohibiting Stark from denying the substance of that response. [HN8](#)[] It is well settled that the response to an interrogatory is admissible as an admission of the respondent (see [United Bank v Cambridge Sporting Goods Corp.](#), 41 N.Y.2d 254, 264, 360 N.E.2d 943, 392 N.Y.S.2d 265 [1976], rearg denied 41 N.Y.2d 901 [1977]; [Smith v Kuhn](#), 221 A.D.2d 620, 621, 634 N.Y.S.2d 167 [1995]; [Bigelow v Acands](#), 196 A.D.2d 436, 439, 601 N.Y.S.2d 478 [1993]). By virtue of the verification, as the court (Lunn, J.) previously indicated, Stark cannot deny the substance of its response to interrogatory No. 18 (c). However, because a response to an interrogatory is not a formal judicial admission, Stark's response to interrogatory No. 18 (c) is not binding and may be explained (see Connors, Practice Commentaries, McKinney's Cons Laws of NY, Book 7B, CPLR C3131:1, at 615 [2005 ed]; [\*\*\*23] see also [Ando v Woodberry](#), 8 N.Y.2d 165, 171, 168 N.E.2d 520, 203 N.Y.S.2d 74 [1960]; [Ferris v Sterling](#), 214 N.Y. 249, 108 N.E. 406 [1915]; [Chamberlain v Iba](#), 181 N.Y. 486, 492, 74 N.E. 481 [1905]; [Kirby v Monroe No. 1 Bd. of Coop. Educ. Servs.](#), 2 A.D.3d 1387, 1388, 769 N.Y.S.2d 670 [2003]; Prince, Richardson on Evidence § 8-211, at 520 [Farrell [\*\*\*\*8] 11th ed]). It will be for the trier of fact to determine the weight of the evidence in light of any explanation offered by Stark (see [Ando](#), 8 N.Y.2d at 171; Prince § 8-212, at 520-521).

[2] Additionally, the court agrees with Miller that it is improper to inform a jury that damages for a [Donnelly Act](#) violation are trebled. [HN9](#)[] The [Donnelly Act](#), like the [Sherman Act](#) upon which it is modeled, requires the trebling of the damage award (see [15 USC § 15](#); [General Business Law § 340](#) [5]). The weight of federal authority prohibits any mention of the trebling requirement to the jury (see [HBE Leasing](#), 22 F.3d at 46) because "[r]eference to treble damages and attorneys['] fees is irrelevant to the jury questions of liability and damages and may tend to confuse or prejudice a jury into reducing [\*\*\*24] its eventual award, thus frustrating Congress's goal of deterring improper [\*163] conduct by assessing treble damages and attorneys['] fees." (*Id. at 45*) Under the pattern jury instructions given in antitrust cases under the [Sherman Act](#) (3A Fed Jury Prac & Instructions § 150.93 [5th ed]), and antitrust cases under the [Donnelly Act](#) (PJI3d P3:58 [2004]), no mention is made of the trebling requirement. Although the court can find no cases discussing this issue under the [Donnelly Act](#), the court agrees with the rationale of the federal courts that have examined the issue ([Anheuser-Busch](#), 71 N.Y.2d at 335; see [X.L.O. Concrete](#), 83 N.Y.2d at 518). [Wanetick](#), which is cited by Stark, arises under a New Jersey consumer fraud law and is not persuasive. The court therefore grants that part of the first motion seeking an order prohibiting Stark from advising the jury that damages for a Donnelly Act violation are trebled.

[\*\*132] Next, the court examines the issue of reconsolidation. Given that the previous order of the court (Stander, J.) bifurcating the trial was entered without objection (see [Response of Carolina, Inc. v Leasco Response, Inc.](#), 537 F.2d 1307, 1324 [5th Cir 1976]), [\*\*\*25] and further, that no appeal from that order was perfected, and given the implications of effectively overruling the action of the prior justice (see [Velasquez v C.F.T., Inc.](#), 267 A.D.2d 229, 699 N.Y.S.2d 470 [1999]; [Dawson v Pavarini Constr. Co.](#), 228 A.D.2d 468, 644 N.Y.S.2d 288 [1996]; [Padela v](#)

9 Misc. 3d 151, \*163L<sup>801</sup> N.Y.S.2d 120, \*\*132L<sup>2005</sup> N.Y. Misc. LEXIS 1163, \*\*\*25L<sup>2005</sup> NY Slip Op 25226, \*\*\*\*8

Rosen & Weidberg, 200 A.D.2d 722, 607 N.Y.S.2d 89 [1994]; *Carel Almo Serv. v Weisskopf*, 42 A.D.2d 953, 348 N.Y.S.2d 557 [1973]), the court denies Miller's motion for reconsolidation. Nevertheless, the court recognizes that [HN10](#) "[t]o be 'liable' under the antitrust laws . . . means that one has violated the antitrust laws and that violation has resulted in an injury to the business or property of the plaintiff, i.e., there was fact of damage" ([Response, 537 F.2d at 1320](#); see [Danny Kresky Enters. Corp. v Magid, 716 F.2d 206, 209-210 \[3d Cir 1983\]](#)). Stated another way, to establish liability, "a plaintiff must prove the existence of 'antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful'" ([Atlantic Richfield Co. v USA Petroleum Co., 495 U.S. 328, 334, 109 L. Ed. 2d 333, 110 S. Ct. 1884 \[1990\]](#) [\*\*\*26] quoting [Brunswick Corp. v Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 \[1977\]](#); see [J. Truett Payne Co., Inc. v Chrysler Motors Corp., 451 U.S. 557, 562, 68 L. Ed. 2d 442, 101 S. Ct. 1923 \[1981\]](#) ["a plaintiff must make some showing of actual injury attributable to something the antitrust laws were designed to prevent"]). Indeed, it is well established that a "treble-damage plaintiff may not recover for losses due to factors other than the defendant's [antitrust] violations" ([Amerinet, Inc. v Xerox Corp., 972 F.2d 1483, 1494 \[8th Cir 1992\]](#), cert denied 506 U.S. 1080, 122 L. Ed. 2d 356, 113 S. Ct. 1048 [1993]). Thus, when an antitrust case has been bifurcated for trial, as this one has been, the plaintiff must establish during the liability portion of the trial that "the violation caused him injury" ([Response, 537 F.2d at 1321](#)). This is true even in cases involving alleged per se violations, as here ([Atlantic, 495 U.S. at 341-345](#)). The court therefore agrees with Miller's contention that the "fact of damage," i.e., whether Miller sustained an antitrust injury, is an issue that must be litigated [\*\*\*27] during the liability portion of [\*\*\*\*9] the trial.<sup>5</sup>

The previous order of the court (Stander, J.) merely indicated that the trial would be bifurcated "on the issues of liability and damages." It did not address the issue, now before the court, regarding Miller's burden of proof during the first phase of the trial. Thus, the previous order of the court is not the law of the case on that issue.

[3] In view of the foregoing, the court reconsiders the issue of the admissibility of evidence of the termination during the liability portion of the trial. [HN11](#) The previous determination of the court (Stander, J.) on that issue was advisory only (see *Miller Brick*, 2 A.D.3d at 1343) and thus subject [\*\*\*28] to revision upon changed circumstances (see [CPLR 2221 \(e\) \(2\)](#)). Because the court now concludes that an antitrust injury is an element [\*\*133] that must be proven during the liability portion of the trial, it is self-evident that evidence of the termination is admissible during the first phase of this trial, if for no other reason than, to show an antitrust injury.<sup>6</sup> The court rejects Stark's contention that the time period set forth in [CPLR 2221 \(d\) \(3\)](#) is applicable here to Miller's motion. The court further rejects Stark's contention that evidence of the termination is inadmissible as a matter of law under [Monsanto](#). (See discussion above.) The court therefore grants that part of the first motion seeking an order allowing evidence during the liability portion of the trial of Miller's termination as a distributor of Stark's products.

[\*\*\*29] Finally, the court denies Stark's cross motion for costs.

#### [\\*165 On Motion for Reargument](#)

Defendant Stark Ceramics moves for reargument of a prior motion, and upon reargument, for an order in limine precluding plaintiff, George C. Miller Brick Company, from adducing proof of a resale price maintenance agreement between it and Stark because such would not establish a violation of the [Donnelly Act](#). Stark also moves for reargument of the prior motion in limine to prevent plaintiff from adducing proof of "antitrust injury" in the liability phase of the trial, consisting of evidence that Stark terminated Miller Brick's distributorship in retaliation for having to pay another distributor, Black Brick, \$ 4,000, representing the difference between Miller Brick's original bid and Black Brick's subsequent bid for the Albion Correctional Facility project. Stark further moves in limine to preclude plaintiff from offering any evidence at trial of the participation of another distributor, and the eventual bid winner on

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<sup>5</sup> Assuming that the trier of fact returns a verdict in favor of Miller during the liability portion of the trial, it will then be Miller's burden of proof during the damage portion of the trial to show "the amount of damages" (see [Rossi v Standard Roofing, Inc., 156 F.3d 452, 484 \[3d Cir 1998\]](#)).

<sup>6</sup> Even under the previous order of the court, it was recognized that evidence of the termination was relevant on the issue of damages.

the Albion prison project, Black Brick, in the allegedly [\*\*\*\*10] illegal bid-rigging scheme, and to preclude plaintiff from offering similar evidence of alleged [\*\*\*30] participation by Momack Building Materials in the alleged conspiracy. Finally, Stark moves to preclude plaintiff from offering hearsay statements of Stark, Black Brick, Momack, or other distributors regarding the existence purpose or scope of alleged conspiracy. The background was provided in the court's prior decision, familiarity with which is assumed.

The cornerstone of Stark's current motion is its argument, raised for the first time in this litigation, that, unlike the Sherman Act (*Dr. Miles Med. Co. v. John D. Park & Sons Co.*, 220 U.S. 373, 55 L. Ed. 502, 31 S. Ct. 376 [1911]), the Donnelly Act does not proscribe a vertical agreement establishing the minimum price at which a distributor may resell products purchased from its supplier. (*Park & Sons Co. v. National Wholesale Druggists' Assn.*, 175 N.Y. 1, 67 N.E. 136 [1903]; *Walsh v. Dwight*, 40 A.D. 513, 58 N.Y.S. 91 [2d Dept 1899]; see also, *Dawn to Dusk v. Brunckhorst Co.*, 23 A.D.2d 780, 781, 258 N.Y.S.2d 746 [2d Dept 1965] ["Nor is it violative of the statute because it fixes the . . . price to his customers and prohibits the distribution of the goods to any dealers who would [\*\*\*31] resell the goods to plaintiff"]; *Port Chester Wine & Liq. Shop v. Miller Brothers Fruiterers*, 253 A.D. 188, 194, 1 N.Y.S.2d 802 [2d Dept 1938] [the Donnelly Act "did not purport to concern itself with vertical price-fixing arrangements based on property rights in good will evidence by a trade name, brand or mark on a commodity in intrastate commerce"]; [\*\*134] *Marsich v. Eastman Kodak Co.*, 244 A.D. 295, 279 N.Y.S. 140 [2d Dept 1935], affd without op *269 N.Y. 621, 200 N.E. 27* [1936]; *Locker v. American Tobacco* [\*166] Co., 121 A.D. 443, 106 N.Y.S. 115 [2d Dept 1907], affd *195 N.Y. 565, 88 N.E. 289* [1909] ["producer may lawfully sell or refuse to sell to any person; may establish the sales price and terms of sale of its products, and what it may lawfully do itself it may lawfully delegate to another, and the exercise of such delegated power by the other is as lawful as if exercised by the producer itself"].)

Stark contends that this so-called New York rule is the more enlightened rule, the federal rule under the Sherman Act under the Dr. Miles Med. Co. case having been largely discredited by the courts *Isaksen v. Vermont Castings, Inc.*, 825 F.2d 1158, 1161-1162 [7th Cir 1987, Posner, J.], [\*\*\*32] cert denied 486 U.S. 1005, 100 L. Ed. 2d 193 [1988], and commentators (Robert Bork, *The Antitrust Paradox*, at 33, 289 [1978]). Thus, Stark contends that the court's previous reliance on *Anheuser Busch, Inc. v. Abrams* (71 N.Y.2d 327, 520 N.E.2d 535, 525 N.Y.S.2d 816 [1988]), for the proposition that the Donnelly Act "should generally be construed in light of Federal precedent and given a different interpretation only where State policy, differences in the statutory language or the legislative history justifies such a result" (*id.*, 71 N.Y.2d at 335, is misplaced to the extent it was employed to uphold the viability of plaintiff's allegations of [\*\*\*\*11] concerted action in this case. Stark contends that Dr. Miles is in direct conflict with over a century's jurisprudence in New York which has, according to Stark, held:

"(i) that retail price maintenance agreements pose no threat whatsoever to the competitive process that the Donnelly Act and prior state anti-trust laws were enacted to protect; and (ii) accordingly, that such laws are not intended to and do not regulate such resale price maintenance agreements in any way." (Stark's mem [\*\*\*33] of law at 8.)

Because Stark seeks an order declaring that

"the allegations of George C. Miller Brick Company, Inc. ('Miller Brick') of resale price maintenance do not establish a violation of the Donnelly Act [,] and [further] precluding Miller Brick from offering proof of 'antitrust injury' in the liability phase, including evidence of Stark Ceramics' termination of the distribution agreement with Miller Brick,"

9 Misc. 3d 151, \*166 A.2d 801 N.Y.S.2d 120, \*\*134 A.2d 2005 N.Y. Misc. LEXIS 1163, \*\*\*33 A.2d 2005 NY Slip Op 25226, \*\*\*\*11

plaintiff describes the motion as, in essence, one for summary judgment, which is both procedurally improper in form and untimely under the CPLR. In this, plaintiff is correct. In [Scalp & Blade v. Advest, Inc. \(309 A.D.2d 219, 765 N.Y.S.2d 92 \[4th Dept 2003\]\)](#), the Court held that a motion of this type "has a concretely restrictive [\*167] effect on the efforts of plaintiffs to prove their case against defendants and recover certain damages from them." [Id. at 224.](#)) [HN12](#)

"the order does not merely limit the production of certain evidence . . . , but rather effectively grants defendants partial summary judgment on the critical substantive issue of what constitutes . . . plaintiffs' causes of action[.] . . . defendants' motion, although labeled [\*\*\*34] one in limine, actually 'was the functional equivalent of a motion for partial summary judgment dismissing the complaint' " [id.](#), quoting [Rondout Elec. v. Dover Union Free School Dist., 304 A.D.2d 808, 810-811, 758 N.Y.S.2d 394 \[2d Dept 2003\]](#).

The court agrees with plaintiff that, if the requested order was issued, it would require outright dismissal of the complaint, and therefore defendant's motion is, in reality, in the nature of one for summary judgment. [HN13](#) Such a motion is precluded at this stage of the proceedings [\*\*\*135] because it was filed more than 120 days after the note of issue was filed. [Brill v. City of New York, 2 N.Y.3d 648, 814 N.E.2d 431, 781 N.Y.S.2d 261 \[2004\]; Clermont v. Hillsdale Indus., 6 A.D.3d 376, 378, 773 N.Y.S.2d 901 \[2d Dept 2004\].](#)

Additionally, Stark's current position with respect to the legality of the arrangements at issue in this case, conceived and proffered to the court for the first time on the eve of trial in this nearly 10-year-old case, is barred by two prior Appellate Division decisions which have established the law of the case. In 2001, the Appellate Division reinstated the complaint against Stark on the ground that [\*\*\*35] "the distribution agreement, a letter from defendant's representative to the distributors, and the deposition testimony of the parties raise issues of fact concerning how and [\*\*\*12] when the distributors could bid on projects outside their territories and whether distributors were intended to bid, if at all, on the State project." (*Miller Brick Co. v. Stark Ceramics*, 281 A.D.2d 960, 961, 722 N.Y.S.2d 679 [4th Dept 2001].) Thereafter, in 2003, the Appellate Division reversed my predecessor's decision to apply the rule of reason standard, finding that the complaint, as "limited [in] its theory of liability to a violation of the [Donnelly Act](#) based on bid rigging and price fixing," involves the application of "the per se standard" because "price fixing is alleged." (2 A.D.3d at 1341 [4th Dept. 2003].) On both appeals, defendant urged the Appellate Division to uphold the rulings of the court below on the ground that the distribution agreements involved in the case in no way violated the antitrust laws of the State of New York. (See 281 A.D.2d 960 [2001] [defendants/respondents' [\*168] brief (at 9) maintaining that the core of the illegal [\*\*\*36] agreement alleged by plaintiffs instead "was entirely in accord with the terms of the Distribution Agreement and Bulletins"--thus, the only acts taken by Stark Ceramics in relation to the New York State Prison Expansion Program were to enforce the terms of its distributorship agreement, resolve conflicts between distributors, and to ultimately terminate Miller Brick pursuant to the terms set forth in the Distribution Agreement".] ) Moreover, in *Miller Brick* (2 A.D.3d 1341 [2003] [brief on behalf of Stark Ceramics, Inc., at 14]), Stark presented the exact same argument that it presented originally on the motion now sought to be reargued: "However, in order for a manufacturer's termination of a distributor to fall within the category of per se illegal restraints (sic), the termination must have been pursuant to a minimum price fixing agreement with at least one other non-terminated distributor." This is, indeed, the same *Monsanto* argument rejected by the undersigned in its decision and order earlier this year, and was therefore fully rejected also by the Appellate Division in 2003. Implicit in these determinations was a corollary decision that the cases now cited by defendant [\*\*\*37] do not preclude relief on the remaining cause of action to be tried in this case. Accordingly, the determinations by the Appellate Division on each of the indicated appeals is law of the case, thereby requiring denial of Stark's current motion.

On the merits, however, the [Anheuser-Busch](#) case is precisely on point, in that it rejected the very argument defendant now makes for the first time in this litigation that vertical restraint agreements are legal in this state. In that case, the targets of a grand jury investigation moved to quash a subpoena issued by the Attorney General

9 Misc. 3d 151, \*168L<sup>1</sup> 801 N.Y.S.2d 120, \*\*135L<sup>2</sup> 2005 N.Y. Misc. LEXIS 1163, \*\*\*37L<sup>3</sup> 2005 NY Slip Op 25226, \*\*\*\*12

pursuant to an investigation into marketing practices in the beer industry alleged to violate the [Donnelly Act](#). As defendant now maintains on this [\*\*136] motion to reargue, the targets of the subpoenas maintained that the [\*\*\*\*13] vertical territorial and other arrangements at issue in that case were per se legal and that such legality was "established by 'seven decades of unanimous precedent' and that the Legislature has acquiesced in such an interpretation of the [Donnelly Act](#) by failing to amend the statute to overrule those decisions." ([71 N.Y.2d at 333](#).) The cases relied on by [\*\*\*38] the grand jury targets referred to above ([71 N.Y.2d at 330](#) [Points of Counsel]), and Judge Bellacosa as the lone dissenter ([71 N.Y.2d at 336-339](#)), are the cases Stark now relies upon in its motion for reargument and reconsideration. The majority opinion

[\*169] "conclude[d], however, that the cases cited by petitioners do not conclusively establish, either singly or in combination, a rule of per se legality for vertical territorial arrangements[,] [n]or does the statutory language foreclose the Attorney-General's position that such arrangements, if shown to result in an unreasonable restraint of trade under the circumstances, are prohibited." ([71 N.Y.2d at 333](#))

This case involves much more than a simple vertical territorial arrangement, although plaintiff clearly alleges that such a vertical territorial arrangement existed. In addition, plaintiff alleges that the territorial arrangement included a key element of price fixing and that such price fixing was enforced by enforced bid rigging and, in addition, termination of a distributor who not only bid outside its territory but undercut the distributor assigned to that territory. Plaintiff [\*\*\*39] claims to be the victim of the scheme after having been forced by Stark to agree to it. As the Court of Appeals has held, the [Donnelly Act](#) reaches such conduct even if the conspiracy is wholly vertical, i.e., supplier/manufacturer and distributor. ([Creative Trading Co. v. Larkin-Pluznick-Larkin, Inc., 148 A.D.2d 352, 354-357, 356, 539 N.Y.S.2d 1 \[1st Dept 1989\]](#) Sullivan, J., dissenting], revd on dissenting op below [75 N.Y.2d 830, 551 N.E.2d 1236, 552 N.Y.S.2d 558 \[1990\]HN14](#)<sup>1</sup> [the [Donnelly Act](#) reaches "competing distributors who conspire among themselves and with a supplier to terminate a fellow distributor for selling at a discount" (emphasis supplied)], citing [United States v. General Motors Corp., 384 U.S. 127, 86 S. Ct. 1321, 16 L. Ed. 2d 415 \[1966\]](#); see also, [Bedell Wholesale Co. v. Philip Morris, 272 A.D.2d 854, 708 N.Y.S.2d 226 \[4th Dept 2000\]](#) [noted in 103 NY Jur. 2d, Trade Regulation § 19, 2003 Cum Supp, at 70, which cited [Creative Trading Co. v. Larkin-Pluznick-Larkin, Inc. \(supra\)](#), and involved a vertical restraint with no horizontal components]). Even the leading New York treatise on the subject acknowledges that the [\*\*\*40] [Donnelly Act](#) would apply in these circumstances, although the author speculates that the Court of Appeals might prefer a rule of reason standard to the per se standard in light of the cases cited by Stark. (Robert L. Haig, Commercial Litigation in the New York State Courts § 79:20, at 1267-1268 [4-A West's NY Prac Series 2005].) In this case, the 2003 Appellate Division decision forecloses any argument on that score.

[\*\*\*\*14] And even that does not describe the end of plaintiff's allegations in this case. Ultimately, this is not solely a "resale price maintenance" case of the kind upheld by the cited New York decisions under the [Donnelly Act](#). As pointed out in plaintiff's [\*170] memorandum of law, [HN15](#)<sup>1</sup> resale price maintenance cases "typically describe those situations where a manufacturer specifies a minimum price list for its product line and prohibits its distributors from underselling one another by lower than that price." *Id.* at 6-7 n 3.) According to plaintiff, "Stark [\*\*137] did not have a 'resale price maintenance' policy in the traditional sense[;][i]nstead, Stark had a bid rigging policy that fixed the price for prison expansion project sales at a certain level," and a termination policy when one [\*\*\*41] distributor, i.e., plaintiff, attempted to undersell (i.e., underbid) on a project. Accordingly, if plaintiff proves its case, defendant will be found guilty of bid rigging under the [Donnelly Act](#). (Cf., [People v. Schwartz, 160 A.D.2d 964, 554 N.Y.S.2d 686 \[2d Dept 1990\]](#).)

Finally, Stark's contention that the doctrine of collateral estoppel precludes it from proving that Black Brick and Momack participated in the alleged illegal scheme is without merit. First, the dismissal of Black Brick from the complaint does not create a preclusion except insofar as Black Brick's potential liability to plaintiff is concerned. Plaintiff's purpose in proving the circumstances surrounding Black Brick's ultimate award of the bid in question, and the participation of Momack, is not for the purpose of establishing their liability. Rather, such evidence is adduced for the purpose of showing that Stark was part of the conspiracy with plaintiff, one of its many New York distributors. Such evidence, under the theory pursued by plaintiff, described in the Appellate Division decisions and this court's February decision and order in this case, will not require any special interrogatories to the jury as to [\*\*\*42] their

participation. The only question the jury will be asked to answer is whether Stark participated with the plaintiff in the alleged scheme, and they may surely consider on relevancy grounds Stark's contemporaneous arrangements with other similarly situated distributors in upstate New York in making that determination. Thus, as plaintiff contends, the issue is not one of issue preclusion under the collateral estoppel doctrine, but whether, as law of the case, Black Brick's dismissal from the complaint, which went unappealed, can preclude plaintiff's effort to show that defendant was part of a conspiracy with it by reference to evidence that other distributors similarly situated, except as to territory, had a similar arrangement. Nothing in the law of the case doctrine [**\*171**] directs a court to preclude the [\*\*\*\*15] proffered evidence, and, accordingly, the motion is denied.<sup>7</sup>

[\*\*\*43] The balance of defendant's motion seeking preclusion of hearsay evidence is denied inasmuch as there is no specification of what is sought to be excluded.

#### Conclusion

Defendant's motion is denied in its entirety.

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<sup>7</sup> Stark's current position is ironic, given that it argued on the original motion that the charged conspiracy between it and plaintiff could not be shown under *Monsanto* absent proof that defendant also agreed on similar terms with its other nonterminated distributors. That motion proceeded, and was decided, on the assumption that plaintiff had no other proof of the agreement between it and Stark. This motion was brought in response to plaintiff's assurances after the court's decision that, indeed, it had such other proof.

The court also rejects Stark's argument that it had insufficient discovery of such proof. Plaintiff provided interrogatory answers identifying the "other distributors" as having been involved in the conspiracy and, in any event, it is no secret who Stark's upstate distributors were and their respective territories.

## **TXU Generation Co., L.P. v. PUC of Tex.**

Court of Appeals of Texas, Third District, Austin

May 19, 2005, Filed

NO. 03-04-00148-CV

**Reporter**

165 S.W.3d 821 \*; 2005 Tex. App. LEXIS 3771 \*\*

TXU Generation Company, L.P.; TXU Portfolio Management Company, L.P.; Oncor Electric Delivery Company; Coalition of Wholesale Electric Market Participants; Occidental Chemical Corporation; Occidental Permian, Ltd.; Occidental Power Marketing, L.P.; Occidental Power Services, Inc.; Oxy Vinyls, L.P.; Ingleside Cogeneration, L.P.; and Coral Power, L.L.C., Appellants v. Public Utility Commission of Texas, Appellee

**Subsequent History:** Petition for review denied by [TXU Generation Co. LP v. PUC of Tex., 2006 Tex. LEXIS 1091 \(Tex., Oct. 27, 2006\)](#)

**Prior History:** [\[\\*\\*1\]](#) DIRECT APPEAL FROM THE PUBLIC UTILITY COMMISSION OF TEXAS.

**Disposition:** Affirmed.

## **Core Terms**

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electricity, market power, reliability, WMO Rule, priced, wholesale market, market participant, withholding, wholesale, prohibited activity, transmission, ancillary services, intent element, generation, provisions, regulation, consumer, notice, statutory authority, vagueness, practices, unconstitutionally vague, electric power, manipulation, contends, preamble, markets, marginal cost, customer, overrule

## **LexisNexis® Headnotes**

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Administrative Law > Governmental Information > Recordkeeping & Reporting

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Transportation Law > Interstate Commerce > Market Participant Doctrine

## **[HN1](#) [down arrow] Governmental Information, Recordkeeping & Reporting**

The Wholesale Market Oversight Rule (WMO Rule), [16 Tex. Admin. Code § 25.503](#), addresses the oversight of the Public Utility Commission of Texas of the wholesale market by enumerating the duties of market participants and defining prohibited activities. [16 Tex. Admin. Code § 25.503\(f\), \(g\)](#). The rule provides a defense to a market

participant who engages in a prohibited activity if the participant demonstrates that the otherwise prohibited activity served a legitimate business purpose and that its adverse effects were not foreseeable. [16 Tex. Admin. Code § 25.503\(h\)](#). The rule defines the role of the Electric Reliability Council of Texas (ERCOT) in enforcing operating standards for market participants and establishes a process for market participants to clarify ERCOT protocols to ensure compliance. [16 Tex. Admin. Code § 25.503\(i\), \(l\)](#). Finally, the rule establishes record-keeping requirements for market participants and ERCOT, and details the Commission's investigation process. [16 Tex. Admin. Code § 25.503\(k\), \(l\)](#).

Administrative Law > Separation of Powers > Constitutional Controls > General Overview

Energy & Utilities Law > Administrative Proceedings > Judicial Review > General Overview

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Administrative Law > ... > Constitutional Controls > Authority to Adjudicate > Validity of Legislation

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > ... > Public Utility Commissions > Hearings & Orders > Judicial Review

Energy & Utilities Law > Utility Companies > General Overview

Governments > Agriculture & Food > General Overview

## [HN2](#) Separation of Powers, Constitutional Controls

In a direct appeal of a Public Utility Commission of Texas rule pursuant to [§ 39.001\(e\)](#) of the Public Utilities Regulation Act, the court of appeals is limited to reviewing the rule's validity. [Tex. Util. Code. Ann. § 39.001\(f\)](#) (Supp. 2004-2005). A validity challenge tests a rule on procedural and constitutional grounds. A validity challenge may also question the agency's statutory authority to promulgate the rule. An agency rule is presumed valid, and the challenging party bears the burden to demonstrate its invalidity.

Business & Corporate Law > ... > Actual Authority > Implied Authority > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Business & Corporate Law > ... > Authority to Act > Actual Authority > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

## [HN3](#) Actual Authority, Implied Authority

The Public Utility Commission of Texas is a creature of the legislature and has no inherent authority. It may exercise only those specific powers that the law confers upon it in clear and express language. As a general rule, the legislature impliedly intends that the agency should have whatever power is reasonably necessary to fulfill a function or perform a duty that the legislature has expressly placed in the agency. Absent specific or implied statutory authority, an agency rule is void because it is made without legal authority.

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

#### **HN4** Agency Rulemaking, Rule Application & Interpretation

The Public Utility Commission of Texas may not exercise what is effectively a new power or a power contradictory to the statute based merely on a claim that the power is expedient for administrative purposes. Although a rule must comport with the Commission's authorizing statute, the legislature does not need to include every specific detail or anticipate all unforeseen circumstances. To establish a rule's facial invalidity, the challengers must show that the rule: (1) contravenes specific statutory language; (2) runs counter to the general objectives of the statute; or (3) imposes additional burdens, conditions, or restrictions in excess of or inconsistent with the relevant statutory provisions. In construing the Commission's authority, the reviewing court looks to the statute as a whole, not any specific provision in isolation.

Administrative Law > Judicial Review > Standards of Review > Deference to Agency Statutory Interpretation

Governments > Legislation > Interpretation

Administrative Law > Judicial Review > Standards of Review > General Overview

#### **HN5** Standards of Review, Deference to Agency Statutory Interpretation

A reviewing court gives serious consideration of the agency's interpretation of a statute, as long as that interpretation does not contradict the plain language of the statute. The legislature intends to give an agency, created to centralize expertise in a certain regulatory area, a large degree of latitude in the methods it uses to accomplish its regulatory function. However, the court need not give as much deference to an agency's interpretation of its statute if that interpretation deals with a non-technical question of law or a matter outside of the agency's expertise.

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN6** Pipelines & Transportation, Electricity Transmission

See [Tex. Util. Code Ann. § 35.004\(e\).](#)

Energy & Utilities Law > Utility Companies > Buying & Selling of Power

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > Pricing Conduct

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

### [HN7](#) Utility Companies, Buying & Selling of Power

The Public Utility Commission of Texas has the authority to address the abuse of market power. [Tex. Util. Code Ann. § 39.157](#) commands the Commission to monitor the market power of those involved in generation, transmission, distribution, and sale of electricity and to remedy abusive behavior by seeking an injunction or civil penalties, imposing administrative penalties, or suspending, revoking, or amending a participant's certificate or registration. [Tex. Util. Code Ann. § 39.157\(a\)](#) (Supp. 2004-2005). Market power abuses include predatory pricing, withholding of production, precluding entry, and collusion. [Tex. Util. Code Ann. § 39.157\(a\)](#) (Supp. 2004-2005).

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > Deregulation & Restructuring

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > General Overview

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Utility Companies > Ownership & Restructuring

Governments > Local Governments > Administrative Boards

### [HN8](#) Electric Power Industry, State Regulation

The Public Utility Commission of Texas is charged with protecting the consumer. For example, the Commission must ensure that, by the time set for the establishment of competition in the retail electricity market, protections are in place which entitle customers to safe, reliable, and reasonably priced electricity. [Tex. Util. Code Ann. § 39.101\(a\)\(1\)](#) (Supp. 2004-2005). A retail electricity customer is entitled to protection from unfair, misleading, or deceptive practices. [Tex. Util. Code Ann. § 39.101\(b\)\(6\)](#). The Commission is also directed to modify its rules regarding customer protections to ensure that at least the same level of customer protection against potential abuses and the same quality of service that exists [prior to competition], is maintained in a restructured electricity market. [Tex. Util. Code Ann. § 39.101\(f\)](#). Although the focus in [§ 39.101](#) is on the retail market, both wholesale and retail rates are now set by the market, and consequently, behavior in the wholesale market which affects price and reliability will directly impact the retail market as well.

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > Access to Electricity

Energy & Utilities Law > Electric Power Industry > Deregulation & Restructuring

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

### [HN9](#) Electricity Distribution & Transmission, Access to Electricity

See [Tex. Util. Code Ann. § 39.151\(a\)](#).

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

#### [\*\*HN10\*\*](#) [L] **Regulators, Public Utility Commissions**

The plain language of [Tex. Util. Code Ann. § 39.151](#) anticipates that the Public Utility Commission of Texas will have rules relating to reliability and accounting because the independent operator's procedures are to be made consistent with the Commission's rules.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Bilateral Contracts

Energy & Utilities Law > Utility Companies > Contracts for Service

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [\*\*HN11\*\*](#) [L] **Types of Contracts, Bilateral Contracts**

The Public Utilities Regulation Act gives the Public Utility Commission of Texas broad authority to monitor and remedy market power abuses. [Tex. Util. Code Ann. § 39.157\(a\)](#). Indeed, some of the specific examples of market power abuses listed in the statute are clearly possible in the wholesale bilateral contracts market. Furthermore, the structure of the Texas electricity system requires the Commission to act in the wholesale market in order to fulfill its statutory obligations to protect the consumer. Price fluctuation in the wholesale market will be reflected in the retail market. Thus, abusive practices in the wholesale market will have a direct effect on price and reliability in the retail market. The statute gives both the Commission and the Electric Reliability Council of Texas authority to address the behavior of market participants in the wholesale market, and such authority extends to the bilateral contracts market.

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [\*\*HN12\*\*](#) [L] **Pipelines & Transportation, Electricity Transmission**

See [16 Tex. Admin. Code § 25.503\(g\)](#).

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Utility Companies > General Overview

#### [\*\*HN13\*\*](#) [L] **Public Utility Commissions, Authorities & Powers**

The legislature specifically directed the Public Utility Commission of Texas to oversee the wholesale market to ensure reasonably priced electric power for ancillary services. [Tex. Util. Code Ann. 35.004\(e\)](#). In the existing competitive wholesale market, scarcity of electric power will be reflected in higher prices throughout the market, including prices for ancillary services. Thus, the Commission's statutory authority to ensure that ancillary services are available at reasonable prices necessarily implies the power to regulate conduct that materially and adversely affects reliability.

Administrative Law > Judicial Review > Standards of Review > Deference to Agency Statutory Interpretation

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN14** [blue icon] **Standards of Review, Deference to Agency Statutory Interpretation**

Although many of the prohibited activities enumerated in the rule clearly contain an element of intent, the court will not imply an element of intent to the general definition of prohibited activities in [16 Tex. Admin. Code § 25.503\(g\)](#) of the Wholesale Market Oversight (WMO) Rule. The WMO Rule reflects the decision of the Public Utility Commission of Texas, based on its expertise, that both intentional and unintentional actions in the wholesale market that adversely affect reliability must be prohibited in order to prevent market power abuse, ensure retail customers safe, reliable, and reasonably priced electricity, and ensure reasonably priced electric power for ancillary services.

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Utility Companies > General Overview

#### **HN15** [blue icon] **Energy & Utilities, State Regulation**

Charged with preventing market power abuse, [Tex. Util. Code Ann. § 39.157](#), ensuring safe, reliable, and reasonably priced electricity for consumers, [Tex. Util. Code Ann. § 39.101\(a\)\(1\)](#), and ensuring reasonably priced electricity for ancillary services, [Tex. Util. Code Ann. § 35.004\(e\)](#), the Public Utility Commission of Texas established the Wholesale Market Oversight (WMO) Rule, [16 Tex. Admin. Code § 25.503](#), which allows the market to set the price of electricity in accordance with the normal forces of supply and demand. Market participants are merely prevented from manipulating the market or acting in such a way as to disrupt the reliability of electricity service or artificially inflating price. Because the WMO Rule allows normal market forces to set the price of power, it does not favor regulation over competition. In fact, the limitations placed on market participants by the Commission exist for the purpose of fostering competition in a market that is uniquely vulnerable to disruption and manipulation.

Administrative Law > ... > Formal Adjudicatory Procedure > Hearings > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

#### **HN16** [blue icon] **Formal Adjudicatory Procedure, Hearings**

[16 Tex. Admin. Code § 25.503\(l\)\(4\)](#) governs the procedure of the Public Utility Commission of Texas for requesting the initiation of an enforcement proceeding after an informal fact-finding review, not the standards to be applied at such a hearing.

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [HN17](#) [L] **Electric Power Industry, State Regulation**

[16 Tex. Admin. Code § 25.503\(m\)](#) applies only to those remedies specifically authorized in the Public Utilities Regulation Act. [Tex. Util. Code Ann. §§ 15.023](#), .028, .030 (1998).

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [HN18](#) [L] **Regulators, Public Utility Commissions**

Although [Tex. Util. Code Ann. § 39.001](#) clearly anticipates competition in both the wholesale and retail markets, the Public Utility Commission of Texas is also required to ensure that electricity is safe, reliable, and reasonably priced for consumers. [Tex. Util. Code Ann. § 39.101\(a\)\(1\)](#). The Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), adequately reflects the legislature's desire to balance market interests and consumer protections.

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > Electricity Generation

Transportation Law > Interstate Commerce > Market Participant Doctrine

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [HN19](#) [L] **Electricity Distribution & Transmission, Electricity Generation**

The Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), specifies that a market participant's withholding of production constitutes an abuse of market power when that participant has "market power."

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Electric Power Industry > General Overview

#### [HN20](#) [L] **Electric Power Industry, State Regulation**

It is appropriate for the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), to take into account the unique nature of the electricity industry in defining market power, and the rule is not inconsistent with the Public Utilities Regulation Act.

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

**HN21** [blue icon] **Pipelines & Transportation, Electricity Transmission**

See [16 Tex. Admin. Code § 25.503\(g\).](#)

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

**HN22** [blue icon] **Electric Power Industry, State Regulation**

See [16 Tex. Admin. Code § 25.503\(g\)\(7\).](#)

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Governments > Legislation > Overbreadth

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Governments > Legislation > Vagueness

**HN23** [blue icon] **Agency Rulemaking, Rule Application & Interpretation**

In a facial challenge, the court will consider any limiting construction of the rule. Courts apply several standards of review to vagueness challenges, depending on the subject of the statute or rule at issue.

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Governments > Legislation > Vagueness

**HN24** [blue icon] **Agency Rulemaking, Rule Application & Interpretation**

A reviewing court will find a rule unconstitutionally vague only if it (1) does not give fair notice of what conduct may be punished, and (2) invites arbitrary and discriminatory enforcement by its lack of guidance for those charged with its enforcement.

Administrative Law > Agency Rulemaking > Rule Application & Interpretation > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

## **HN25** [blue icon] Agency Rulemaking, Rule Application & Interpretation

In determining whether a rule gives fair notice, the reviewing court examines whether the rule conveys sufficiently definite warning as to the proscribed conduct when measured by common understanding and practices.

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

## **HN26** [blue icon] Energy & Utilities Law, Antitrust Issues

The Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), specifically states that activities that would otherwise be prohibited, including practices that materially and adversely affect reliability, are not violations when (1) they serve a legitimate business purpose consistent with prices set by competitive market forces, and (2) the adverse effect on reliability, price, or accounting was not known or foreseeable with the exercise of due diligence. [16 Tex. Admin. Code § 25.503\(h\)](#). This provision gives clear notice that unforeseen accidents will not give rise to liability under the rule. The fact that [§ 25.503\(h\)](#) is an affirmative defense does not lessen the notice to market participants of what conduct is prohibited. Certainly, participants in the wholesale electricity market can determine whether their actions are taken in the service of a legitimate business purpose that is not anticompetitive. Furthermore, the rule does not require clairvoyance as to whether an action will impact price, reliability, or accounting--only diligence.

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Transportation Law > Interstate Commerce > Market Participant Doctrine

## **HN27** [blue icon] Electric Power Industry, State Regulation

The fluid concept of market power in the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), does not render enforcement of the market power abuse provision so uncertain as to deprive market participants of constitutionally required fair notice. Notice is determined by reading the rule in its entirety. [Section 25.503\(h\)](#) of the rule exempts otherwise prohibited conduct when a market participant has acted in accordance with the protocols of the Electric Reliability Council of Texas or has (1) pursued a legitimate business purpose and (2) exercised due diligence to avoid an adverse affect on prices, reliability and accounting. Thus, the examples brought forward where a market participant would be found to have engaged in prohibited conduct because it was not aware that it possessed market power are misplaced. The rule simply requires market participants to be diligent in avoiding adverse affects on the market. If a diligent inquiry would not reveal the adverse affect of legitimate activity on the market, the activity is excluded from the rule's definition of market power abuse.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Governments > Legislation > Vagueness

## **HN28** [blue icon] Judicial & Legislative Restraints, Overbreadth & Vagueness of Legislation

The absence of a definition of market power does not render the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), unconstitutionally vague.

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Governments > Legislation > Vagueness

Transportation Law > Interstate Commerce > Market Participant Doctrine

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [\*\*HN29\*\*](#) [+] **Public Utility Commissions, Authorities & Powers**

The Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), defines "efficient operation of the market" as characterized by the fullest use of competitive auctions to procure ancillary services, minimal cost socialization, and the most economical utilization of resources, subject to operational and other constraints. 16 Tex. Admin. Code Ann. [§ 25.503\(c\)\(2\)](#). This definition certainly provides guidance of what the Public Utility Commission of Texas is seeking. More importantly, the rule does not impose a duty to scour the protocols for inefficiency. There is a duty to report only if a market participant subjectively believes that a procedure produces an outcome inconsistent with the efficient and reliable operation of the market. The provision is not unconstitutionally vague.

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [\*\*HN30\*\*](#) [+] **Procedural Due Process, Scope of Protection**

Each of the challenged provisions of the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), when read in the context of the entire rule, provides reasonable notice of what conduct may be punished and does not invite arbitrary and discriminatory enforcement.

Constitutional Law > Bill of Rights > Fundamental Rights > Eminent Domain & Takings

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### [\*\*HN31\*\*](#) [+] **Fundamental Rights, Eminent Domain & Takings**

Because the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#), does not require market participants to sell power at marginal cost, the rule is not an unconstitutional taking in all of its applications.

Administrative Law > Agency Rulemaking > State Proceedings

#### [\*\*HN32\*\*](#) [+] **Agency Rulemaking, State Proceedings**

Proper notice is given when a proposed rule is changed to incorporate comments and no new subjects of regulation or persons besides those previously given notice are affected. The federal standard for adequate notice under the

federal Administrative Procedure Act states that the modified final rule must be a "logical outgrowth" of the proposed rule. Stated differently, if the final rule does not materially alter the issues addressed in the proposed rule, then notice will be deemed sufficient. The two standards are consistent: The relevant inquiry under both standards is whether the agency's notice fairly apprises affected parties of the pertinent issues to allow them to comment and participate in the rulemaking process in a meaningful and informed manner.

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Transportation Law > Interstate Commerce > Market Participant Doctrine

Administrative Law > Agency Rulemaking > State Proceedings

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

### **HN33** [blue icon] **Public Utility Commissions, Authorities & Powers**

The proposed rule of the Public Utility Commission of Texas provided adequate notice of its more fluid concept of market power in the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#). The proposed rule contains a section prohibiting "economic withholding" and defines the term as an offer of energy or capacity by a market participant in an amount sufficiently large that the market cannot clear without the offer. By defining economic withholding in terms of whether the market can clear without the offer, the Commission indicated that its prohibition on economic withholding would apply regardless of traditional notions of market power. The Commission satisfied the notice requirements of the Administrative Procedure Act.

Administrative Law > Agency Rulemaking > State Proceedings

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

### **HN34** [blue icon] **Agency Rulemaking, State Proceedings**

The Public Utility Commission of Texas complied with the Administrative Procedure Act by including a concise statement of its statutory authority to promulgate the Wholesale Market Oversight Rule, [16 Tex. Admin. Code § 25.503](#).

**Judges:** Before Chief Justice Law, Justices B. A. Smith and Pemberton: Opinion by Justice B. A. Smith; Dissenting Opinion by Justice Pemberton.

**Opinion by:** Bea Ann Smith

## **Opinion**

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[\*827] In this direct appeal, we consider a challenge to the validity of the Public Utility Commission's rule, 29 Tex. Reg. 1899 (2004) (to be codified at [16 Tex. Admin. Code § 25.503](#) (Pub. Util. Comm'n)),<sup>1</sup> [\*\*2] governing its

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<sup>1</sup> Although the commission's rule has not yet been codified, we will use its administrative code citation for the sake of clarity and convenience. We will refer to the rule as the Wholesale Market Oversight Rule (WMO Rule).

oversight of the competitive wholesale electricity market. Appellants and intervenor (collectively, "market participants")<sup>2</sup> contend that the WMO Rule (1) exceeds the Commission's statutory authority, (2) is unconstitutionally vague, (3) represents an unconstitutional taking, and (4) was passed in violation of provisions of the Administrative Procedure Act (APA). We affirm the Commission's order adopting the rule.

## BACKGROUND

An understanding of the structure of the electricity market in Texas is important to a proper determination of the validity of the challenged rule. The electricity market is unlike an ordinary market for goods or services because of the unique attributes of electricity. Electricity cannot be easily stored once it is generated and it relies on a complex infrastructure to deliver electric power from generators to the consumer. Because of constraints in the transmission system, electric power generated in some areas of the market may not be available for use in other locations. As we will discuss throughout this opinion, **[\*\*3]** these attributes create problems that do not arise in other competitive markets.

There are three principal components to the electricity industry: "generation of power; transmission of that power on high-voltage lines over long distances; and distribution of power over shorter distances to the ultimate consumer." *City Pub. Serv. Bd. of San Antonio v. Public Util. Comm'n, 9 S.W.3d 868, 870 (Tex. App.--Austin 2000), aff'd, 53 S.W.3d 310, 312, 44 Tex. Sup. Ct. J. 1014 (Tex. 2001)*. The entire industry has historically been considered a natural monopoly. *Reliant Energy, Inc. v. Public Util. Comm'n, 101 S.W.3d 129, 133 (Tex. App.--Austin 2003), rev'd and remanded Centerpoint Energy, Inc. v. Public Util. Comm'n, 143 S.W.3d 81, 47 Tex. Sup. Ct. J. 1156 (Tex. 2004)*. More recently, in recognition that the power generation and power distribution components of the electricity industry are not monopolies warranting strict regulation, the legislature has opened the wholesale electricity markets and retail electricity market to competition and market forces. See *Tex. Util. Code Ann. § 39.001(a)* (West Supp. 2004-05) (production and sale of electricity **[\*\*4]** not monopoly warranting regulation of rates, operation and services). The transmission component of the industry remains closely regulated by the Commission. See *Tex. Util. Code Ann. § 35.004* (West. Supp. 2004-05). This aspect of the industry is administered by the independent organization Electric Reliability Council of Texas (ERCOT).<sup>3</sup>

**[\*828]** The WMO Rule at issue applies primarily to participants in the wholesale electricity market. Both electric power and capacity are available in the wholesale market through (1) bilateral agreements and (2) the balancing energy services (BES) or ancillary services market.<sup>4</sup> See *Tex. Com. Energy v. TXU Energy, Inc., 2004 U.S. Dist. LEXIS 13908, at \*11 (S.D. Tex. June 24, 2004)*. The unique nature of electricity presents challenges to the industry. The transmission of electric power relies on a complex transmission **[\*\*5]** grid which itself needs to be balanced by either adding power or removing power from the grid. The transmission grid is kept in balance with power and capacity purchased through the BES market. Although the majority of electric power is bought and sold through bilateral contracts, retailers may purchase short term power through the BES market as well. See *2004 U.S. Dist. LEXIS 13908, at \*7*.

In restructuring electricity markets in favor of competition, the legislature was aware that the unique nature of electricity and the industry was not wholly consistent with a fully deregulated market and the application of established antitrust principles. In recognition of this fact, the legislature decided to retain a regulatory scheme with regard to transmission services. See *Tex. Util. Code Ann. § 35.004*. It allowed utilities to recover **[\*\*6]** the costs of

<sup>2</sup> Appellants include TXU Generation Company, L.P., TXU Portfolio Management Company, L.P., TXU Electric Delivery Company (collectively, TXU); Coalition of Wholesale Electric Market Participants (Coalition); Occidental Chemical Corporation, Occidental Permian, Ltd., Occidental Power Marketing, L.P., Occidental Power Services, Inc., Oxy Vinyls, L.P., Ingleside Cogeneration, L.P. (collectively, Occidental); Coral Power, L.L.C.; and Texas Genco, L.P. is the intervenor.

<sup>3</sup> ERCOT is also a term used to refer to the transmission system which provides power to roughly 85 percent of the State.

<sup>4</sup> The BES is a market for same day purchases of power made in fifteen-minute intervals. The ancillary services market is a market for same day or day-ahead purchases of capacity.

prudently incurred expenditures that were rendered unrecoverable as a result of the deregulated market. See *id.* §§ 39.251-265 (West Supp. 2004-05); *Reliant Energy, 101 S.W.3d at 132*. Specific consumer protection provisions were added to ensure that deregulation, in fact, achieves a benefit to the consumer. See *id.* § 39.101 (West Supp. 2004-05).

Furthermore, the legislature directed the Commission to monitor and address market power abuses associated with the generation, transmission, distribution, and sale of electricity. See *id.* § 39.157 (West Supp. 2004-05). A review of the record reflects that the legislature's concerns about anticompetitive practices and manipulation in the wholesale market were well founded.

One instance of market manipulation involved power generators overscheduling the amount of power they anticipated adding to the transmission grid. This overscheduling created congestion in the grid which those same generators were then paid to relieve. The Commission became aware of this practice and eventually required participants to refund \$ 30,000,000 obtained as a result of these improper practices. See *Tex. Com. Energy, 2004 U.S. Dist. LEXIS 13908, at \*13*. [\*\*7] The Commission has identified the practice of "hockey stick bidding" as another example of anticompetitive manipulation of the wholesale market. This bidding process involved a pricing strategy that created short term artificial price spikes in the BES market. See *2004 U.S. Dist. LEXIS 13908, at \*14-15* (describing February 2003 price spike in BES market). A Commission report states that this bidding practice added at least \$ 17 million in additional cost to power used over the course of two days in February 2003.

The Commission has also given considerable attention to the conduct of market participants in the California electricity market where abusive practices resulted in power shortages and soaring prices. See *Enron Corp. v. California ex rel. Lockyer (In re Enron Corp.), 314 B.R. 524, \*8-11 (D.N.Y. Sept. 29, 2004)* (describing manipulation of California wholesale electricity market). [\*829] Against the backdrop of these abusive practices, the Commission established the WMO Rule to articulate standards that the Commission will apply in monitoring the activities of those participating in the wholesale electricity markets. See *16 Tex. Admin. Code. § 25.503(a)* [\*\*8] .

**HN1**[] The WMO Rule addresses the Commission's oversight of the wholesale market by enumerating the duties of market participants and defining prohibited activities. See *id.* § 25.503(f),(g). The rule provides a defense to a market participant who engages in a prohibited activity if the participant demonstrates that the otherwise prohibited activity served a legitimate business purpose and that its adverse effects were not foreseeable. See *id.* at § 25.503(h). The rule defines the role of ERCOT in enforcing operating standards for market participants and establishes a process for market participants to clarify ERCOT protocols to ensure compliance. See *id.* at § 25.503(i),(j). Finally, the rule establishes record-keeping requirements for market participants and ERCOT, and details the Commission's investigation process. See *id.* at § 25.503(k),(l). The challenges raised in this direct appeal apply almost exclusively to those portions of the rule that define the duties of market participants and those activities which are prohibited.

## DIRECT APPEAL

**HN2**[] In a direct appeal of a Commission rule pursuant to *section 39.001(e) of the Public Utilities Regulation Act* (PURA), we [\*\*9] are limited to reviewing the rule's validity. See *Tex. Util. Code. Ann. § 39.001(f)* (West Supp. 2004-05); *Office of Pub. Util. Counsel v. Public Util. Comm'n, 104 S.W.3d 225, 232-33 (Tex. App.--Austin 2003, no pet.)*, *City Public Service Board of San Antonio v. Public Utility Commission of Texas, 96 S.W.3d 355, 359 (Tex. App.--Austin 2002, no pet.)*. A validity challenge tests a rule on procedural and constitutional grounds. *City of Alvin v. Public Utility Commission of Texas, 143 S.W.3d 872, 878 (Tex. App.--Austin 2004, no pet.)*. A validity challenge may also question the agency's statutory authority to promulgate the rule. *Id.* An agency rule is presumed valid, and the challenging party bears the burden to demonstrate its invalidity. *Office of Pub. Util. Counsel, 104 S.W.3d at 232*. In this case, the market participants raise issues concerning the statutory authority of the Commission to promulgate the WMO Rule, the constitutionality of the rule, and the procedures through which the rule was enacted.

## STATUTORY AUTHORITY

All of the market participants contend that, by enacting the WMO Rule, the Commission [\*\*10] has assumed powers that are not authorized by the legislature. [HN3](#)[<sup>1</sup>] The Commission is a creature of the legislature and has no inherent authority. [Public Util. Comm'n v. GTE-Southwest, Inc., 901 S.W.2d 401, 406, 38 Tex. Sup. Ct. J. 485 \(Tex. 1995\)](#). It "may exercise only those specific powers that the law confers upon it in clear and express language. As a general rule, the legislature impliedly intends that the agency should have whatever power is reasonably necessary to fulfill a function or perform a duty that the legislature has expressly placed in the agency." [Id. at 407](#). Absent specific or implied statutory authority, an agency rule is void because it is made without legal authority. [Office of Pub. Util. Counsel, 104 S.W.3d at 232](#).

[HN4](#)[<sup>1</sup>] The Commission may not exercise what is effectively a new power or a power contradictory to the statute based merely on a claim that the power is expedient for administrative purposes. [GTE-Southwest, Inc., 901 S.W.2d at 406](#). Although a rule must comport with the Commission's authorizing statute, the legislature does not need to include every specific detail or anticipate all unforeseen circumstances. [Railroad Comm'n v. Lone Star Gas Co., 844 S.W.2d 679, 687, 36 Tex. Sup. Ct. J. 436 \(Tex. 1992\)](#). [\*\*11] [\*830] To establish the WMO Rule's facial invalidity, the market participants must show that the rule: (1) contravenes specific statutory language; (2) runs counter to the general objectives of the statute; or (3) imposes additional burdens, conditions, or restrictions in excess of or inconsistent with the relevant statutory provisions. See [City of Corpus Christi v. Public Util. Comm'n, 51 S.W.3d 231, 236, 44 Tex. Sup. Ct. J. 823, 44 Tex. Sup. Ct. J. 1101 \(Tex. 2001\)](#); [Office of Pub. Util. Counsel, 104 S.W.3d at 232](#). In construing the Commission's authority, we look to the statute as a whole, not any specific provision in isolation. [Reliant Energy, Inc. v. Public Util. Comm'n, 62 S.W.3d 833, 839 \(Tex. App.--Austin 2001, no pet.\)](#).

[HN5](#)[<sup>1</sup>] We give serious consideration of the Commission's interpretation of PURA, as long as that interpretation does not contradict the plain language of the statute. [Continental Casualty Company v. Downs, 81 S.W.3d 803, 807, 45 Tex. Sup. Ct. J. 755 \(Tex. 2002\)](#). The legislature intends to give an agency, created to centralize expertise in a certain regulatory area, a large degree of latitude in the methods it uses to accomplish its regulatory function. [State v. Public Util. Comm'n, 883 S.W.2d 190, 197, 37 Tex. Sup. Ct. J. 1102 \(Tex. 1994\)](#). [\*\*12] However, we need not give as much deference to an agency's interpretation of its statute if that interpretation deals with a non-technical question of law or a matter outside of the agency's expertise. [Rylander v. Fisher Controls Int'l., Inc., 45 S.W.3d 291, 302 \(Tex. App.--Austin 2001, no pet.\)](#).

## Statutory Powers of the Commission

Before addressing the contentions of the market participants, it is useful to review the relevant statutory powers granted to the Commission by the legislature. [Section 39.001\(a\) of PURA](#) explains that the statute's purpose is to "protect the public interest during the transition to and in the establishment of a fully competitive electric power industry." [Tex. Util. Code Ann. § 39.001\(a\)](#). [Section 39.001\(d\)](#) states that this objective is to be carried out through competitive rather than regulatory means to the greatest extent feasible, and that the Commission's rules should be "practical and limited so as to impose the least impact on competition." [Id. § 39.001\(d\)](#). Several provisions of the statute deal directly with the Commission's authority to oversee the behavior of participants in the wholesale [\*\*13] electricity market.

The statute clearly gives the Commission broad authority to create rules governing the conduct of market participants in the BES and ancillary services market. [Section 35.004\(e\)](#) states:

[HN6](#)[<sup>1</sup>] The commission shall ensure that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, predatory, or anticompetitive.

*Id.* [§ 35.004\(e\)](#).<sup>5</sup> In addition [HN7](#) the Commission has the authority to address the abuse [**\*831**] of market power. [Section 39.157](#) commands the Commission to monitor the market power of those involved in generation, transmission, distribution, and sale of electricity and to remedy abusive behavior by seeking an injunction or civil penalties, imposing administrative penalties, or suspending, revoking, or amending a participant's certificate or registration. *Id.* [§ 39.157\(a\)](#) (West Supp. 2004-05). Market power abuses include predatory pricing, withholding of production, precluding entry, and collusion. *Id.*

[\*\*14] [HN8](#) The Commission is also charged with protecting the consumer. For example, the Commission must ensure that, by the time set for the establishment of competition in the retail electricity market, protections are in place which entitle customers to "safe, reliable, and reasonably priced electricity." *Id.* [§ 39.101\(a\)\(1\)](#) (West Supp. 2004-05). A retail electricity customer is entitled to protection from unfair, misleading, or deceptive practices. *Id.* [§ 39.101\(b\)\(6\)](#). The Commission is also directed to modify its rules regarding customer protections to ensure that "at least the same level of customer protection against potential abuses and the same quality of service that exists [prior to competition], is maintained in a restructured electricity market." *Id.* [§ 39.101\(f\)](#). Although the focus in [section 39.101](#) is on the retail market, both wholesale and retail rates are now set by the market, and consequently, behavior in the wholesale market which affects price and reliability will directly impact the retail market as well.

## Commission's Authority Over the Wholesale Market

We initially address Coalition and Coral Power's contention that the WMO Rule is invalid because [\*\*15] it unlawfully usurps authority granted to ERCOT by the legislature. See [City Pub. Serv. Bd., 53 S.W.3d at 316](#) (as creature of legislature, Commission has no authority beyond those powers conferred by legislature). [PURA section 39.151](#) calls for the establishment of an independent organization charged with ensuring:

- [HN9](#) (1) access to transmission and distribution systems;
- (2) reliability and adequacy of the regional electric network delegates;
- (3) timely distribution of information concerning customer choice; and
- (4) accurate accounting of production and delivery in the wholesale market.

[Tex. Util. Code Ann. § 39.151\(a\)](#). ERCOT is the established independent organization for most of the State of Texas. See [Hammack v. Public Util. Comm'n, 131 S.W.3d 713, 719 \(Tex. App.--Austin 2004, pet. denied\)](#). Coalition and Coral Power insist that legislature granted this authority to ERCOT and limited the Commission's role in these matters to "oversight and review." See *id.* [§ 39.151\(d\)](#). They contend that the WMO Rule's detailed provisions governing the conduct of market participants oversteps the role of oversight [**\*16**] and review and assumes powers delegated to ERCOT.

<sup>5</sup> Coalition contends that the final sentence in [section 35.004\(e\)](#) negates the Commission's authority over the ancillary services market once customer service is introduced. The final sentence of [section 35.004\(e\)](#) states:

On the introduction of customer choice in the ERCOT power region, acquisition of generation-related ancillary services on a nondiscriminatory basis *by the independent organization in ERCOT* on behalf of entities selling electricity at retail shall be deemed to meet the requirements of this subsection.

[Tex. Util. Code Ann. § 35.004\(e\)](#) (West 2004-05) (emphasis added). Reading the statute as a whole, however, it is clear that the legislature intended that only acquisitions of ancillary services by the independent organization would be deemed to meet the requirements of the section. This is because the independent organization is not affiliated with any market participant and is already subject to Commission oversight. See *id.* [§ 39.151](#).

Coalition and Coral Power's contention is based on an incomplete reading of the statute. The provision granting the commission "oversight and review" authority states:

An independent organization certified by the commission for a power region shall establish and enforce procedures *consistent with this title and the commission's rules* relating to the reliability of the regional electric network and accounting for the production and delivery of electricity among generators and all other market participants. The procedures shall be subject to commission oversight and review.

*Id.* (emphasis added). Here, [HN10](#)[<sup>1</sup>] the plain language of the statute anticipates that the [\*832] Commission will have rules relating to reliability and accounting because the independent operator's procedures are to be made consistent with the Commission's rules. Although Coalition and Coral power may question the wisdom of establishing overlapping procedures of the independent organization and Commission rules relating to reliability and accounting, this is a matter to be addressed to the legislature.

Coalition further contends that the Commission lacks [\*\*17] the statutory authority to prohibit market power abuses in the wholesale bilateral contracts market. However, [HN11](#)[<sup>1</sup>] the statute gives the Commission broad authority to monitor and remedy market power abuses. See *id.* [§ 39.157\(a\)](#). Indeed, some of the specific examples of market power abuses listed in the statute are clearly possible in the wholesale bilateral contracts market. Furthermore, the structure of the Texas electricity system requires the Commission to act in the wholesale market in order to fulfill its statutory obligations to protect the consumer. In our system, price fluctuation in the wholesale market will be reflected in the retail market. Thus, abusive practices in the wholesale market will have a direct effect on price and reliability in the retail market. Because we find that the statute gives both the Commission and ERCOT authority to address the behavior of market participants in the wholesale market, and that such authority extends to the bilateral contracts market, we overrule Coalition and Coral Power's challenge to the validity of the rule on these grounds.

### Intent as an Element

Next, Occidental, TXU, and Texas Genco challenge the WMO Rule on the [\*\*18] grounds that it lacks an intent element in defining prohibited conduct. See [16 Tex. Admin. Code § 25.503\(g\)](#). They argue that the Commission lacks the statutory authority to prohibit conduct that is not intentional and that the prohibition's inclusion of unintentional conduct runs counter to the general objective of the statute to impose only "practical and limited" rules favoring competition rather than regulation. However, Occidental, TXU, and Texas Genco's argument relies on the incorrect assumption that the only statutory basis for the WMO Rule's prohibited activities is the prevention of market power abuse pursuant to [PURA section 39.157](#). Because we hold that the Commission is empowered to regulate conduct in the wholesale market for the purposes of protecting consumers and ensuring reasonably priced power for ancillary services, we will overrule Occidental, TXU, and Texas Genco's contention.

Texas Genco directs this Court to antitrust principles in the context of interpreting the term "market power abuses." It contends that the element of intent is inherent in the term "market power abuse" and therefore any prohibited activities included in [\*\*19] the rule must also contain an element of intent. In fact, the United States Supreme Court has read an intent element into the [Sherman Antitrust Act](#). See [Verizon Communications Inc v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 124 S. Ct. 872, 878-79, 157 L. Ed. 2d 823 \(2004\)](#); [United States v. Grinnell Corp., 384 U.S. 563, 570-71, 16 L. Ed. 2d 778, 86 S. Ct. 1698 \(1966\)](#). The [Sherman Act](#) prohibits monopolization and does not expressly contain an element of intent. [15 U.S.C.A. § 2 \(West 1997\)](#) ("Every person who shall monopolize . . . shall be deemed guilty."). The court explained that an offense under the act requires, "in addition to the possession of monopoly power in the relevant market, 'the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.'" [Verizon, 124 S. Ct. at 878](#) (citing [Grinnell Corp., 384 U. S. at 570-571](#)). The court further [\*833] justified reading willfulness into the statute:

The mere possession of monopoly power, and the concomitant charging of monopoly prices, is not only [\*\*20] not unlawful; it is an important element of the free-market system. The opportunity to charge monopoly prices--at least for a short period--is what attracts "business acumen" in the first place; it induces risk taking that

produces innovation and economic growth. To safeguard the incentive to innovate, the possession of monopoly power will not be found unlawful unless it is accompanied by an element of anticompetitive conduct.

*Id. at 878-79.* Similarly, the Supreme Court has interpreted language in the *Securities and Exchange Act* which prohibits the use of any "manipulative or deceptive device or contrivance" in the sale or purchase of securities to include an element of willfulness. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 199, 47 L. Ed. 2d 668, 96 S. Ct. 1375 (1975) (terms "manipulative, device, and contrivance" indicate willful conduct).

Although **antitrust law** does not control our interpretation of PURA,<sup>6</sup> the reasoning of the Supreme Court in interpreting the *Sherman Antitrust Act* and the *Securities and Exchange Act* is persuasive when interpreting the Commission's authority to monitor and remedy "market power abuse." See *Tex. Util. Code Ann. 39.157(a)* [\*\*21]. Abuse is defined as "a corrupt practice" or "deceitful act." Webster's New International Dictionary 8 (3rd ed. 1986). The term "market power abuse" suggests that the legislature intended to prohibit only intentional or willful conduct. See *Ernst & Ernst*, 425 U.S. at 197.

Section (g) of the WMO Rule prohibits [HN12](#) [\*\*22] "any act or practice that materially and adversely affects the reliability of the regional electric network" or the proper accounting for the production and delivery of electricity." While this general prohibition lacks any element of intent, the rule then lists a number of specific practices that all appear to include an element of intent. The dissent insists that an element of intent be implied in the WMO Rule. If the authority for this rule was derived only from [section 39.157\(a\)](#) governing "market power abuse," we would agree that an element of intent is implied. However, we look to the statute as a whole, not any specific provision in isolation, to determine the Commission's statutory authority. See *Reliant Energy*, 62 S.W.3d at [839](#).

The dissent, Occidental, TXU, and Texas Genco all contend that the absence of an intent element in the WMO Rule exceeds the Commission's statutory authority. The dissent states that both *chapter 39 of PURA* and the *Texas Free Enterprise and Antitrust Act* seek to balance the policy goals of promoting competition and protecting the integrity of market mechanisms. It then concludes that the majority ignores these antitrust principles. The dissent overlooks a vital objective of PURA--to protect the consumer in the new competitive marketplace. [\*\*23] See *Tex. Util. Code Ann. §§ 39.001(a)* (West 2004-05) ("this chapter is enacted to protect the public interest during the transition to and the establishment of a fully competitive electric power industry"), [39.101\(a\)\(1\)](#) (consumers [\*834] entitled to safe, reliable, and reasonably priced electricity) (West 2004-05). As we will discuss below, the Commission also has statutory obligations to protect consumers in a deregulated market and to ensure reasonably priced ancillary services for the transmission of electricity. The WMO Rule's prohibition of some unintentional conduct is authorized by these additional statutory powers. See *id.*; *Tex. Util. Code Ann. § 35.004(e)* (West 2004-05).

Reviewing the Commission's order, it is clear that the Commission relied on the consumer protection provisions of PURA as a basis for its authority in drafting the WMO Rule, as well as the market power abuse provision in [section 39.157](#). See 29 Tex. Reg. 1905 (purpose of the WMO Rule is to protect consumer). [Section 39.101\(a\) of PURA](#) commands the Commission to establish protections which ensure that customers receive "safe, reliable, and reasonably [\*\*24] priced electricity." Although [section 39.101](#) was established to protect retail customers, the legislature has decided that both the retail and wholesale electricity markets should be governed by market forces. Thus, issues relating to reliability or price in the wholesale market will necessarily be reflected in the retail market.<sup>7</sup>

<sup>6</sup> Texas Genco cites language in [PURA section 39.158\(b\)](#) that the statute is intended to complement other existing state and federal **antitrust law**. It contends that this provision indicates the legislature's intent that the statute be construed using "established antitrust principles." Texas Genco's contention is based on a reading of one sentence in [section 39.158\(b\)](#) in isolation. [Section 39.158\(b\)](#) has nothing to do with construing other provisions within the statute; it merely states that the remedies in the statute were intended to add to, not replace, existing antitrust provisions.

<sup>7</sup> Texas Genco acknowledges in its reply brief that increased prices in the Texas wholesale market will be reflected in the retail market by distinguishing the Texas industry from California where "utilities could not increase rates to reflect increases in

In the market system established by the legislature, the Commission would be unable to ensure retail customers "safe, reliable, and reasonably priced electricity" if its authority did not extend to the wholesale market. See [GTE-Southwest, Inc., 901 S.W.2d at 407](#) (legislature impliedly intends agency has all power reasonably necessary to carry out statutory function).

[\*\*25] In addition, [HN13](#)<sup>↑</sup> the legislature specifically directed the Commission to oversee the wholesale market to ensure reasonably priced electric power for ancillary services. [Tex. Util. Code Ann. 35.004\(e\)](#). In the existing competitive wholesale market, scarcity of electric power will be reflected in higher prices throughout the market, including prices for ancillary services. Thus, the Commission's statutory authority to ensure that ancillary services are available at reasonable prices necessarily implies the power to regulate conduct that materially and adversely affects reliability. See [GTE-Southwest, Inc., 901 S.W.2d at 407](#).

[HN14](#)<sup>↑</sup> Although many of the prohibited activities enumerated in the rule clearly contain an element of intent, we will not imply an element of intent to the general definition of prohibited activities in [section 25.503\(g\)](#) of the WMO Rule. The WMO Rule reflects the Commission's decision, based on its expertise, that both intentional and unintentional actions in the wholesale market that adversely affect reliability must be prohibited in order to prevent market power abuse, ensure retail customers "safe, reliable, and reasonably priced" [\[\\*\\*26\]](#) electricity," and ensure reasonably priced electric power for ancillary services. See [Public Util. Comm'n, 883 S.W.2d at 197](#) (deference given to agency interpretation of statute that relies upon agency expertise). We overrule Occidental, TXU, and Texas Genco's contention that the WMO Rule's definition of prohibited activity must contain an element of intent.

### Rule Not Inconsistent With Statute

We also disagree with Occidental, TXU, and Texas Genco's contention that the prohibition of unintentional activities runs counter to the general objectives of [\[\\*835\]](#) the statute. They argue that the WMO Rule (1) favors regulation over competition, and (2) is not practical and limited in its impact on competition. See [Tex. Util. Code Ann. § 39.001\(d\)](#). [HN15](#)<sup>↑</sup> Charged with preventing market power abuse, see *id.* [§ 39.157](#), ensuring safe, reliable, and reasonably priced electricity for consumers, see *id.* [§ 39.101\(a\)\(1\)](#), and ensuring reasonably priced electricity for ancillary services, see *id.* [§ 35.004\(e\)](#), the Commission established the WMO Rule which allows the market to set the price of electricity in accordance with the normal forces of [\[\\*\\*27\]](#) supply and demand. Market participants are merely prevented from manipulating the market or acting in such a way as to disrupt the reliability of electricity service or artificially inflating price. Because the WMO Rule allows normal market forces to set the price of power, it does not favor regulation over competition. In fact, the limitations placed on market participants by the Commission exist for the purpose of fostering competition in a market that is uniquely vulnerable to disruption and manipulation.

The WMO Rule is also practical and limited. The rule is broad enough to encompass all activities that may materially affect reliability, but it is limited in its application. The affirmative defense provision allows market participants to demonstrate that activities which may have materially affected the reliability of electric service were in service of a legitimate business purpose and the resulting effect on the market was not foreseeable. See [16 Tex. Admin. Code § 25.503\(h\)](#).

Occidental argues that the WMO Rule's informal investigation process in which a market participant may justify an otherwise prohibited activity is not "practical and [\[\\*\\*28\]](#) limited." See [Tex. Util. Code Ann. § 39.001\(d\)](#). It explains that informal investigations are not limited in duration and subjects market participants to "significant financial risk and uncertainty." However, we hesitate to second guess the Commission's determination that the WMO Rule is a practical and limited means to achieve the Commission's legitimate goals. The WMO Rule balances the sometimes competing statutory obligations of establishing a competitive market for electricity and ensuring safe, reliable, and reasonably priced power for consumers and ancillary services by allowing market forces to set the price of electricity, but prohibiting market manipulation and activities that will materially affect reliability. The Commission

was undoubtably aware that even an informal investigation of those who might innocently engage in prohibited activities would impose a burden on the market participant. But the Commission's balancing of its statutory obligations through the WMO Rule relies upon the Commission's considerable understanding of the operation of the electricity market and this is precisely the sort of agency interpretation that courts should [\[\\*\\*29\]](#) give deference to. See [Public Util. Comm'n, 883 S.W.2d at 197](#). We overrule Occidental, TXU, and Texas Genco's contention that the rule is inconsistent with the general objectives of the statute.

### **Burden of Proof**

Because we hold that no intent element is mandated by statute, we also reject the market participants' contentions and the comments by the dissent that the WMO Rule impermissibly shifts the burden of proof on intent to market participants through the affirmative defense provision in [section 25.503\(h\)](#). More specifically, Occidental and Coalition insist that the WMO Rule is invalid because it generally shifts the burden of proof from the Commission to market participants. Coalition contends that [section 25.503\(l\)\(4\)](#) of the WMO Rule requires only a minimal showing of a violation before it shifts the burden to a market participant [\[\\*836\]](#) to prove its innocence. However, [HN16](#)<sup>↑</sup> this provision governs the Commission's procedure for requesting the initiation of an enforcement proceeding after an informal fact-finding review, not the standards to be applied at such a hearing. The rule requires the Commission to include specific information regarding its investigation [\[\\*\\*30\]](#) "as part of its *prima facie case*." *Id.* [§ 25.503\(l\)\(4\)\(A\)-\(D\)](#). We note that the rule does not equate the required information with a *prima facie* showing of a violation in an enforcement proceeding. Rather, it enumerates specific showings to be made by the Commission in order initiate an enforcement proceeding. Our reading of the language of the WMO Rule is confirmed by the Commission's admission in its post-submission letter brief comparing the required showing of prohibited conduct to a showing of probable cause and explaining that "subsection (l) does not describe the evidence required for the Commission to find at the conclusion of [an enforcement action] that a market participant has violated the Rule." As referenced by the WMO Rule, an enforcement action is governed by the procedures laid out in [section 22.246](#) of the administrative code. See [16 Tex. Admin. Code § 22.246](#) (administrative penalties).<sup>8</sup> Because [section 25.503\(l\)\(4\)](#) does not establish a burden of proof for enforcement proceedings, we reject Occidental and Coalition's challenge to the validity of the WMO Rule on these grounds.

### **[\*\*31] Scope of the Remedy**

Coalition also contends that [section 25.503\(m\)](#) impermissibly expands the Commission's authority by authorizing the imposition of "any legal remedy" for a violation of the rule by a market entity. However, the preamble of the rule states that subsection (m) was not intended to expand or limit the types of remedies available to the Commission. Furthermore, the Commission concedes in its brief that it only has authority to impose those remedies available under PURA. We agree that [HN17](#)<sup>↑</sup> [subsection \(m\) of rule 25.503](#) applies only to those remedies specifically authorized in PURA. See [Tex. Util. Code Ann. §§ 15.023, .028, .030](#) (West 1998).

### **No Impermissible Regulation of Price**

Coalition and Coral Power next contend that the Commission's rule impermissibly regulates the price of electricity by requiring market participants to charge marginal cost prices. This contention relies on language in the preamble to the rule that states, "pricing in excess of marginal cost by a seller who is immune from the chastening hand of competition is an abuse of market power," and on additional language that the Commission has a duty to [\[\\*\\*32\]](#) protect the public from prices that are "substantially above the marginal cost of a marginally efficient unit when not

<sup>8</sup> Although the burden of proof is not discussed in [section 22.246](#) of the administrative code, the Commission states in its post-submission letter brief that "in all cases the burden is on the Commission staff to demonstrate the elements of a *prima facie case* to the satisfaction of an administrative law judge, if applicable, and ultimately to the Commissioners as decisionmakers."

tempered by competition." 29 Tex. Reg. 1916. We do not read these statements in the preamble to set the price of power at "marginal cost." In fact, the Commission deleted a provision in its proposed rule which did exactly that. Read in context, the preamble merely makes the wholly unremarkable observation that prices that are substantially above the marginal cost of power from the most expensive generating unit, under circumstances where there is no possibility of a competing offer, are harmful to the public. In light of the administrative record and the explicit statements by the Commission that the [\*837] WMO Rule does not require marginal-cost pricing, we find no merit in the theory that a market participant will be coerced into setting prices at an unprofitable rate out of an unsubstantiated fear that the Commission will initiate an investigation.

In a related point, Coalition and Coral Power defend the market's susceptibility to "temporary price spikes." They contend that the WMO Rule interferes with "the normal forces of competition," and thus imposes regulatory rather [\*\*33] than competitive means to control market behavior. See [Tex. Util. Code Ann. § 39.001\(d\)](#). Presumably, Coalition and Coral Power adopt the reasoning of the Supreme Court in *Verizon*, that the opportunity to impose monopoly prices provides incentive to market participants to innovate and develop the industry. See [Verizon, 124 S. Ct. at 878-79. HN18](#)<sup>18</sup> Although the statute clearly anticipates competition in both the wholesale and retail markets, the Commission is also required to ensure that electricity is safe, reliable, and reasonably priced for consumers. See *id.* [§ 39.101\(a\)\(1\)](#). We conclude that the Commission's rule adequately reflects the legislature's desire to balance market interests and consumer protections. We overrule Coalition and Coral Power's issues regarding the regulation of price.

## Market Power

Coral Power contends that the Commission's concept of market power is inconsistent with the statute and case law defining market power. [HN19](#)<sup>19</sup> The WMO Rule specifies that a market participant's withholding of production constitutes an abuse of market power when that participant has "market power." The Commission explains in [\*\*34] the preamble to the rule that its concept of market power is necessarily fluid:

In electricity markets, it is difficult to find markets that continuously operate under a competitive environment, and it is not unusual to find local market power in geographical pockets, even when the generation share of each resource owner is low, because transmission constraints or other reliability constraints often give some resource owners temporary or localized market power. Market power is a dynamic phenomenon in electricity markets, and the commission must have the ability to address abuses that occur during the times when the market is not competitive, even as those times become less frequent.

29 Tex. Reg. 1916. Coral Power points to a provision of the statute which limits a generator's share of installed capacity to twenty percent of the total. See [Tex. Util. Code Ann. § 39.154\(a\)](#). Coral Power also directs us to federal antitrust case law which states that claims of illegal monopolization under the [Sherman Act](#) should usually be rejected when the alleged monopoly possesses less than thirty percent market share. See [M & M Med. Supply & Serv. v. Pleasant Valley Hosp., 981 F.2d 160, 168 \(4th Cir. 1992\)](#) [\*\*35] (en banc) (citing 3 Philip Areeda & Donald F. Turner, [Antitrust Law](#) P 835, at 350). Based on the statutory limit of generation capacity to twenty percent and federal [antitrust law](#), Coral Power argues that the Commission may not adopt its own concept of market power which subjects to scrutiny those generators who possess less than twenty percent capacity.

We find no indication that the legislature intended to adopt twenty percent as a cutoff definition of market power. Had the legislature believed that a generation capacity of more than twenty percent is required to possess market power, then the limitations on generation capacity would render [PURA section 39.157](#)'s prohibition on market power abuse irrelevant. See [Meritor Auto., Inc. v. Ruan Leasing, 1\\*838\] 44 S.W.3d 86, 90, 44 Tex. Sup. Ct. J. 549 \(Tex. 2001\)](#) (we presume entire statute intended to be effective and "when possible, each sentence, phrase, clause and word is given effect, so that the statute makes sense as a cohesive whole"). We also do not find the reasoning of the Fourth Circuit in *M & M Medical Supply* to be applicable to the Texas electricity industry. See [981 F.2d at 168](#). The electricity industry is inherently [\*\*36] different from commerce in other goods and services. The sale of electricity is bound to a transmission grid which may often obtain power or capacity only from certain generators in certain locations. It would make little sense to determine market power as a percentage of total capacity statewide

in instances when only a portion of the capacity is actually available. Furthermore, the Commission has substantial expertise in the application of market forces to the electricity market. We grant deference to the Commission's interpretation of PURA when that interpretation is based on the Commission's specialized expertise. See [Public Util. Comm'n, 883 S.W.2d at 197](#). We hold that [HN20](#)<sup>↑</sup> it is appropriate for the Commission's rule to take into account the unique nature of the electricity industry in defining market power and that the rule is not inconsistent with the statute. We overrule Coral Power's challenge to the WMO Rule's use of the term market power.

## CONSTITUTIONAL CHALLENGES

### Vagueness

All market participants allege that the WMO Rule is unconstitutionally vague. Their primary concerns focus on the general definition of a prohibited activity in [section 25.503\(g\)](#) [\[\\*37\]](#) and the prohibition of market power abuse in [subsection \(g\)\(7\)](#). The general provision prohibits [HN21](#)<sup>↑</sup> "any act or practice that materially and adversely affects the reliability of the regional electric network or the proper accounting for the production and delivery of electricity." [16 Tex. Admin. Code § 25.503\(g\)](#). The prohibition on market power abuse includes [HN22](#)<sup>↑</sup> "withholding of production, whether economic withholding or physical withholding, by a market participant who has market power." *Id.* [§ 25.503\(g\)\(7\)](#). The WMO Rule does not define the term market power.

Because this is a direct appeal, we may consider only a facial challenge to the rule: that the rule is impermissibly vague in all of its applications. See [Village of Hoffman Estates v. Flipside, Hoffman Estates, Inc., 455 U.S. 489, 494-95, 71 L. Ed. 2d 362, 102 S. Ct. 1186 \(1982\)](#); [City Pub. Servs. Bd. of San Antonio, 96 S.W.3d at 359](#). [HN23](#)<sup>↑</sup> In a facial challenge, we will consider any limiting construction of the rule provided by the Commission. See [Village of Hoffman, 455 U.S. at 494](#). Courts apply several standards of review to vagueness challenges, depending [\[\\*38\]](#) on the subject of the statute or rule at issue. We first note that the market participants do not allege that the WMO Rule impinges upon any constitutionally protected conduct, and therefore, we do not apply the higher scrutiny of an "overbreadth" challenge. See [Village of Hoffman Estates, 455 U.S. at 494](#). Instead we will apply the standards for determining whether the rule is unduly vague.

[HN24](#)<sup>↑</sup> We will find a rule unconstitutionally vague only if it (1) does not give fair notice of what conduct may be punished, and (2) invites arbitrary and discriminatory enforcement by its lack of guidance for those charged with its enforcement.<sup>9</sup> [\[\\*839\] Rooms with a View, Inc. v. Private Nat. Mortgage Ass'n, Inc., 7 S.W.3d 840, 845 \(Tex. App.-Austin 1999, pet. denied\)](#); see [Village of Hoffman Estates, 455 U.S. at 498](#); [Commission for Lawyer Discipline v. Benton, 980 S.W.2d 425, 437, 41 Tex. Sup. Ct. J. 1250 \(Tex. 1998\)](#). The United States Supreme Court has explained:

Although the doctrine focuses both on actual notice to citizens and arbitrary enforcement, we have recognized recently that the more important aspect of vagueness doctrine 'is not actual notice, [\[\\*39\]](#) but the other principal element of the doctrine--the requirement that a legislature establish minimal guidelines to govern law enforcement.'

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<sup>9</sup> We decline the Commission's invitation to apply the less stringent standard for vagueness applicable to economic regulation. Where, as here, a rule or statute carries "potentially significant civil and administrative penalties, including fines and license revocation," quasi-criminal treatment is appropriate and thus the more strict standard of review applies." [Ford Motor Co. v. Texas Dep't of Transp., 264 F.3d 493, 508 \(5th Cir. 2001\)](#) (citing [Women's Med. Ctr. of N. W. Houston v. Bell, 248 F.3d 411, 422 \(5th Cir. 2001\)](#)).

*Kolender v. Lawson*, 461 U.S. 352, 357-58, 75 L. Ed. 2d 903, 103 S. Ct. 1855 (1983) (citing *Smith v. Goguen*, 415 U.S. 566, 574, 39 L. Ed. 2d 605, 94 S. Ct. 1242 (1974)). Moreover, Justice Tom C. Clark noted that courts must take a realistic approach to ruling on vagueness:

Few words possess the precision of mathematical symbols, most statutes must deal with untold and unforeseen variations in factual situations, and the practical necessities of discharging the business of government inevitably limit the specificity with which legislators can spell out prohibitions. Consequently, no more than a reasonable degree of certainty can be demanded. Nor is it unfair to require that one who deliberately goes perilously close to an area of proscribed conduct shall take the risk that he may cross the line.

*Boyce Motor Lines, Inc. v. United States*, 342 U.S. 337, 340, 96 L. Ed. 367, 72 S. Ct. 329 (1952); see *Rooms with a View*, 7 S.W.3d at 845 (statute not automatically void for vagueness simply because it is difficult [\*\*40] to determine whether certain "marginal" acts fall within its language).

The market participants contend that subsection (g) of the WMO Rule is unconstitutionally vague because it does not give fair notice of what conduct may be punished under the law. See *Rooms with a View*, 7 S.W.3d at 845. **HN25**[<sup>1</sup>] In determining whether a rule gives fair notice, we examine whether the rule conveys sufficiently definite warning as to the proscribed conduct when measured [\*\*41] by common understanding and practices. See *Pennington v. Singleton*, 606 S.W.2d 682, 689, 23 Tex. Sup. Ct. J. 587 (Tex. 1980). Because our concern is for those to whom the WMO Rule is directed, we scrutinize the rule by asking whether the ordinary participant in the wholesale electric power market could understand and comply with it. See *Commission for Lawyer Discipline*, 980 S.W.2d at 437 (disciplinary rules scrutinized under "ordinary lawyer" standard).

### **Prohibited activities**

Coalition, Texas Genco, TXU, and Occidental object to the general definition of a prohibited activity contained in the WMO Rule. See *16 Tex. Admin. Code § 25.503(g)*. TXU presents examples of mechanical failures and computer glitches which may adversely affect reliability or accounting. It contends that the rule gives insufficient notice because a market participant could be found to have engaged in a prohibited activity as a result of accidents or ordinary mechanical breakdowns. It argues that an open-ended, broadly worded prohibition is confusing, creates unknown risks to market participants and does not provide the specificity needed to allow market [\*\*42] participants to take measures to avoid violations. The dissent acknowledges [\*840] these contentions stating "the market participants go as far as to urge that [WMO Rule] is unconstitutionally vague, and they are not far off the mark. . . ." However, we do not read this subsection of the rule in isolation. See *Reliant Energy*, 62 S.W.3d at 839. **HN26**[<sup>1</sup>] The WMO Rule specifically states that activities that would otherwise be prohibited, including practices that materially and adversely affect reliability, are not violations when (1) they serve a legitimate business purpose consistent with prices set by competitive market forces, and (2) the adverse effect on reliability, price, or accounting was not known or foreseeable with the exercise of due diligence. *16 Tex. Admin. Code § 25.503(h)*. This provision gives clear notice that the unforeseen accidents described by TXU will not give rise to liability under the rule.<sup>10</sup> The fact that subsection (h) is an affirmative defense does not lessen the notice to market participants of what conduct is prohibited.<sup>11</sup> Certainly, participants in the wholesale electricity market can determine whether their actions [\*\*43] are taken in the service of a legitimate business purpose that is not anticompetitive. Furthermore, the rule does not require clairvoyance as to whether an action will impact price, reliability, or accounting--only diligence.

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<sup>10</sup> The Commission also points out in its post-submission letter brief that the ERCOT protocols address issues such as scheduled maintenance and the shutdown of plants. When an action is authorized by ERCOT under its protocols, it is not a prohibited activity. See *16 Tex. Admin. Code § 25.503(g)* (prohibited activity excludes acts or practices expressly allowed by ERCOT protocols or by official interpretations of protocols).

<sup>11</sup> TXU complains of the stigmatizing effect of informal commission investigations in which it is compelled to provide information demonstrating that certain actions served legitimate business purposes. However, we cannot conclude that an informal investigation, even when it is disclosed to the public, amounts to the sort of "punishment" which raises vagueness concerns.

[\*\*44] Courts have upheld similarly general prohibitions when challenged for vagueness. For example, the *Sherman Antitrust Act*'s prohibition on anticompetitive behavior merely states that "every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States . . . shall be deemed guilty of a felony." [15 U.S.C.A. § 2](#). This provision has consistently been found to provide fair notice. See [Nash v. United States, 229 U.S. 373, 57 L. Ed. 1232, 33 S. Ct. 780, 781-82 \(1913\)](#); <sup>12</sup> [Atlas Building Prods. Co. v. Diamond Block and Gravel Co., 269 F.2d 950, 955 \(10th Cir. 1959\)](#) (restraint of trade and monopolization provision of *Sherman Act* have long been sustained against claim of unconstitutional vagueness).

[\*\*45] In *Pennington*, the state supreme court held that the *Texas Deceptive Trade Practices--Consumer Protection Act* (DTPA) provided adequate notice to survive a vagueness challenge. [Pennington, 606 S.W.2d at 689-90](#). Although the supreme court allowed "greater leeway" noting that [\*841] the DTPA is a regulatory statute governing business activity, the similarities between the DTPA and the WMO Rule make the reasoning persuasive. The DTPA contains a general prohibition that "false, misleading, or deceptive acts or practices in the conduct of any trade or commerce are hereby declared unlawful." [Tex. Bus. & Com. Code Ann. § 17.46\(a\)](#) (West Supp. 2004-05). It then provides a non-exhaustive list of false, misleading, or deceptive acts. *Id.* [§ 17.46\(b\)](#). The supreme court explained that the general nature of the statute was necessary:

The boundaries of illegality under the DTPA must remain flexible because it is impossible to list all methods by which a consumer may be misled or deceived.

[Pennington, 606 S.W.2d at 689](#).<sup>13</sup> We note that the supreme court also declined to require an intent element in order for the statute [\*\*46] to pass constitutional muster. [Id. at 689-90](#).

The dissent counters that the United States Supreme Court has imposed an element of willfulness on the *Sherman Act* in order to cure vagueness. See [United States v. Grinnell Corp., 384 U.S. 563, 570-71, 16 L. Ed. 2d 778, 86 S. Ct. 1698 \(1966\)](#); [Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 124 S. Ct. 872, 878-79, 157 L. Ed. 2d 823 \(2004\)](#). However, this element of intent was imposed as a matter of statutory interpretation, [\*\*47] not out of vagueness concerns. See [Verizon Communications, 123 S. Ct. at 878-79](#); see also [Ernst v. Hochfelder, 425 U.S. 185, 199, 47 L. Ed. 2d 668, 96 S. Ct. 1375 \(1975\)](#) (construing language of *Securities and Exchange Act* to include element of intent).

The dissent also incorrectly construes language from the Texas Supreme Court's opinion in [Caller-Times Pub. Co. v. Triad Comm., Inc., 826 S.W.2d 576, 581, 35 Tex. Sup. Ct. J. 509 \(Tex. 1992\)](#). There, the supreme court noted while interpreting the *Texas Antitrust Act* that a vague standard has a "chilling effect" on business. *Id.* Again, this statement was made as a matter of statutory interpretation, not in the context of a vagueness challenge. Moreover, the United States Supreme Court has found a constitutional violation from the "chilling effect" of a law only where the law's vagueness would limit rights that are afforded heightened constitutional protection, such as free speech.

<sup>12</sup> In *Nash*, Justice Holmes explained that the constitution's guarantee of fair notice does not equate to perfect notice:

The law is full of instances where a man's fate depends on his estimating rightly, that is, as the jury subsequently estimates it, some matter of degree. If his judgment is wrong, not only may he incur a fine or a short imprisonment, as here; he may incur the penalty of death. . . . The criterion in such cases is to examine whether common social duty would, under the circumstances, have suggested a more circumspect conduct.

[Nash v. United States, 229 U.S. 373, 33 S. Ct. 780, 781-82, 57 L. Ed. 1232 \(1913\)](#).

<sup>13</sup> In construing the DTPA, the supreme court noted the need for [section 17.46\(a\)](#)'s "catch-all" provision:

A broad interpretation is warranted, however, due to human inventiveness in engaging in deceptive or misleading conduct. The legislature did not intend its express purpose of protecting consumers from false trade practices to be circumvented by those who would seek out loopholes in the Act's provisions.

[Pennington v. Singleton, 606 S.W.2d 682, 688, 23 Tex. Sup. Ct. J. 587 \(Tex. 1980\)](#).

See [\*Dombrowski v. Pfister, 380 U.S. 479, 486-87, 14 L. Ed. 2d 22, 85 S. Ct. 1116 \(1965\)\*](#). And even in the area of free speech, the United States Supreme Court has never considered the chilling effect of a law to be a sufficient basis, in and of [\[\\*\\*48\]](#) itself, for prohibiting state action. [\*Younger v. Harris, 401 U.S. 37, 51, 27 L. Ed. 2d 669, 91 S. Ct. 746 \(1971\)\*](#). Thus, we find no support in the decisions of the federal or state supreme courts for the proposition that the WMO Rule is unconstitutionally vague.<sup>14</sup>

**[\*842]** We hold that the WMO Rule's general definition of prohibited activities provides the fair notice required by the constitution. Reading the statute as a whole, we conclude [\[\\*\\*49\]](#) that the broad language in the definition is tempered by the availability of a defense when a market participant has acted in accordance with ERCOT protocols, or has (1) pursued a legitimate business purpose and (2) exercised due diligence to avoid an adverse affect on prices, reliability and accounting. See [\*16 Tex. Admin. Code § 25.503\(h\)\*](#). We overrule Coalition, Texas Genco, TXU, and Occidental's vagueness challenge to the WMO Rule's prohibited activities.

#### ***Market power***

All market participants contend that the Commission's failure to define market power in the WMO Rule renders it unconstitutionally vague. They point to the prohibition of market power abuse, which includes, "withholding of production, whether economic withholding or physical withholding, by a market participant who has market power." [\*16 Tex. Admin. Code 25.503\(g\)\(7\)\*](#). Market participants contend that, without a clear definition of market power, they cannot know if or when they possess market power and, therefore, are uncertain when the rule may apply to their decisions on when to operate generation resources and what price to set. Coral [\[\\*\\*50\]](#) Power gives the example of its generation resources which may provide power to ERCOT or to the Southwest Power Pool (SPP). These resources consist of less than ten percent of the total ERCOT capacity. Coral Power continually decides whether to sell power to ERCOT or SPP based on the expected market price. It argues that, without a definition of market power, it cannot know whether the decision to sell power to SPP rather than ERCOT will be considered withholding and, therefore, a violation under [section 25.503\(g\)\(7\)](#). TXU asserts that the failure to define market power leaves enforcement of the market power abuse rule completely in the Commission's discretion, creating the possibility of arbitrary enforcement. See [\*Coffee City v. Thompson, 535 S.W.2d 758, 763 \(Tex. Civ. App.--Tyler 1976, writ ref'd n.r.e.\)\*](#).

Although the Commission agrees that a definition of market power is needed, it provides some guidance in the preamble to the WMO Rule. The Commission explains that the traditional concepts of market power do not fit the Texas electricity market. 29 Tex. Reg. 1916. It characterizes market power in the wholesale electricity market as a "dynamic phenomenon" and notes [\[\\*\\*51\]](#) that constraints in transmission and reliability often give resource owners "temporary or localized market power." *Id.* The Commission points to similar language in an order by the Federal Energy Regulatory Commission (FERC) in the rulemaking record stating that market participants who normally do not possess market power may exercise market power in instances of extreme supply or demand conditions.

The lack of a well defined concept of market power does produce some uncertainty in the enforcement of the rule. However, [HN27](#)<sup>15</sup> this more fluid concept of market power does not render enforcement of the market power abuse provision so uncertain as to deprive market participants of constitutionally required fair notice. See [\*Boyce Motor Lines, 342 U.S. at 340\*](#) ("no more than a reasonable degree of certainty can be demanded"). Notice is determined by reading the rule in its entirety. As we discussed above, [section 25.503\(h\)](#) of the rule exempts otherwise prohibited conduct when a market participant has acted in accordance with ERCOT protocols or has (1) pursued a legitimate business purpose and (2) exercised due diligence to avoid an adverse affect on prices, reliability and accounting. [\[\\*\\*52\]](#) [\[\\*843\]](#) Thus, the examples brought forward where a market participant would be found to have engaged in prohibited conduct because it was not aware that it possessed market power are

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<sup>14</sup> We also reject the dissent's argument that vagueness in the WMO Rule would "chill competition in a manner inconsistent with the legislature's intent." As we have discussed above, the affirmative defense included in the WMO Rule alleviates much of the complained of uncertainty by giving a market participant guidance that, if it is diligent as to the effects of its actions on the market, the market participant will not be subject to liability under the rule. Nor do we conclude that any remaining uncertainty in the WMO Rule would result in some sort of *de facto* regulation.

misplaced. The rule simply requires market participants to be diligent in avoiding adverse affects on the market. If a diligent inquiry would not reveal the adverse affect of legitimate activity on the market, the activity is excluded from the rule's definition of market power abuse.<sup>15</sup> See *id.*

[\*\*53] The Commission's fluid concept of market power also does not create the possibility of arbitrary enforcement. TXU compares the failure to define market power in the WMO Rule with the ordinance in *Coffee City*, where the issuance of building permits was left to the "arbitrary discretion . . . of the city secretary without any rule or standard to follow." *Coffee City*, 535 S.W.2d at 763. By contrast, the WMO Rule provides detailed guidance on how violations of the rule are to be investigated, see *16 Tex. Admin. Code § 25.503(l)(1-3)*, prosecuted, see *id.* § 25.503(l)(4), and enforced. See *id.* § 22.246 (entitlement to a hearing before administrative law judge). Reading the WMO Rule in its entirety, and in context of other administrative code provisions dealing with enforcement, we conclude that **HN28**<sup>↑</sup>] the absence of a definition of market power does not render the rule unconstitutionally vague. We overrule all market participants' issues concerning the vagueness of the WMO Rule's use of the term market power.

### **Miscellaneous provisions**

A variety of other provisions in the WMO Rule have been challenged as unconstitutionally [\*\*54] vague. The arguments supporting these contentions stem primarily from reading terms in the rule in isolation rather than in the context of the entire rule. See *Reliant Energy*, 62 S.W.3d at 839. We will address each specific contention to determine whether the rule provides the reasonable degree of certainty required by the constitution.

TXU contends that the rule is unconstitutionally vague because it fails to define what sort of conduct constitutes the "economic withholding" that is prohibited in *section 25.503(g)(7)*. TXU recognizes the Commission's discussion of economic withholding in the preamble to the rule but claims that the Commission requires market participants to price power at "marginal cost," an equally undefined term. See 29 Tex. Reg. 1916. We have already held in this opinion that the rule does not "set prices" at marginal cost. The preamble gives an example of economic withholding in which a market participant would bid all or a large portion of its production "at a very high price, regardless of marginal costs." *Id.* The Commission explains that a market participant who has market power can be assured that its artificially high bid will be [\*\*55] selected often enough to compensate for those instances when the bids are not accepted because the market contains a sufficient supply at a reasonable price. *Id.* The prohibition on economic withholding was established to prevent the creation of artificial scarcity of reasonably priced power in the market. Considering the Commission's comments in the preamble, see *Village of Hoffman*, 455 U.S. at 494, and the fact that the [\*844] rule does not set the price of power at marginal cost, we hold that the rule provides reasonable notice of the meaning of economic withholding to avoid vagueness.

Coalition challenges *section 25.503(f)(12)*'s requirement that a market participant "who identifies a provision in the ERCOT procedures that produces an outcome inconsistent with the efficient and reliable operation of the ERCOT-administered markets" call the provision to the attention of the appropriate ERCOT subcommittee. Coalition complains that a market participant may violate the rule simply because it does not share the Commission's evaluation of the intent or effect of a protocol. **HN29**<sup>↑</sup>] The rule defines "efficient operation of the market" as characterized by "the fullest use of competitive [\*\*56] auctions to procure ancillary services, minimal cost socialization, and the most economical utilization of resources, subject to operational and other constraints." *16 Tex. Admin. Code Ann. § 25.503(c)(2)*. This definition certainly provides guidance of what the Commission is seeking. More importantly, the rule does not impose a duty to scour the protocols for inefficiency. There is a duty to report only if a market participant subjectively believes that a procedure produces an outcome inconsistent with the efficient and reliable operation of the market. The provision is not unconstitutionally vague.

<sup>15</sup> Occidental contends that the prohibition on creating "artificial congestion" is unconstitutionally vague because "a market participant cannot create artificial congestion without knowing how others operate their units . . . and that market participants do not always have sufficient knowledge to anticipate the effects the their actions may produce." If, in fact, the market participant lacked access to information which would reveal the possibility of creating congestion, *section 25.503(h)* would exempt the conduct from prosecution as a prohibited activity. See *16 Tex. Admin. Code § 25.503(h)*.

Coalition complains that [section 25.503\(i\)](#) requires market participants to follow official interpretations of ERCOT protocols by ERCOT employees when the Commission may later determine that the official interpretation violates the rule. It contends that provision violates due process by requiring market participants to comply with vague and inconsistent legal requirements. Again we find that the affirmative defense for actions taken with a legitimate business purpose--coupled with the exercise of due diligence as to the effect on reliability, price, and accounting--gives [\[\\*57\]](#) sufficient notice of what conduct may subject market participants to liability. See *id.* [§ 25.503\(h\)](#). Although [subsection \(i\)\(6\)](#) does state that reliance on informal communication with ERCOT staff may not be relied on as an affirmative defense, reliance on an official interpretation by ERCOT would represent diligence under the rule.

Coalition also challenges the WMO Rule's guidance to the Commission in monitoring the activities of market participants as unconstitutionally vague. It points to provisions stating that the Commission will consider, *in monitoring the market*, whether an activity (1) materially reduced competitiveness of the market, including whether the activity unfairly impacted other market participants in a way that restricts competition, or (2) interfered with the efficient operation of the market. See *id.* [§ 25.503\(d\)\(2\), \(4\)](#). Despite the reference to enforcement in the title, [section 25.503\(d\)](#) merely details subjects that the Commission should consider in *monitoring* the market. Because nothing in [section 25.503\(d\)](#) will subject a market participant to punishment, we overrule Coalition's vagueness challenge.

The Commission's rule does not enumerate all [\[\\*58\]](#) of the practices that are prohibited, but the constitution does not require such precision. We hold that [HN30](#)<sup>15</sup> each of the challenged provisions of the Commission's rule, when read in the context of the entire rule, provides reasonable notice of what conduct may be punished and does not invite arbitrary and discriminatory enforcement. See [Village of Hoffman Estates, 455 U.S. at 498](#); [Commission for Lawyer Discipline, 980 S.W.2d at 437](#); [Rooms with a View, 7 S.W.3d at 845](#). We overrule all of the additional vagueness challenges.

#### **[\*845] Unconstitutional Taking**

Coalition and TXU contend that the WMO Rule results in an unconstitutional taking without just compensation. Because this is a direct appeal Coalition and TXU may only challenge the facial validity of the rule: that the rule constitutes an unconstitutional taking in all of its applications. See [Village of Hoffman Estates, 455 U.S. at 494-95](#); [City Pub. Serv. Bd., 96 S.W.3d at 359](#). Both appellants cite language in the rule's preamble which they interpret as requiring a market participant to offer all of its capacity at "marginal cost" under certain circumstances. [\[\\*59\]](#) See [29 Tex. Reg. 1916-17](#). They contend that marginal cost does not encompass the full cost of producing power and therefore the rule results in an unconstitutional taking.

As we explained in our discussion of whether the WMO Rule regulates price and our discussion of economic withholding, the rule does *not* require market participants to sell power at marginal cost. The preamble merely states that offering power at a price substantially above the marginal cost of a producer's least efficient unit, when competing offers are unavailable, is an abuse of market power. [HN31](#)<sup>16</sup> Because we hold that the WMO Rule does not require market participants to sell power at marginal cost, the rule is not an unconstitutional taking in all of its applications.<sup>16</sup> We overrule Coalition and TXU's facial challenge to the rule as an unconstitutional taking.

#### **[\*\*60] COMPLIANCE WITH THE APA**

Coral Power raises two issues contending the Commission failed to comply with the APA. Coral Power contends that the Commission (1) failed to provide adequate notice as required by [sections 2001.024](#) and [.029](#), and (2) failed to substantially comply with [APA section 2001.033](#)'s requirement of a concise restatement of the statutory authority of the rule.

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<sup>16</sup> Counsel for TXU acknowledged at oral argument that a facial challenge would be inappropriate if the rule does not require a market participants to price power at marginal cost.

## Notice and Comment

Coral Power claims that the Commission failed to provide adequate notice that the WMO Rule would define market power to include "local" or "momentary" market power. See 29 Tex. Reg. 1916. It contends that nothing in the Commission's proposed rule indicated that market power would be interpreted outside of traditional notions of that term, and therefore, Coral Power was deprived of the opportunity for meaningful comment. See *Unified Loans, Inc. v. Pettijohn*, 955 S.W.2d 649, 651 (Tex. App.--Austin 1997, no pet.) ("Adequate notice is essential for fairness as well as a meaningful opportunity to comment on a proposed rule.").

The supreme court recently discussed the notice requirements of the APA in *Texas Workers' Compensation Commission v. Patient Advocates of Texas*, 136 S.W.3d 643, 649-50, 47 Tex. Sup. Ct. J. 607 (Tex. 2004). [\*\*61]

The supreme court cited a case from this court in which we held that [HN32](#) proper notice is given when a proposed rule is changed to incorporate comments and "and no new subjects of regulation or persons besides those previously given notice are affected." *Id.* (citing *State Bd. of Ins. v. Deffebach*, 631 S.W.2d 794, 801 (Tex. App.--Austin 1982, writ ref'd n.r.e.)). The supreme court also discussed the federal standard for adequate notice under the federal APA stating that the modified final rule must be a "logical outgrowth" of the proposed rule. *Id.* "Stated differently, if the final rule does not materially alter the issues addressed in the proposed rule, then notice will be deemed sufficient." *Id.* The supreme court concluded that the two standards are consistent:

[\*846] The relevant inquiry under both standards is whether the agency's notice fairly apprises affected parties of the pertinent issues to allow them to comment and participate in the rulemaking process in a meaningful and informed manner.

*Id.*

We hold that [HN33](#) the Commission's proposed rule provided adequate notice of its more fluid concept of market power. The proposed rule contains a section [\*\*62] prohibiting "economic withholding" and defines the term as "an offer of energy or capacity by a market participant in an amount sufficiently large that the market cannot clear without the offer." By defining economic withholding in terms of whether the market can clear without the offer, the Commission indicated that its prohibition on economic withholding would apply regardless of traditional notions of market power. Moreover, Coral Power's own comments in the rulemaking record regarding artificial shortages and withholding of power reflect that it had notice that the rule's provisions might affect it. Because the proposed rule apprised Coral Power that it would be affected, and Coral Power actually participated with meaningful comment, we hold that the Commission satisfied the notice requirements of the APA. See *id.* We overrule Coral Power's first issue concerning compliance with the APA.

## Concise Statement of Statutory Provisions

Coral Power also contends that the Commission failed to provide a concise restatement of its statutory authority to enact the WMO Rule. See *Tex. Gov't Code Ann. § 2001.033(a)(2)* (West 2000). Specifically, it [\*\*63] contends that the only stated purpose for the rule is to ensure reliability of electric power and that the rule oversteps the Commission's statutory powers to do so. Coral Power cites a statement in the third paragraph of the preamble that the new rule is needed to ensure reliability of the markets and power during the transition to a fully competitive market. 29 Tex. Reg. 1899. Based on this one sentence, Coral Power concludes that the Commission's stated authority is limited to its powers to ensure reliability during the transition to competition.

However, the paragraph following the one cited by Coral Power states that the WMO Rule was "proposed as part of the Commission's efforts to adopt competition rules to protect the public interest during the transition to and in the establishment of a fully competitive electric power industry under [Chapter 39](#) of [PURA]." 29 Tex. Reg. 1899. The preamble lists those functions delegated to the commission by the statute:

Among those functions were the adoption and enforcement of rules to ensure customer protections and customer entitlements; the establishment of rules governing ERCOT and oversight of ERCOT activities; the assessment [\*\*64] of market power; and the mitigation of market power abuses.

29 Tex. Reg. 1900. The Commission then concludes that "in order to protect the public interest and to assure that prices are determined by the normal forces of competition, the commission finds that it must adopt this rule governing the enforcement of wholesale electricity markets and ERCOT administered markets." *Id.* Reading the preamble as a whole, we find that the Commission clearly stated that the purpose of the rule extends beyond reliability and includes protecting retail customers by addressing anticompetitive manipulation of the wholesale market.

Furthermore, the statutorily delegated functions listed by the Commission support its authority to enact the rule. Although the Commission does not enumerate the specific provisions in [Chapter 39 of PURA](#) [\*847] that correspond with the delegated functions of ensuring reliability, protecting customers and addressing manipulation of the wholesale market, our review of the statute confirms that the Commission possesses these powers. The authority to ensure reliability is granted by the consumer protections in [PURA sections 39.101\(a\)\(1\)](#) (customer entitled to safe, reliable, [\*\*65] and reasonably priced electricity) and [35.004\(e\)](#) (relating to ancillary services market), and [section 39.151\(d\)](#) (independent organization's procedures shall be consistent with Commission rules regarding reliability). The authority to protect consumers stems from [PURA section 39.101\(a\)\(1\), \(b\)\(6\)](#) (customer entitled to be protected from unfair, misleading, deceptive practices), and (f) (commission shall modify rules to assure at least same quality of service that existed before transition to competition). Finally, the Commission's authority to address manipulation of the wholesale market is found in [PURA section 39.157\(a\)](#) (Commission shall monitor market power and address market power abuse), and through the statute's reliability and consumer protection provisions. Coral Power presents a chart in its brief that outlines why various statutory provisions do not grant the Commission authority to enact the rule. All Coral Power's arguments concerning the scope of the Commission's authority under the statute have been thoroughly discussed and rejected earlier in this opinion. We hold that [HN34](#)[] the Commission complied with the APA by including a concise statement of its statutory authority to promulgate [\*\*66] the rule.

Coral Power also contends that the Commission did not substantially comply with the APA because the Commission's reasoned justification does not demonstrate in a relatively clear and logical fashion that the rule is a reasonable means to a legitimate objective. See [Tex. Gov't Code Ann. § 2001.035](#) (West 2000). Coral Power argues that the rule "far exceeds" the Commission's statutory reliability oversight and enforcement responsibilities. However, Coral Power's argument is premised on the incorrect assumptions that the Commission's only objective in the rule is to ensure reliability and that other statutory provisions do not grant the Commission the authority to enact the rule. We have already held that the purpose of the rule also encompasses protecting consumers and preventing manipulation of the wholesale market. These are legitimate objectives authorized by the statute and Coral Power has not shown how the rule is not a reasonable means of protecting consumers and preventing manipulation of the market. Because the purpose of the WMO Rule extends beyond the objective of ensuring reliability, we overrule Coral Power's final substantial compliance [\*\*67] challenge.

## CONCLUSION

In summary, the appellants and the dissent ignore what the legislature fully recognized when it restructured the state's electricity market: In this transition period, a purely competitive market would not serve the needs of either the utilities or the retail customers. For example, utilities must be allowed to recover their investment costs that might be stranded and not recouped in a market-driven rate structure; transmission and distribution must continue to be regulated to a degree; and the transition to a competitive market must also safeguard retail customers by ensuring "safe, reliable, and reasonably priced electricity." [Chapter 39 of PURA](#) gives the Commission the authority to address market power abuses, to provide reasonably priced ancillary services, to protect utilities from some

losses resulting from deregulation, and to protect the legislatively sanctioned "customer safeguards." **[\*848]**<sup>17</sup> The Commission's enactment of the WMO Rule, giving it oversight of the wholesale market, furthers these combined statutory mandates and thus does not exceed the Commission's authority. Rather than chill competition, this rule reasonably promotes a form of competition **[\*\*68]** most likely to accomplish the goals the legislature envisioned in restructuring the state's electric market.

We hold that (1) the Commission possessed the statutory authority to enact the WMO Rule, (2) the rule as adopted was consistent with the general objectives of the statute, (3) the rule is not unconstitutionally vague, (4) the rule does not constitute an unconstitutional taking, and (5) the Commission substantially complied with the requirements of the APA. Accordingly, we sustain the validity of the WMO Rule as enacted by the Commission.

Bea Ann Smith, Justice

**Dissent by:** Bob Pemberton

## Dissent

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### **DISSENTING OPINION**

Because I believe that the Public Utility Commission's rule, **[\*\*69]** 29 Tex. Reg. 1899 (2004) (to be codified at [16 Tex. Admin. Code § 25.503](#) (Pub. Util. Comm'n)) (Wholesale Market Oversight Rule (WMO Rule)), exceeds the Commission's statutory authority, I respectfully dissent.

The defects in [rule 25.503](#) begin with the absence of an intent requirement--participants in the deregulated wholesale electricity market are at peril of presumed liability based solely on the effects of their competitive conduct, even if inadvertent. [16 Tex. Admin. Code § 25.503\(g\)](#). The core concepts found in [rule 25.503](#) are derived from [section 39.157 of PURA](#). See 29 Tex. Reg. 1905. [Section 39.157](#) requires the Commission to "monitor market power" and maintain oversight over "market power abuses," defined as "practices by persons possessing market power that are unreasonably discriminatory or tend to unreasonably restrict, impair, or reduce the level of competition, including practices that tie unregulated products or services to regulated products or services or unreasonably discriminate in the provision of regulated services," and "include predatory pricing, withholding of production, precluding entry, and **[\*\*70]** collusion." [Tex. Util. Code Ann. § 39.157\(a\)](#) (West Supp. 2004-05). These are familiar antitrust concepts. See, e.g., [Verizon Communications, Inc. v. Law Offices of Curtis V. Trinko, 540 U.S. 398, 124 S. Ct. 872, 878-79, 157 L. Ed. 2d 823 \(2004\)](#); see also [Tex. Util. Code Ann. § 39.157\(a\)](#) (clarifying that subsection did not affect enforcement of state or federal antitrust laws). The code construction act thus compels us to look to [antitrust law](#) when construing [section 39.157](#). [Tex. Govt. Code Ann. § 311.011\(b\)](#) (West 2005) ("words and phrases that have acquired a technical or particular meaning, whether by legislative definition or otherwise, shall be construed accordingly.").<sup>1</sup>

As the majority concedes, [section 39.157](#) implies an intent requirement for proving "market **[\*\*71]** power abuse" under that provision because it employs antitrust concepts that carry with them the implication of an intent element. Slip op. at 14 ("If the authority for this rule was derived only from [section 39.157\(a\)](#) governing 'market power' **[\*849]** abuse,' we would agree that an element of intent is implied."). In adopting a rule that implements the requirements of [section 39.157](#) yet omits the intent requirement implicit in its terms, the Commission exceeds its statutory

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<sup>17</sup> "On or before June 30, 2001, the commission shall modify its current rules regarding customer protections to ensure that at least the same level of customer protection against potential abuses and the same quality of service that exists on December 31, 1999, is maintained in a restructured electric industry." [Sec. 39.101\(f\)](#).

<sup>1</sup> I thus disagree with the majority's dismissal of state and federal antitrust authorities as merely "persuasive." Slip op. at 14 & n.6.

authority. See [State of Texas v. Public Utility Commission of Texas, 131 S.W.3d 314, 321 \(Tex. App.--Austin 2004, pet. denied\)](#) (court to consider whether rule: (1) contravenes specific statutory language; (2) runs counter to general objectives of statute; or (3) imposes additional burdens, conditions, or restrictions in excess of or inconsistent with relevant statutory provisions).

By departing from the requirements of [section 39.157, rule 25.503](#) distorts the legislature's careful balancing of the dual policy goals reflected in the statute, encouraging the innovation and risk-taking of competition while protecting the integrity of market mechanisms. See [Law Offices of Curtis V. Trinko, 124 S. Ct. at 878-79.](#) [\*\*72] Indeed, both [chapter 39 of PURA](#) as a whole and the [Texas Free Enterprise and Antitrust Act](#) seek to balance such interests. Compare [Tex. Util. Code Ann. § 39.001\(a\)](#) (West Supp. 2004-05), with [Tex. Bus. & Com. Code Ann. § 15.04](#) (West 2002); see also [Tex. Gov't Code Ann. § 311.023\(4\)](#) (West 2005) (courts may consider "common law or former statutory provisions, including laws on the same or similar subjects"). The term "market power abuse" in [section 39.157](#), like similar standards employed in the antitrust context, carries with it an unmistakable legislative intent to proscribe a type of conduct only where intent can be proven. See [Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199, 47 L. Ed. 2d 668, 96 S. Ct. 1375 \(1975\)](#); see also [United States v. Grinnell Corp., 384 U.S. 563, 570-71, 16 L. Ed. 2d 778, 86 S. Ct. 1698 \(1966\)](#). Absent an intent requirement, "market power abuse" is rather unclear.<sup>2</sup> The market participants go as far as to urge that the term is unconstitutionally vague, and they are not far off the mark, though we need not reach that issue. The majority, in fact, concedes that "the [\*\*73] lack of a well defined concept of market power does produce some uncertainty in the enforcement of the rule," slip. op. at 32, but dismisses its significance.

In the antitrust context, the Texas Supreme Court has [\*\*74] cautioned that "a vague standard [of predatory pricing] has a chilling effect on business. Business must be able to determine prospectively what price it may legally charge." [Caller-Times Pub. Co. v. Triad Comm., Inc., 826 S.W.2d 576, 581, 35 Tex. Sup. Ct. J. 509 \(Tex. 1992\)](#). Accordingly, the court rejected a subjective intent standard because "a seller cannot predict where it may legally set a price" and "this standard creates a lack of predictability in the law which punishes those who would engage in vigorous competition." *Id.* [Rule 25.503](#)'s "market power abuse" standard suffers similar defects: a market participant cannot predict what competitive conduct on its part could give rise to effects that the Commission deems "abuse" or "withholding." In addition, the enumerated list of prohibited activities is not even exclusive. See [16 Tex. Admin. Code § 25.503\(g\)](#) (term "prohibited [\*850] activity" includes, but is not limited to, enumerated "acts and practices"). Without the balancing factor of an intent requirement, these features of [rule 25.503](#) chill competition in a manner inconsistent with the legislature's intent.<sup>3</sup>

[\*\*75] Further compounding the problem is the burden of proof: market participants are presumed to have violated [rule 25.503](#) if the effect of their competitive activities, even inadvertently, is whatever may constitute "market power abuse." See *id.* Subsection (h) excludes from "prohibited activity" conduct by market participants that "served a legitimate business purpose consistent with prices set by competitive market forces; and that it did not know, and could not reasonably anticipate, that its actions would inflate prices, adversely affect . . . reliability [or] proper accounting." However, this affirmative "defense" applies *only* "if the market entity establishes" it. *Id.* [§ 25.503\(h\)](#).

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<sup>2</sup>The WMO Rule does not define "market power abuse" other than to explain that the term includes "withholding of production, whether economic withholding or physical withholding, by a market participant who has market power, constitutes an abuse of market power." See [16 Tex. Admin. Code Ann. § 25.503\(g\)\(7\)](#). Given the nature of the wholesale electricity market, it is unclear whether or how market participants could ascertain whether they possess "market power" at a given moment amid the myriad, fluid circumstances on the grid, much less conform their conduct to avoid the prohibited effects. Nor is it clear whether or how market participants could ascertain how to avoid committing such other violations as creating "artificial congestion." See *id.* [§ 25.503\(g\)\(1\)](#).

<sup>3</sup>In response to my discussion of *Caller-Times* and federal antitrust cases, the majority inaccurately portrays my arguments and attempts to pigeonhole them as relating to constitutional vagueness issues rather than statutory construction. Slip op. at 29-30. As is apparent above, my arguments concern the proper construction of [section 39.157](#), and respecting the legislature's balancing of interests reflected therein. Having determined that [rule 25.93](#) exceeds the Commission's statutory power, I would not reach the constitutional issues.

The significance of the placement of the burden of proof cannot be underestimated, especially in an administrative proceeding subject only to substantial-evidence review. See [\*Richardson v. City of Pasadena\*, 513 S.W.2d 1, 3, 17 Tex. Sup. Ct. J. 401 \(Tex. 1974\)](#).<sup>4</sup>

[\*\*76] The legislature's philosophical foundation underlying chapter 39 was that "the production and sale of electricity is not a monopoly warranting regulation of rates, operations, and services and that the public interest in competitive electric markets requires that, except for transmission and distribution services and for the recovery of stranded costs, electric services and their prices should be determined by customer choices and the normal forces of competition." [\*Tex. Util. Code Ann § 39.001\(a\)\*](#). To this end, the legislature mandated that regulatory authorities "shall authorize or order competitive rather than regulatory methods to achieve the goals of the chapter to the greatest extent feasible and shall adopt rules and orders that are practical and limited so as to impose the least impact on competition." *Id. § 39.001(d)*. In my view, the Commission, in [\*rule 25.503\*](#), has strayed from these principles, as well as from the language and intent of [\*section 39.157\*](#) in particular. See [\*Railroad Comm'n v. Lone Star Gas Co.\*, 844 S.W.2d 679, 685, 36 Tex. Sup. Ct. J. 436 \(Tex. 1992\)](#) (quoting [\*Gerst v. Oak Cliff Savings & Loan Ass'n\*, 432 S.W.2d 702, 706, 11 Tex. Sup. Ct. J. 490 \(Tex. 1968\)](#)) [\*\*77] ("The determining factor . . . whether . . . a particular administrative agency has exceeded its rule-making powers is that the rule's provisions must be in harmony with the general objectives of the Act involved.").")

Having conceded that the [\*section 39.157\*](#)'s "market power abuse" concept contains an implied intent element, the [\*851] majority posits two alternative statutory bases to support a rule that implements [\*section 39.157\*](#)'s conduct standards yet omits its implied intent element. First, the majority looks to [\*PURA section 39.101\*](#), which requires the Commission to "ensure that retail consumer protections are established that entitle a consumer . . . to safe, reliable, and reasonably priced electricity." [\*Tex. Util. Code Ann. § 39.101\*](#). Second, the majority relies on [\*section 35.004\(e\)\*](#), which requires the Commission to "ensure that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices." *Id. § 35.004(e)*.

Based on their plain language, both provisions are limited in scope. [\*Section 35.004\(e\)\*](#) speaks only to ancillary services, which the parties represent is a small component of the wholesale electricity [\*\*78] market. [\*Section 39.101\*](#) does not speak to the wholesale market at all but only to the *retail* electricity market. Within these limited provisions, the majority nonetheless finds broad-ranging regulatory power. Slip op. at 15-17.

Regarding [\*section 39.101\*](#), the majority acknowledges that the provision is addressed solely to the retail market but extrapolates that because "both the retail and wholesale electric markets should be governed by market forces" and "issues relating to reliability or price in the wholesale market will necessarily be reflected in the retail market," the Commission's power to ensure retail customers "safe, reliable, and reasonably priced electricity" for retail consumers would necessarily permit it to act in the wholesale market. Slip op. at 15-16. Similarly, the majority suggests that because "in the existing competitive wholesale market, scarcity of electric power will be reflected in higher prices throughout the market," its authority under [\*section 35.004\(e\)\*](#) to ensure that ancillary services are available at reasonable prices would permit it broad power to regulate conduct throughout the entire wholesale market. Slip op. at 16. As a matter of statutory construction, [\*\*79] I disagree that [\*section 39.101\*](#) and [\*section 35.004\(e\)\*](#) grant the Commission such broad-ranging regulatory power in the wholesale market. See [\*Reliant Energy v. Public Util. Comm'n\*, 101 S.W.3d at 145](#) (overbroad Commission rule invalid).

Moreover, even if [\*section 39.101\*](#) and [\*35.004\(e\)\*](#) would otherwise confer general power on the Commission to act *in some manner* with regard to wholesale transactions, such an authorization is not limitless--rather, the Commission must act in conformity with the broader statutory objectives and framework of the electricity deregulation statutes.

<sup>4</sup> In such an environment, it is perhaps not surprising that several of the market participants equate [\*rule 25.503\*](#) with back-door price regulation. They contend that uncertainty regarding the nature of competitive conduct that is proscribed, the prospect of sanctions based not on intent but mere effect, and a "guilty until proven innocent" burden of proof has compelled them to cling to any guidance they could discern from the rule, such as the Commission's reference to marginal cost pricing in the preamble to the rule. See 29 Tex. Reg. 1899, 1916 (2004) (to be codified at [\*16 Tex. Admin. Code § 25.503\*](#) (Pub. Util. Comm'n)) ("Pricing in excess of marginal cost by a seller who is immune from the chastening hand of competition is an abuse of market power.").

Were it otherwise, the Commission's general duties to ensure "safe, reliable, and reasonably priced electricity" in the retail market, as contemplated in [section 39.101](#), and that ancillary services are available at "reasonable prices," per [section 35.004\(e\)](#), could be invoked to justify virtually any manner of regulation (including that of prices) if, in the Commission's judgment, such actions would ensure "reliability" and "reasonable prices." The limitation that prevents such measures lies not within the terms of [sections 39.101](#) or [35.004\(e\)](#) but in the overall structure and general objectives of [\*80] electricity deregulation legislation<sup>5</sup> and the legislature's explicit mandate that "regulatory authorities . . . shall authorize or order competitive rather than regulatory methods to achieve the goals of the chapter to the greatest extent feasible and shall adopt rules and orders that are practical [\*852] and limited so as to impose the least impact on competition." [Tex. Util. Code Ann. §§ 39.001\(a\), \(c\)](#); see [State of Texas v. Public Utility Commission of Texas](#), 131 S.W.3d 314 at 321 (rule invalid if it contravenes specific statutory language or runs counter to general objectives of statute); see also [Railroad Comm'n v. Lone Star Gas Co.](#), 844 S.W.2d 679, 685, 36 Tex. Sup. Ct. J. 436 (Tex. 1992) (determining factor whether particular administrative agency has exceeded its rule-making powers is "that the rule's provisions must be in harmony with the general objectives of the Act involved."). The majority overlooks the context of [sections 39.101](#) and [35.004\(e\)](#) within the statutory framework.

[\*\*81] Beyond the majority's reliance on [sections 39.101](#) and [35.004\(e\)](#), it continually returns to the notion that Commission members and staff are experts to whose decisions we should defer. It couples this deference with policy observations to the effect that "electricity is different." I concede that the Commission has expertise regarding the behavior of the Texas electricity market and that the legislature intended it to have some flexibility in effectuating its statutory duties. However, even if the legislature intends that an agency created to centralize expertise in a certain regulatory area "be given a large degree of latitude in the methods it uses to accomplish its regulatory function," [Texas Mun. Power Agency v. Public Util. Comm'n](#), 150 S.W.3d 579, 586 (Tex. App.--Austin 2004, pet. filed), an agency may not, in the guise of implied powers, exercise what is effectively a new power on the theory that such exercise is expedient for the agency's purpose, [Public Util. Comm'n v. GTE-Southwest, Inc.](#), 901 S.W.2d 401, 407, 38 Tex. Sup. Ct. J. 485 (Tex. 1995), nor may it contravene specific statutory language, run counter to the general objectives of the statute, or impose additional [\*82] burdens, conditions, or restrictions in excess of or inconsistent with the relevant statutory provisions. [State v. Public Util. Comm'n](#), 131 S.W.3d at 321.

I also recognize the unique nature of electricity as a commodity, which can create some conceptual challenges when applying antitrust or other economic concepts. However, nothing about the nature of electricity suggests that we should construe Commission statutory power more broadly than the terms of those enactments would otherwise provide. The legislature was aware of the unique nature of electricity when it deregulated the industry, enacted its competition mandates in chapter 39, and employed antitrust concepts in the standards it chose to govern the wholesale marketplace. Those standards should govern our analysis of the Commission's power here and, in my view, compel us to invalidate [rule 25.93](#).

Finally, by reaching such a conclusion, I do not, as the majority accuses, "ignore" legislative intent to protect consumer welfare in a deregulated electricity market, much less suggest that consumer protection is not a statutory goal. To the contrary, our duty is to faithfully follow the legislature's intent to advance [\*83] consumer welfare, but we should not lose sight of the legislature's overarching policy judgment that consumer welfare is ordinarily best advanced by vigorously competitive retail and wholesale electricity markets rather than by regulation. See [Tex. Util. Code Ann. § 39.001\(a\) & \(d\)](#). And, where, as in [section 39.157](#), the legislature has carefully and precisely balanced competing considerations in its pursuit of consumer welfare--preventing market abuses without causing what it views as too great a chilling effect on competition--we should be faithful to its judgment and ensure that the Commission's rules are in conformity.

For these reasons, I respectfully dissent.

Bob Pemberton, Justice

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<sup>5</sup> The legislature enacted [section 35.004\(e\)](#) as part of the 1999 electricity deregulation bill. See Act of May 27, 1999, 76th Leg., R.S., ch. 405, §§ 17, 39, 1999 Tex. Gen. Laws 2543, 2552, 2558-2602.

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## Xcaliber Int'l Ltd., LLC v. Edmondson

United States District Court for the Northern District of Oklahoma

May 20, 2005, Decided ; May 20, 2005, Filed

Case No. 04-CV-0922-CVE-PJC

### **Reporter**

2005 U.S. Dist. LEXIS 26705 \*; 2005 WL 5654220

XCALIBER INTERNATIONAL LIMITED, LLC, and KT&G CORP., Plaintiffs, v. W.A. DREW EDMONDSON, in his official capacity as Attorney General, State of Oklahoma, Defendant.

**Subsequent History:** Reconsideration denied by [Xcaliber Int'l Ltd., LLC v. Edmondson, 2005 U.S. Dist. LEXIS 40448 \(N.D. Okla., Aug. 31, 2005\)](#)

Affirmed by [KT&G Corp. v. AG of Okla., 2008 U.S. App. LEXIS 16190 \(10th Cir. Okla., July 23, 2008\)](#)

**Prior History:** [Xcaliber Int'l Ltd., LLC v. Edmondson, 2005 U.S. Dist. LEXIS 43890 \(N.D. Okla., Apr. 5, 2005\)](#)

## **Core Terms**

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allocable share, manufacturers, market share, escrow, antitrust, cigarette, summary judgment, costs, private party, Sherman Act, Participating, plaintiffs', advertisements, cartel, state action, price-fixing, settlement, tobacco, exempt, output, prices, join

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Regulated Practices > Private Actions

Antitrust & Trade Law > Regulated Practices > Private Actions > Remedies

### [HN1](#) **Regulated Practices, Private Actions**

To bring an antitrust claim for injunctive relief, private plaintiffs must show, above and beyond the constitutional case or controversy requirements: (1) that the acts violating the antitrust laws threatened to cause those plaintiffs injury in fact to their business or property; (2) that that injury is not too remote or duplicative of the recovery of a more directly injured person; and (3) that such injury is antitrust injury, which is defined as the kind of injury that the antitrust laws were intended to prevent and flows from that which makes the defendants' acts unlawful.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

### [HN2](#) **Summary Judgment, Entitlement as Matter of Law**

Summary judgment pursuant to [Fed. R. Civ. P. 56](#) is appropriate where there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. The plain language of [Fed. R. Civ. P. 56\(c\)](#) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial. Summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to secure the just, speedy and inexpensive determination of every action.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

### [HN3](#) Summary Judgment, Burdens of Proof

When the moving party has carried its burden under [Fed. R. Civ. P. 56\(c\)](#), its opponent must do more than simply show that there is some metaphysical doubt as to the material facts. Where the record taken as a whole could not lead a rational trier of fact to find for the non-moving party, there is no genuine issue for trial. The mere existence of a scintilla of evidence in support of a non-moving plaintiff's position will be insufficient; there must be evidence on which the trier of fact could reasonably find for the plaintiff. In essence, the inquiry for the court is whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law. In its review, the court construes the record in the light most favorable to the party opposing summary judgment.

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Antitrust & Trade Law > Sherman Act

### [HN4](#) Scope, Exemptions

The Sherman Act, [15 U.S.C.S. § 1 et seq.](#), prohibits private parties from entering into agreements, combinations, or conspiracies in unreasonable restraint of trade, but does not prohibit a state from directly imposing restraints on competition in the exercise of its police and regulatory powers. A state legislature may set prices or control output; it simply may not authorize or require private parties to do so. If there has been no delegation of regulatory authority to private parties, the state action is "ipso facto" immune from antitrust challenge and so, not subject to preemption. Further, where a state does not authorize or require a party to engage in private or hybrid conduct that would violate antitrust laws, Midcal analysis is not required.

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Antitrust & Trade Law > Sherman Act

Antitrust & Trade Law > Sherman Act > Scope > General Overview

### [HN5](#) Scope, Exemptions

Because the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), does not prohibit state governments from directly imposing restraints on competition in the exercise of their police and regulatory powers, to prevail on a preemption claim under the Sherman Act, a plaintiff must show that it is injured by a hybrid restraint, which is defined as a government action delegating regulatory power to private parties so that they can enforce their own private market decisions.

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

## **HN6** Scope, Exemptions

A state's unstated motive in enacting legislation is irrelevant. State action is exempt from antitrust liability regardless of the state's motives in taking the action. As long as the conduct causing anticompetitive effect is unilateral state action, taken under that state's police powers, it is protected from preemption by the state action doctrine.

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For Attorney General of the State of Oklahoma, WA. Drew Edmondson, in his official capacity as Attorney General, W A Edmondson, Defendant: Gary D Wilson, WASHINGTON, DC; Guy Lee Hurst, Office of the Attorney General (OKC-4545), OKLAHOMA CITY, [\*2] OK; Mark Greenwold, National Association of Attorneys General, WASHINGTON, DC; Mark Lawton Jones Office of the Attorney General (OKC-4545) OKLAHOMA CITY, OK; Peter J Levin, National Association of Attorneys General, WASHINGTON, DC; Susan K Noland, Office of the Attorney General (OKC-4545), OKLAHOMA CITY, OK.

**Judges:** CLAIRE V. EAGAN, CHIEF JUDGE.

**Opinion by:** CLAIRE V. EAGAN

## **Opinion**

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### **ORDER**

Now before the Court are the motion and amended motion for summary judgment (Dkt. ## 79 and 124)<sup>1</sup> filed by the defendant W. A. Drew Edmondson, Attorney General of the State of Oklahoma ("Attorney General"), as to the antitrust claim brought against him by plaintiffs Xcaliber International Limited, LLC ("Xcaliber") and KT&G Corp. ("KT&G").

### **[\*3] I.**

Plaintiffs Xcaliber and KT&G each manufacture tobacco products that are distributed in Oklahoma. In the mid-1990s, several states sued major tobacco manufacturers to recover costs incurred through the treatment of

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<sup>1</sup> The amended motion (Dkt. # 124) was submitted before plaintiffs' response was filed, but only officially filed thereafter. The amended motion is not substantively changed from the original, only correcting citation problems. The response was filed with reference to the original motion; the reply was originally filed with reference to the amended motion. The sur-reply was filed with reference to both. The Court will therefore address both.

smoking-related diseases as a result of the manufacturers' marketing practices and violations of consumer protection, antitrust, and various state laws. These suits were settled by the execution of a Master Settlement Agreement ("MSA") in 1998. This agreement was signed by fifty-two governmental jurisdictions: 46 states (including Oklahoma), the District of Columbia, Puerto Rico, and four territories, now designated by the MSA as "Settling States." The manufacturer signatories of the MSA were Phillip Morris, Lorillard, Brown & Williamson, and R.J. Reynolds, collectively referred to as the "Original Participating Manufacturers" ("OPMs").

Under the terms of the MSA, the Settling States agreed to release their claims against the OPMs in return for annual payments, the amount of which is specified in the MSA and adjusts for changes in the overall volume of cigarette sales. Each manufacturer's responsibility for these payments is based principally on its own market [\*4] share. The annual payment is allocated among the Settling States according to a fixed formula. Oklahoma's allocable share under the MSA is 1.036137% of the total national payments. The MSA also prohibits PMs from political lobbying, restricts their trade association activities, and forces them to relinquish legal challenges to state laws regulating tobacco. It also contains a variety of prohibitions on advertising and promotional activities, such as advertisements aimed at the youth market, outdoor advertisements, transit advertisements, and advertisements containing cartoons.

The MSA also includes a provision permitting other cigarette manufacturers to join the agreement. Those who joined within 90 days of the MSA's execution date are exempt from annual MSA payments, provided their yearly market shares do not exceed their 1998 levels or 125% of their 1997 levels. Other manufacturers who become "Subsequent Participating Manufacturers" ("SPMs") after the expiration of that period do not benefit from this exemption. Both exempt and non-exempt SPMs are bound by the advertising and other restrictions of the MSA. Non-exempt SPMs make payments to the Settling States based on the numbers [\*5] of cigarettes they sell. OPMs and SPMs are collectively referred to as "Participating Manufacturers" ("PMs"). Manufacturers declining to join the MSA are referred to as "Non-Participating Manufacturers" ("NPMs").

The terms of the MSA also anticipate changes in market share resulting from the activity of NPMs. Loss of OPM market share to NPMs generally trebles the decrease in payment obligations by OPMs when a loss of more than two percent results from a "disadvantage" arising from the MSA's terms, such as price competition from NPMs (cause of market share loss is determined by a national economic consulting firm). Such changes in market share would result in a significant loss in tobacco settlement revenue by the Settling State. Under the MSA, a Settling State may immunize itself from that loss by enacting and enforcing a form Escrow Statute which requires NPMs distributing in that state either to join the MSA as SPMs and make future settlement payments accordingly, or to make regular deposits based on their cigarette sales into a rolling escrow account. Oklahoma has enacted such a statute ("Escrow Statute") codified at [Okla. Stat. tit. 37, § 600.21 et seq.](#)

The escrow payments [\*6] made under the Oklahoma Escrow Statute are either to be released to the state in satisfaction of any judgment or settlement obtained against that manufacturer in a suit brought by the state, or returned to the NPM after twenty-five (25) years. The original statute also provided for an immediate refund of any amount paid into escrow greater than the allocable share Oklahoma would have received had the NPM been a PM. This is referred to as the "Allocable Share Release Provision" ([Okla. Stat. tit. 37, § 600.23\(B\)\(2\)](#) (2001)) and was intended to create an equivalence between the NPMs' escrow obligation under the escrow statute and their hypothetical payment obligations under the MSA had they been PMs.

The Attorney General contends that this original version of the statute created an unintended loophole. The statute operated as intended only if the NPMs distributed their products nationally because then the total escrow obligation to all states with similar tobacco statutes would approximate the total payments those NPMs would have made under the MSA. However, if an NPM concentrated its sales in only a few states, especially if those states had small allocable share percentages, as [\*7] does Oklahoma, that NPM could recoup the majority of its escrow payments through the Allocable Share Release Provision. For example, an NPM selling cigarettes only in Oklahoma was able to obtain a release of nearly ninety-nine (99) percent of its escrow payments, and would have no escrow obligation to any other state.

To remedy this unintended consequence, in 2003, Oklahoma enacted the Allocable Share Amendment, which went into effect on January 1, 2005. Under the amended statute, releases may be obtained only for amounts in excess of the MSA payments a given NPM would have been required to make as a PM on account of the number of cigarettes sold in Oklahoma, without reference to Oklahoma's MSA allocable share. For an NPM concentrating its sales in Oklahoma, this means significantly smaller releases of escrow payments than under the original provision.

Plaintiffs allege that the effect of the amendment is not only to prevent them from competing against PMs, but to drive them out of business altogether. Xcaliber and KT&G filed suit against the Attorney General on December 10, 2004, challenging the amended statute on antitrust grounds, alleging that it supports a price-fixing scheme [\*8] and an output cartel among the PMs (who are private parties), which is illegal per se under section 1 of the Sherman Act ([15 U.S.C. § 1](#)), and which has caused irreparable damage to their business and property.

The Attorney General moves for summary judgment on the grounds that: (1) the Allocable Share Amendment is not preempted because it is state action that neither mandates nor authorizes private parties to commit a per se violation of the Sherman Act; and (2) plaintiffs cannot prevail by claiming that the effect of the Allocable Share Amendment is to establish an output cartel and price-fixing scheme by MSA participating manufacturers because (a) plaintiffs lack legal interest or standing to challenge the MSA <sup>2</sup> and (b) the undisputed facts establish that nothing in the MSA or the implementing statutes operates to support or establish such a cartel, or any other hybrid restraint on competition, leaving the Allocable Share Amendment immune from antitrust scrutiny under the state action doctrine.

## [\*9] II.

**HN2** [↑] Summary judgment pursuant to [Fed. R. Civ. P. 56](#) is appropriate where there is no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. [Celotex Corp. v. Catrett](#), 477 U.S. 317, 322-23, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986); [Anderson v. Liberty Lobby, Inc.](#), 477 U.S. 242, 250, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986); [Kendall v. Watkins](#), 998 F.2d 848, 850 (10th Cir. 1993). The plain language of [Rule 56\(c\)](#) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient to establish the existence of an element essential to that party's case, and on which that party will bear the burden of proof at trial. [Celotex](#), 477 U.S. at 317. "Summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed 'to secure the just, speedy and inexpensive determination of every action.'" [Id. at 327](#).

**HN3** [↑] "When the moving party has carried its burden under [Rule 56\(c\)](#), its opponent must do more than simply show that [\*10] there is some metaphysical doubt as to the material facts. ... Where the record taken as a whole could not lead a rational trier of fact to find for the non-moving party, there is no 'genuine issue for trial.'" [Matsushita Elec. Indus. Co. v. Zenith Radio Corp.](#), 475 U.S. 574, 586-87, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986) (citations omitted). "The mere existence of a scintilla of evidence in support of the plaintiff's position will be insufficient; there must be evidence on which the [trier of fact] could reasonably find for the plaintiff." [Anderson](#), 477 U.S. at 252. In essence, the inquiry for the Court is "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law." [Id. at 250](#). In its review, the

<sup>2</sup> **HN1** [↑] To bring an antitrust claim for injunctive relief, private plaintiffs must show, above and beyond the constitutional case or controversy requirements, "(1) that the acts violating the antitrust laws ... threatened to cause [those plaintiffs] injury in fact to [their] business or property; (2) that this injury is not too remote or duplicative of the recovery of a more directly injured person; [and] (3) that such injury is antitrust injury,' which is defined as the kind of injury that the antitrust laws were intended to prevent and flows from that which makes defendants' acts unlawful." 2 Phillip E. Areeda et al., [Antitrust Law](#) P335a (2d ed. 2000) (quoting [Brunswick Corp. v. Pueblo Bowl-O-Mat](#), 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977)); see also [Full Draw Prods. v. Easton Sports, Inc.](#), 182 F.3d 745, 750 (10th Cir. 1999); [Sports Racing Servs., Inc. v. Sports Car Club of Am., Inc.](#), 131 F.3d 874 (10th Cir. 1997); [City of Chanute, Kan. v. Williams Natural Gas Co.](#), 955 F.2d 641, 652 (10th Cir. 1992). Plaintiffs' complaint sufficiently alleged both antitrust injury and causal connection to withstand a motion to dismiss. However, at this stage, the Court must address the merits of plaintiffs' allegations of antitrust injury before proceeding with standing analysis.

Court construes the record in the light most favorable to the party opposing summary judgment. *Garratt v. Walker*, 164 F.3d 1249, 1251 (10th Cir. 1998).

### III.

Defendant first argues that Oklahoma's Allocable Share Amendment is not preempted because it is state action that does not "compel or permit -- either expressly or impliedly [\*11] -- any private party to engage in any type of anti-competitive conduct." Defendant's Amended Motion (Dkt. # 124), at 7. For the most part, this argument has already been addressed by the Court's order of April 5, 2005 in connection with defendant's motion to dismiss, wherein the Court found that the Allocable Share Amendment "does not, on its face, mandate or authorize antitrust violations, nor place irresistible pressure on private parties to violate antitrust laws." Order (Dkt. # 103) at 14.

Nonetheless, plaintiffs have argued that raising costs for PM competitors (NPMs) constitutes a per se violation of **antitrust law**.<sup>3</sup> As the Court noted its April 5, 2005 order, the Sherman Act [HN4](#) prohibits private parties from entering into agreements, combinations, or conspiracies in unreasonable restraint of trade, but does not prohibit a state from directly imposing restraints on competition in the exercise of its police and regulatory powers. See *Parker v. Brown*, 317 U.S. 341, 350-51, 63 S. Ct. 307, 87 L. Ed. 315 (1943). A state legislature may set prices or control output; it simply may not authorize or require private parties to do so. *Id.*; see also *F.T.C. v. Ticor Title Ins. Co.*, 504 U.S. 621, 632-33, 112 S. Ct. 2169, 119 L. Ed. 2d 410 (1992). [\*12] Although plaintiffs assert that "the Amended Statute grants Participating Manufacturers (OPMs and SPMs) additional power to increase their prices by imposing costs on their NPM competitors without any semblance of effective state supervision," in fact, the statute directly sets the cost increase, capping it at the level of MSA-imposed costs. This, as a unilateral state action, makes state supervision a non-issue. Private cigarette manufacturers, PMs, have no control or discretion over the setting of these NPM costs.

[\*13] Accordingly, the Court reiterates that, standing alone, the Allocable Share Amendment is not preempted by the Sherman Act. However, consideration of the Allocable Share Amendment within the context of the MSA and its implementing legislation could produce a different result, and so the Court proceeds with an analysis of the alleged anticompetitive effect.

### IV.

Defendant moves for summary judgment on the ground that plaintiffs cannot prevail by claiming that the effect of the Allocable Share Amendment is to support an output cartel and price-fixing scheme by MSA participating manufacturers because nothing in the MSA establishes such an alleged cartel. In fact, they argue, (1) the undisputed facts establish that nothing in the MSA-related statutes operates to effect anything that could be claimed to be a hybrid restraint; and (2) there is no other authority supporting plaintiffs' claim of preemption.<sup>4</sup>

<sup>3</sup> Plaintiffs cite *United States v. Socony Vacuum Oil Co.*, 310 U.S. 150, 221-223, 60 S. Ct. 811, 84 L. Ed. 1129 (1940), for the proposition that the Sherman Act condemns any agreement or state legislation that raises, depresses, fixes, pegs, or stabilizes the price of a commodity. Plaintiff's Response (Dkt. # 114), at 14 (emphasis added). However, *Socony Vacuum* was the criminal prosecution of an oil company and others under [Section 1](#) of the Sherman Act and dealt only with private action. Similarly, the other cases cited in plaintiffs' response and surreply briefs to support the argument that raising rivals' costs is a per se violation involve only private action. See *United States v. Andreas*, 216 F.3d 645 (7th Cir. 2000); *Gen. Leaseways, Inc. v. Nat'l Truck Leasing Assn.*, 744 F.2d 588 (7th Cir. 1984); *Nat'l Soc'y. of Prof'l Eng'r's v. United States*, 435 U.S. 679, 98 S. Ct. 1355, 55 L. Ed. 2d 637 (1978).

<sup>4</sup> Defendant also argues that (1) there is no basis for evaluating the MSA or Allocable Share Amendment under the rule of reason; and (2) even if the analysis laid out in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97, 105, 100 S. Ct. 937, 63 L. Ed. 2d 233 (1980), were applied, state supervision of the only conduct required or authorized by the statute -- payment of statutorily specified amounts into escrow--would prevent any challenge to the Allocable Share Amendment.

[\*14] [HN5](#) Because the Sherman Act does not prohibit state governments from directly imposing restraints on competition in the exercise of their police and regulatory powers, to prevail on a preemption claim under the Sherman Act, a plaintiff must show that it is injured by a hybrid restraint, which is defined as a government action delegating regulatory power to private parties so that they can enforce their own private market decisions. See [324 Liquor Corp. v. Duffy, 479 U.S. 335, 345-46, 107 S. Ct. 720, 93 L. Ed. 2d 667 \(1987\)](#); [Fisher v. City of Berkeley, 475 U.S. 260, 268, 106 S. Ct. 1045, 89 L. Ed. 2d 206 \(1986\)](#); [Rice v. Norman Williams Co., 458 U.S. 654, 665, 102 S. Ct. 3294, 73 L. Ed. 2d 1042 \(1982\)](#) (Stevens, J., concurring); [Parker, 317 U.S. at 350-51](#). Accordingly, the Court must now determine whether any such power has been delegated to PMs, through the enactment of the Allocable Share Amendment, to enforce their own private market decisions about cigarette pricing.<sup>5</sup>

[\*15] Plaintiffs argue that the anticompetitive effects of the Allocable Share Amendment arise out of its alleged effective enforcement of an MSA scheme changing the competitive equilibrium in the cigarette market. Plaintiffs cite the conclusion of the Third Circuit that "the penalty of higher settlement payments for increased market share [has discouraged] reducing prices ... [and instead created for MSA signatories] an incentive to raise prices to match increases by competitors." Plaintiff's Response (Dkt. # 114), at 18 (quoting [A.D. Bedell Wholesale Co. v. Philip Morris Inc., 263 F.3d 239, 248 \(3d Cir. 2001\)](#)). They allege the same cartel in this case.

However, there is no evidence that the MSAA incorporates penalties for increased market share by any class of PM which would serve to effect a market-sharing or price-fixing agreement. There is no provision in the MSA, nor any evidence in the summary judgment record, to support the claim that OPM or non-exempt SPM payments for increased market share would be in any way disproportionate to the payments they made based on the market share they had upon joining the MSA. See MSA, Part IX; Defendant's Amended Motion [\*16] (Dkt. # 124), Ex. 4, Report of Jonathan Gruber, P 10. Although there is certainly a sharp rise in payments for exempt SPMs who exceed their grandfathered market share, the evidence in the summary judgment record indicates that the amount they pay at that point is not disproportionate when compared to the payments made all along by non-exempt SPMs, and so does not act as a penalty. MSA, Part IX(i); Defendant's Amended Motion (Dkt. # 124), Ex. 4, Report of Jonathan Gruber, P43; *Id.*, Ex. 15, Report of Jeremy Bulow, P50; Plaintiffs' Response (Dkt. # 114), Ex. A, Deposition of Jeremy Bulow, at 68,11.8-16. Further, both experts agree that as long as their marginal costs are still lower than their marginal revenues, all of these manufacturers will continue to produce regardless of changes in their relative market shares. Plaintiffs' Response (Dkt. # 114), Ex. A, Deposition of Jeremy Bulow, at 13, 11. 2-25; *Id.* at 68,11.8-16; Defendant's Amended Motion (Dkt. # 124), Ex. 4, Report of Jonathan Gruber, P51. According to both experts, each manufacturer makes a unilateral decision as to price and output in light of the costs imposed by the MSA and its implementing legislation, including [\*17] the Allocable Share Amendment.<sup>6</sup> Defendant's Amended

If there has been no delegation of regulatory authority to private parties, the state action is "ipso facto" immune from antitrust challenge and so, not subject to preemption. [Hoover v. Ronwin, 466 U.S. 558, 567-68, 104 S. Ct. 1989, 80 L. Ed. 2d 590 \(1984\)](#). Further, where a state does not authorize or require a party to engage in private or hybrid conduct that would violate antitrust laws, *Midcal* analysis is not required. [Massachusetts Food Ass'n v. Massachusetts Alcoholic Beverages Control Comm'n, 197 F.3d 560 \(1st Cir. 1999\)](#). Accordingly, because the Court has found no hybrid restraint, nor any other manner in which the Allocable Share Amendment serves to enforce an private decision to restrain competition, it does not reach either of these arguments.

<sup>5</sup> Although plaintiffs, in their surreply, assert that the Court has found the Allocable Share Amendment serves to enforce the MSA, obviating the need for private parties to act to create an anticompetitive scheme, plaintiffs have overstated the Court's order addressing defendant's motion to dismiss. By its nature, an order addressing a motion to dismiss makes no finding as to the merits of a case. The sole purpose of such an order is to determine whether the allegations of a plaintiff's complaint sufficiently support a claim for relief. The Court found that the allegations supported an antitrust claim, not that the allegations had been proved.

<sup>6</sup> Although plaintiffs point to the Allocable Share Amendment's imposition of higher costs upon NPMs, and their resultant increase in prices, the fact that the higher costs may affect NPM decisions about where to distribute their cigarettes or lessen their competitive advantage as against PMs has no bearing on antitrust analysis as long as there is no private or hybrid restraint. So, although these facts may be disputed, they do not create a genuine issue of material fact as to plaintiffs' antitrust claim.

Motion (Dkt. # 124), Ex. 4, Report of Jonathan Gruber, PP10, 51; Plaintiffs' Response (Dkt. # 114), Ex. A, Deposition of Jeremy Bulow, at 18,11.4-8.

For these reasons, although the Allocable Share Amendment may be said to lessen the competitive threat of NPMs for PMs by narrowing the gap created by MSA-imposed costs, it cannot be said to serve to enforce any market-sharing or price-fixing agreement among manufacturers, or any other private decision to [\*18] restrain competition.<sup>7</sup> The Allocable Share Amendment cannot be said to create or constitute either a private or a hybrid restraint. It is therefore protected from antitrust scrutiny by the state action doctrine.

## V.

Finally, plaintiffs have presented an abundance of evidence that the actual purpose, and perhaps even the effect, of the Allocable Share Amendment, is to protect the market share of participating manufacturers and to drive NPMs [\*19] out of business, rather than to advance the public health and safety goals contemplated by the MSA. However, HN6[<sup>8</sup>] a state's unstated motive in enacting legislation is irrelevant. See *City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 379, 111 S. Ct. 1344, 113 L. Ed. 2d 382 (1991) (rejecting an interpretation of the Sherman Act "that would allow Plaintiffs to look behind the actions of state sovereigns to base their claims on 'perceived conspiracies to restrain trade'"); *Hoover v. Ronwin*, 466 U.S. 558, 580, 104 S. Ct. 1989, 80 L. Ed. 2d 590 (1984) (state action is "exempt from antitrust liability regardless of the State's motives in taking the action"). As long as the conduct causing anticompetitive effect is unilateral state action, taken under that state's police powers, as discussed above, it is protected from preemption by the state action doctrine.

## VI.

**IT IS THEREFORE ORDERED** that defendant's motion for summary judgment (Dkt. ## 79 and 124) is hereby granted.<sup>8</sup>

[\*20] Dated this 20th day of May, 2005.

CLAIRES V. EAGAN, CHIEF JUDGE

UNITED STATES DISTRICT COURT

## **JUDGMENT**

This matter has come before the Court for consideration and an Order granting summary judgment in favor of the defendant has been entered as to plaintiffs' antitrust claim. The Order resolved all remaining issues in this case, leaving nothing to be litigated.

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<sup>7</sup> Although plaintiffs have pointed to the *Bedell* court's recognition of OPM lock-step price increases following the initial enactment of the MSA implementing legislation and to the OPMs' similar substantial price increases in January 2005, they have offered no evidence, other than temporal proximity, supporting a causal connection between these later price increases and the Allocable Share Amendment. This, in light of the expert testimony that PMs make their output and pricing decisions unilaterally, is insufficient to raise a genuine issue of material fact.

<sup>8</sup> Because the Court has found no Sherman Act violation, and so no antitrust injury, it grants summary judgment based on state action immunity and does not reach the remainder of the standing analysis discussed in note 2 *supra*.

In the briefing related to the motion for preliminary injunction, plaintiffs also claim to seek an injunction against enforcement of any associated tax regulations intended to be applied in connection with the Allocable Share provision. Because the Court has dismissed constitutional challenges to the amended escrow statute, and granted summary judgment as to the antitrust claim, the issue of the tax regulations is moot.

**IT IS THEREFORE ORDERED, ADJUDGED AND DECREED** that judgment is hereby entered for the defendant W.A. Drew Edmondson, in his official capacity as Attorney General, State of Oklahoma and against plaintiffs' Xcaliber International Limited, LLC and KT&G Corporation pursuant to the Court's Order on plaintiffs' antitrust claim.

Dated this 20th day of May, 2005.

CLAIRE V. EAGAN, CHIEF JUDGE

UNITED STATES DISTRICT COURT

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## **California ex rel. Lockyer v. Safeway, Inc.**

United States District Court for the Central District of California

May 25, 2005, Decided ; May 25, 2005, Filed

No. CV 04-0687-GHK(SSx)

### **Reporter**

371 F. Supp. 2d 1179 \*; 2005 U.S. Dist. LEXIS 10572 \*\*; 177 L.R.R.M. 2674; 2005-1 Trade Cas. (CCH) P74,805

STATE OF CALIFORNIA, ex rel. BILL LOCKYER, Plaintiff, vs. SAFEWAY, INC., dba Vons, a Safeway Company, ALBERTSON'S, INC., RALPHS GROCERY COMPANY, a division of the Kroger Company, FOOD 4 LESS FOOD COMPANY, a division of the Kroger Company, and DOES 1 through 100, inclusive, Defendants.

**Subsequent History:** Summary judgment denied by [California v. Safeway, 2008 U.S. Dist. LEXIS 120337 \(C.D. Cal., Mar. 6, 2008\)](#)

**Prior History:** [California ex rel. Lockyer v. Safeway, Inc., 355 F. Supp. 2d 1111, 2005 U.S. Dist. LEXIS 2744 \(C.D. Cal., 2005\)](#)

## **Core Terms**

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exemption, negotiations, nonstatutory, antitrust, lockout, collective bargaining, Supermarkets, parties, revenue sharing, Sales, multiemployer, anti trust law, Sherman Act, revenue-sharing, collective bargaining process, bargaining unit, labor dispute, bargaining, labor law, commerce, immune, competitor, tail, national labor policy, collective-bargaining, bargaining process, provisions, employees, Redistribution, pre-strike

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Evidence > Burdens of Proof > Allocation

Civil Procedure > Judgments > Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

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Civil Procedure > ... > Summary Judgment > Supporting Materials > Discovery Materials

Civil Procedure > Trials > Judgment as Matter of Law > General Overview

Civil Procedure > Trials > Judgment as Matter of Law > Directed Verdicts

Evidence > Burdens of Proof > General Overview

## **HN1**[ **Entitlement as Matter of Law, Genuine Disputes**

A court may grant summary judgment only if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#). Defendants, having raised the nonstatutory labor exemption as an affirmative defense, bear the burden of proof on this defense at trial. To be entitled to summary judgment, a moving party with the burden of proof at trial must come forward with evidence which would entitle it to a directed verdict if the evidence went uncontested at trial. Summary judgment is appropriate when the issue turns only on questions of law, the resolution of which does not involve disputed material facts.

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Statutory Exemptions

Antitrust & Trade Law > Sherman Act > General Overview

## **HN2**[ **Labor, Nonstatutory Exemptions**

Federal labor statutes set forth a national labor policy favoring collective bargaining, and require good-faith bargaining over wages, hours and working conditions. Moreover, multiemployer bargaining itself is a well-established, important, pervasive method of collective bargaining, offering advantages to both management and labor. This process, however, necessarily entails some amount of restraint on competition. In an attempt to harmonize the Sherman Act with the national labor policy of promoting the peaceful settlement of industrial disputes by subjecting labor-management controversies to the mediatory influence of negotiation, the U.S. Supreme Court has recognized a nonstatutory labor exemption to antitrust liability. The implicit exemption recognizes that, to give effect to federal labor laws and policies and to allow meaningful collective bargaining to take place, some restraints on competition imposed through the bargaining process must be shielded from antitrust sanctions.

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

Contracts Law > ... > Affirmative Defenses > Coercion & Duress > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Statutory Exemptions

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[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > Sherman Act > Scope > Exemptions](#)

[Contracts Law > Defenses > Illegal Bargains](#)

[Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview](#)

### **HN3** **Labor, Nonstatutory Exemptions**

National labor policy places beyond reach of the Sherman Act agreements between unions and employers as to "when, as well as how long, employees must work."

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Labor & Employment Law > ... > Employment Contracts > Conditions & Terms > Compensation & Benefits](#)

[Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview](#)

[Labor & Employment Law > Collective Bargaining & Labor Relations > Impasse Resolution](#)

[Labor & Employment Law > ... > Employment Contracts > Conditions & Terms > General Overview](#)

### **HN4** **Antitrust & Trade Law, Sherman Act**

As a matter of logic, it would be difficult, if not impossible, to require groups of employers and employees to bargain together, but at the same time to forbid them to make among themselves or with each other any of the competition-restricting agreements potentially necessary to make the process work or its results mutually acceptable.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Labor & Employment Law > Collective Bargaining & Labor Relations > Federal Preemption > Primacy of Labor Policy](#)

[Antitrust & Trade Law > Exemptions & Immunities > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions](#)

[Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview](#)

### **HN5** **Antitrust & Trade Law, Sherman Act**

The "nonstatutory exemption to the antitrust laws" has never been regarded as an open-ended invitation to those involved in a labor dispute to restrain competition in the product market. It is a limited nonstatutory exemption from antitrust sanctions.

[Antitrust & Trade Law > Sherman Act > Scope > Exemptions](#)

371 F. Supp. 2d 1179, \*1179L 2005 U.S. Dist. LEXIS 10572, \*\*10572

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Statutory Exemptions

#### **HN6** Scope, Exemptions

There are limits to what a union or an employer may offer or extract in the name of wages, and because they must bargain does not mean that the agreement reached may disregard other laws.

Antitrust & Trade Law > Sherman Act > General Overview

Contracts Law > ... > Negotiable Instruments > Negotiations > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### **HN7** Antitrust & Trade Law, Sherman Act

The U.S. Supreme Court has focused on harmonizing labor and antitrust laws by applying the nonstatutory labor exemption where there was an actual or potential conflict between the interests of labor relations and antitrust enforcement. Where no such conflict existed, it declined to apply the exemption. As is apparent from the Court's case law, the inquiry is necessarily fact specific and requires application of various considerations that help discern whether the harmonizing principle is served by applying the exemption to the challenged conduct in a particular case. In a recent case, the Court noted that the conduct took place during and immediately after a collective-bargaining negotiation. It grew out of, and was directly related to, the lawful operation of the bargaining process. It involved a matter that the parties were required to negotiate collectively. And it concerned only the parties to the collective-bargaining relationship. While the U.S. District Court for the Central District of California does not view this statement as declaring rigid factors that must be found in every case for the exemption to apply, it nevertheless believes that the Supreme Court signaled the importance of these considerations in determining whether there is an actual or potential conflict between labor and antitrust laws that requires accommodation through the application of the exemption.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

#### **HN8** Antitrust & Trade Law, Sherman Act

The "nonstatutory exemption to the antitrust laws" is ill-suited for actions taken after termination or successful completion of the collective bargaining process.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > Impasse Resolution

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > Strikes & Work Stoppages

#### **HN9**[] **Antitrust & Trade Law, Sherman Act**

Once a strike is over and a new collective bargaining agreement is agreed upon, there is not even an arguable case for reliance on the collective bargaining process to justify an exemption from the antitrust laws.

Antitrust & Trade Law > Sherman Act > General Overview

#### **HN10**[] **Antitrust & Trade Law, Sherman Act**

Antitrust laws are directed at conduct that suppresses competition in the marketing of goods and services.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### **HN11**[] **Antitrust & Trade Law, Sherman Act**

While national labor policy encourages collective bargaining, it does not require, imply or ensure that the parties to the bargaining process must have equality of bargaining position at all times. While a negotiating party should be able to take appropriate action to respond to opposing tactics, such action should not be protected categorically from antitrust scrutiny merely because it is helpful to the negotiating position of a party to the bargaining process.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### **HN12**[] **Antitrust & Trade Law, Sherman Act**

Methods used in labor negotiations are not immune from antitrust attack simply because the goal is legal.

Labor & Employment Law > Collective Bargaining & Labor Relations > Strikes & Work Stoppages

#### **HN13**[] **Collective Bargaining & Labor Relations, Strikes & Work Stoppages**

The statutory linkage of strikes and lockouts demonstrates that they are two sides of the same coin under national labor policy.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > Strikes & Work Stoppages

#### [\*\*HN14\*\*](#) [ ↴ ] **Antitrust & Trade Law, Sherman Act**

The same way a strike restrains the employees' provision of services to the employer, a lockout restrains the employers' purchase of those services from the employees. Both are fundamentally restraints on labor. Specifically, they are restraints on the labor market governed by a particular collective bargaining agreement. Though such restraints may indirectly affect commerce by restricting production or sales of goods or services to consumers, they are not the kind of restraints at which the Sherman Act is aimed. The work stoppage, whether initiated by the employers in a lockout or by the employees in a strike, does not restrict competition in the market among competitors in the industry.

Antitrust & Trade Law > Clayton Act > General Overview

Governments > Federal Government > US Congress

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### [\*\*HN15\*\*](#) [ ↴ ] **Antitrust & Trade Law, Clayton Act**

The nonstatutory exemption is not a mere equalization of the specific immunities afforded to organized labor by Congress in the Clayton and Norris-LaGuardia Acts, but rather is a judicially-created exemption that is necessary for an entirely different statutory scheme--the National Labor Relations Act--to function as Congress intended.

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

Business & Corporate Compliance > ... > Unfair Labor Practices > Employer Violations > Interference With Protected Activities

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Collectives & Cooperatives > Clayton Act

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Statutory Exemptions

Labor & Employment Law > Collective Bargaining & Labor Relations > Strikes & Work Stoppages

#### [\*\*HN16\*\*](#) [ ↴ ] **Labor, Nonstatutory Exemptions**

The basic sources of organized labor's exemption from federal antitrust laws are §§ 6, 20 ([15 U.S.C.S. § 17](#); [29 U.S.C.S. § 52](#)) of the Clayton Act, and [29 U.S.C.S. §§ 104, 105, 113](#) of the Norris-LaGuardia Act. These statutes declare that labor unions are not combinations or conspiracies in restraint of trade, and exempt specific union activities, including secondary picketing and boycotts, from the operation of the antitrust laws. They do not exempt concerted action or agreements between unions and nonlabor parties. The U.S. Supreme Court has recognized, however, that a proper accommodation between the congressional policy favoring collective bargaining under the

National Labor Relations Act and the congressional policy favoring free competition in business markets requires that some union-employer agreements be accorded a limited nonstatutory exemption from antitrust sanctions.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### [HN17](#) [blue icon] Antitrust & Trade Law, Sherman Act

While Brown extended the nonstatutory exemption to encompass certain employer-only agreements, it did not fundamentally alter the dynamics of the relationship between the nonstatutory and statutory exemptions. It held that employers are entitled to the nonstatutory exemption over agreements that are necessary to make the statutorily authorized collective-bargaining process work as Congress intended. Therefore, any application of the implicit nonstatutory exemption must be limited to those instances where the exemption is necessary to carry out Congress's intent as expressed in national labor policy.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

#### [HN18](#) [blue icon] Antitrust & Trade Law, Sherman Act

Mere lawfulness under the labor laws is not sufficient to create an antitrust immunity. Labor policy may be indifferent as to certain conduct, and then no labor policy purpose is served by immunizing it if it is anticompetitive.

Antitrust & Trade Law > Sherman Act > General Overview

Labor & Employment Law > Collective Bargaining & Labor Relations > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > Nonstatutory Exemptions

#### [HN19](#) [blue icon] Antitrust & Trade Law, Sherman Act

The incidental benefits that revenue sharing affords to employers in their labor negotiations cannot be utilized as a cat's-paw to pull employers' chestnuts out of the antitrust fires.

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For Food 4 Less Food Company, a division of the Kroger Company, Defendant: Peter F. Burns, Linda S. Husar, Robert B. Pringle, Thelen Reid and Priest, San Francisco, CA.

For Ralphs Grocery Company a division of the Kroger Company, Defendant: Peter F. Burns, Linda S. Husar, Robert B. Pringle, Thelen Reid and Priest, San Francisco, CA.

371 F. Supp. 2d 1179, \*1179L 2005 U.S. Dist. LEXIS 10572, \*\*10572

For Safeway Inc., a Safeway Company, Defendant: Daniel A Beck, Latham & Watkins, Los Angeles, CA; Peter K. Huston, J. Thomas Rosch, Latham & Watkins, San Francisco, CA.

For Los Angeles Times Communicaitons, LLC, doing business as Los Angeles Times, Intervenor: Erica L Craven, Karl Olson, Levy Ram & Olson, San Francisco, CA; Karlene Worthington Goller, Los Angeles Times Legal Dept., Los Angeles, CA.

**Judges:** [\[\\*\\*1\]](#) GEORGE H. KING, United States District Judge.

**Opinion by:** GEORGE H. KING

## Opinion

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### [\*1181] MEMORANDUM AND ORDER

#### RE: DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

I

#### INTRODUCTION

On February 2, 2004, California Attorney General Bill Lockyer, on behalf of the State of California ("the State"), filed a complaint alleging that defendants Safeway, Inc., d.b.a. Vons, Albertson's, Inc., Ralphs Grocery Company, ("the Supermarkets") and Food 4 Less Food Company ("Food 4 Less") (collectively "Defendants") engaged in an unlawful combination and conspiracy in restraint of interstate trade and commerce in violation of section 1 of the Sherman Act. [15 U.S.C. § 1](#). The State alleged that Defendants violated antitrust laws by entering into a Mutual Strike Assistance Agreement ("MSAA") whereby they agreed, among other things, to share revenue in the event of a strike. Defendants now move for summary judgment, arguing that their MSAA is immunized from antitrust challenge because it is related to the Supermarkets' participation in multiemployer collective bargaining and thus falls within the nonstatutory labor exemption to the antitrust laws. Having carefully considered all of the [\[\\*\\*2\]](#) parties' briefs, evidence and oral arguments, we rule as follows:

II

#### Summary Judgment Standard

**HN1** [Footnote] We may grant summary judgment only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." [Fed. R. Civ. P. 56\(c\)](#). See also [Celotex Corp. v. Catrett](#), 477 U.S. 317, 322, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986). Defendants, having raised the nonstatutory labor exemption as an affirmative defense, bear the burden of proof on this defense at trial. To be entitled to summary judgment, a moving party with the burden of proof at trial "must come forward with evidence which would entitle it to a directed verdict if the evidence went uncontested at trial." [C.A.R. Transp. Brokerage Co. v. Darden Rests., Inc.](#), 213 F.3d 474, 480 (9th Cir. 2000) (quoting [Houghton v. South](#), 965 F.2d 1532, 1536 (9th Cir. 1992)). Summary judgment is appropriate when the issue turns only on questions of law, "the resolution of which does not involve disputed [\[\\*\\*3\]](#) material facts." [Applied Med. Res. Corp. v. U.S. Surgical Corp.](#), 352 F. Supp. 2d 1119, 1123 (C.D. Cal. 2005).

**III****Facts**

Virtually all relevant facts are undisputed. Ralphs, Albertson's and Vons, three of the largest supermarket chains in Southern California, joined together in a multiemployer collective bargaining unit to negotiate with certain United Food and Commercial Workers ("UFCW") labor organizations. Their collective bargaining agreement ("CBA") with UFCW was set to expire on October 5, 2003. (Defs.' Ex. H). In anticipation of a labor dispute, the Supermarkets executed a pair of MSAs on September 5, 2003.<sup>1</sup> (Cox Decl. P 6). Pursuant to the MSAA, the Supermarkets agreed to lock out all union employees within 48 hours in the event any of their stores were to experience a strike. They also agreed to share revenue according to a fixed formula,<sup>2</sup> beginning at "12:01 a.m. on the Monday at the start of the week in which the strike or lockout . . . commences and continuing for two . . . full weeks following the week in which each strike or lockout ends." (MSAA at P 4(C)). Moreover, the revenue sharing was not limited to the employers participating **[\*\*4]** in the multiemployer bargaining unit. It included Food 4 Less, a chain that was not a signatory to the Ralphs/Vons/Albertson's CBA.

On October 11, 2003, the unions struck local Vons stores. (Cox Decl. P 7). In response, Ralphs and Albertson's locked out their union employees the next day. (Schroeder Decl. P 12; Bohn Decl. P 9). The unions initially picketed all three supermarket chains, but stopped picketing Ralphs stores on October 31, 2003. (Schroeder Decl. P 13). Selective picketing of Vons and Albertson's stores continued until the end of the strike in late February 2004.<sup>3</sup> Ultimately, Ralphs and Food 4 Less paid Vons and Albertson's approximately \$ 142 million in revenue **[\*\*5]** sharing for the strike period, and another \$ 4.2 million for the two-week period following the strike. (Schroeder Decl. P 13).

**IV****Discussion**

The State does not challenge the entirety of the MSAA. Instead, it claims only that the revenue-sharing provision, the inclusion of Food 4 Less, and the so-called two week "tail" provision (the "challenged provisions" or "challenged conduct") violate **[\*1183]** antitrust laws. Defendants assert, and the State disputes, that all of the challenged provisions are immune from antitrust scrutiny under the nonstatutory labor exemption. Our task on this motion is limited to deciding whether the nonstatutory labor exemption applies to these challenged provisions. If so, the State's antitrust claim necessarily fails. If not, further proceedings will be necessary to determine **[\*\*6]** whether these provisions in fact

**A****The Nonstatutory Labor Exemption**

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<sup>1</sup> Although there are two separate MSAs in the record, each covering different labor organizations, they have identical terms. (Pls.' Exs. 16 & 17). We thus refer to them as a single agreement.

<sup>2</sup> The revenue-sharing formula is set forth at paragraph 6 of the MSAA, and is reproduced verbatim as Appendix A to this Memorandum and Order.

<sup>3</sup> The Supermarkets and the unions entered into an agreement to end the strike on February 26, 2004. The unions' members ratified the agreement on February 29, 2004. (Cox Decl. P 7; Schroeder Decl. P 15).

**HN2**<sup>4</sup> Federal labor statutes set forth a national labor policy favoring collective bargaining, and require good-faith bargaining over wages, hours and working conditions. *Brown v. Pro Football, Inc.*, 518 U.S. 231, 236, 135 L. Ed. 2d 521, 116 S. Ct. 2116 (1996).<sup>4</sup> Moreover, "[m]ultiemployer bargaining itself is a well-established, important, pervasive method of collective bargaining, offering advantages to both management and labor." *Id. at 240*. This process, however, necessarily entails some amount of restraint on competition. In an attempt to harmonize the *Sherman Act* with the national labor policy "of promoting the peaceful settlement of industrial disputes by subjecting labor-management controversies to the mediatory influence of negotiation," the Supreme Court recognized a nonstatutory labor exemption to antitrust liability. *United Mine Workers of Am. v. Pennington*, 381 U.S. 657, 665, 14 L. Ed. 2d 626, 85 S. Ct. 1585 (1965) (quoting *Fibreboard Paper Prods. Corp. v. NLRB*, 379 U.S. 203, 211, 13 L. Ed. 2d 233, 85 S. Ct. 398 (1964)). "[T]he implicit exemption recognizes that, to give effect to federal labor laws and policies and to allow [\*\*7] meaningful collective bargaining to take place, some restraints on competition imposed through the bargaining process must be shielded from antitrust sanctions." *Brown*, 518 U.S. at 237. violate the antitrust laws.

For example, in *Local Union No. 189, Amalgamated Meat Cutters, and Butcher Workmen v. Jewel Tea Co.*, 381 U.S. 676, 679-80, 14 L. Ed. 2d 640, 85 S. Ct. 1596 (1965) (plurality opinion) (White, J.), a meat cutters union successfully negotiated a concession from a multiemployer bargaining unit by which the markets agreed that meat would not be sold before 9 a.m. or after 6 p.m. Jewel Tea Company and National Tea Company, two of the employers in the bargaining unit, signed the agreement under duress [\*\*8] of a strike vote. Contending that the agreement was illegal, they brought suit under the Sherman Act. *Id. at 680-81*. Justice White, writing for a plurality, concluded that the agreement was immune from antitrust attack under the nonstatutory labor exemption because **HN3** national labor policy places beyond reach of the Sherman Act agreements between unions and employers as to "when, as well as how long, employees must work." *Id. at 691*. Were it otherwise, collective bargaining would be frustrated. See *id. at 689*; *Connell Constr. v. Plumbers & Steamfitters Local Union No. 100*, 421 U.S. 616, 622, 44 L. Ed. 2d 418, 95 S. Ct. 1830 (1975) (stating that "the goals of federal labor law never could be achieved" were it otherwise).

Also, in *Brown*, 518 U.S. at 234, the Supreme Court considered the exemption in the context of an agreement solely among employers. When [\*1184] NFL employers reached an impasse with players in negotiations over salaries for a developmental squad, the employers unilaterally implemented the developmental squad program at the salary they had last proposed. *Id. at 235*. The players alleged the employers' agreement [\*\*9] among themselves to implement the wage provisions violated the Sherman Act. *Id.* The Court disagreed, concluding that the exemption applied to the employers' practice of jointly imposing the "last best good-faith wage offer" at an impasse. *Id. at 250*. It also observed that **HN4** "[a]s a matter of logic, it would be difficult, if not impossible, to require groups of employers and employees to bargain together, but at the same time to forbid them to make among themselves or with each other *any* of the competition-restricting agreements potentially necessary to make the process work or its results mutually acceptable." *Id. at 237* (emphasis in original).

However, **HN5** the exemption has never been regarded as an open-ended invitation to those involved in a labor dispute to restrain competition in the product market. It is a "*limited* nonstatutory exemption from antitrust sanctions." *Connell*, 421 U.S. at 622 (emphasis added). For example, in *Pennington*, 381 U.S. at 668-69, the Supreme Court held that the exemption did not protect an agreement between a union and large mine operators that sought to eliminate smaller companies, [\*\*10] thereby allowing the larger companies to control the market. Among other things, the agreement forced a particular wage and royalty scale upon the smaller operators. *Id. at 660*. The Court noted that "there is nothing in the labor policy indicating that the union and the employers in one bargaining unit are free to bargain about the wages, hours and working conditions of other bargaining units or to attempt to settle these matters for the entire industry. On the contrary, the duty to bargain unit by unit leads to a quite different conclusion." *Id. at 666*. Moreover, the conduct ran directly counter to policies underlying the antitrust

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<sup>4</sup> Throughout this opinion we refer to *Brown v. Pro Football, Inc.* simply as "*Brown*." There is, however, another similarly named, relevant Supreme Court opinion. See *NLRB v. Brown*, 380 U.S. 278, 13 L. Ed. 2d 839, 85 S. Ct. 980 (1965). To distinguish the two, we refer to the latter by its full name ("NLRB v. Brown").

laws. *Id. at 668*. Thus, in harmonizing the Sherman Act with labor law, there was no basis for applying the limited exemption. *Id. at 668-69*. HN6<sup>5</sup> "[T]here are limits to what a union or an employer may offer or extract in the name of wages, and because they must bargain does not mean that the agreement reached may disregard other laws." *Id. at 665*.

Likewise, in *Connell*, 421 U.S. at 619-26, the Supreme Court considered the scope of the exemption in a case in [\*\*11] which a union, through picketing, reached an agreement with general contractors to deal only with subcontractors who were parties to the union's collective bargaining agreement. Although the union's goal was to organize the subcontractors' employees, it eschewed any interest in representing any employees of the general contractors. Thus, the agreement was reached outside of any collective bargaining between the union and the general contractors. The Court concluded that the union's methods were not immune from antitrust attack simply because its goal was legal under labor law. *Id. at 625*. The agreement imposed on the general contractors caused all nonunion subcontractors to become ineligible to compete for available work. Balancing labor policy with the interests protected by the antitrust laws, the Court explained:

This kind of direct restraint on the business market has substantial anticompetitive effects, both actual and potential, that would not follow naturally from the elimination of competition over wages and working conditions. It contravenes antitrust policies to a degree not justified by congressional labor policy, and [\*1185] therefore cannot claim a nonstatutory [\*\*12] exemption from the antitrust laws.

*Id.*

In all of these decisions, HN7<sup>5</sup> the Supreme Court's focus was on harmonizing labor and antitrust laws by applying the nonstatutory labor exemption where there was an actual or potential conflict between the interests of labor relations and antitrust enforcement. Where no such conflict existed, the Court declined to apply the exemption. As is apparent from the Court's case law, the inquiry is necessarily fact specific and requires application of various considerations that help us discern whether the harmonizing principle is served by applying the exemption to the challenged conduct in a particular case.

In deciding that the exemption applied in *Brown*, its most recent opinion on the issue, the Court noted that the "conduct took place during and immediately after a collective-bargaining negotiation. It grew out of, and was directly related to, the lawful operation of the bargaining process. It involved a matter that the parties were required to negotiate collectively. And it concerned only the parties to the collective-bargaining relationship." *Brown*, 518 U.S. at 250. While we do not view this statement as declaring [\*\*13] rigid factors that must be found in every case for the exemption to apply,<sup>5</sup> we nevertheless believe that the Court signaled the importance of these considerations in determining whether there is an actual or potential conflict between labor and antitrust laws that requires accommodation through the application of the exemption.

[\*\*14] Each of the considerations described in *Brown* relates in some way to the scope of the exemption. While none is controlling, together they provide a valuable analytical tool for us to use in deciding whether the challenged conduct merits application of the exemption in this case.

<sup>5</sup> Prior to the Supreme Court's decision in *Brown*, the Ninth Circuit used a three-factor test to determine whether this exemption applied. *Phoenix Elec. Co. v. Nat'l Elec. Contractors Ass'n*, 81 F.3d 858, 861 (9th Cir. 1996) (applying the exemption when "(1) the restraint primarily affects the parties to the agreement and no one else, (2) the agreement concerns wages, hours, or conditions of employment that are mandatory subjects of collective bargaining, and (3) the agreement is produced from bona fide, arm's-length collective bargaining.") (citing test from *Mackey v. Nat'l Football League*, 543 F.2d 606, 614 (8th Cir. 1976)). To the extent that this so-called "Mackey test" exempts only agreements between unions and employers, it does not survive *Brown*, which extended the exemption to an employer-only agreement. See *Clarett v. Nat'l Football League*, 369 F.3d 124, 134 (2d Cir. 2004) ("the suggestion that the Mackey factors provide the proper guideposts . . . simply does not comport with the Supreme Court's most recent treatment of the non-statutory labor exemption in *Brown*. . . ."). Moreover, while the Mackey test required all three factors to be present, *Brown* does not adopt such a rigid test. But even if *Phoenix Elec. Co.* were still good law, the challenged provisions would clearly not be exempt from antitrust scrutiny because they do not concern wages, hours or conditions of employment as required by the second factor of the Mackey test.

**B*****Brown's Considerations*****1. The Timing of the Revenue Sharing Provisions**

The first consideration set forth in *Brown* examines whether the timing of the conduct was closely connected to the collective bargaining process. It is undisputed that the Supermarkets' multiemployer bargaining unit, in anticipation of the impending labor dispute, entered into the MSAA on September 5, 2003, one month before the expiration of their CBA. The MSAA's revenue-sharing terms were triggered [\*1186] by a strike against or lockout by any one of the Supermarkets. (MSAA at P 5(F)). In this way, the timing of the revenue sharing generally fell within the collective bargaining process.

However, the timing analysis is complicated by the fact that the revenue sharing ran for not only the entire duration of the strike, but also two full weeks after the conclusion of the labor dispute. Defendants assert that [\*\*15] the "tail" is justified under *Brown* because the Supreme Court applied the exemption to conduct taking place "during and immediately after a collective-bargaining negotiation." *Brown*, 518 U.S. at 250 (emphasis added). However, viewing *Brown* in the context of its facts, it is clear that the time following the breakdown in negotiations between the players and the NFL was itself part of the bargaining process.

During labor negotiations, the National Football League proposed its wage terms for a developmental squad to the players' union in April 1989, which the players rejected. *Id. at 234*. Two months later, in June, negotiations broke down, and the parties reached an impasse. *Id. at 235*. The league then unilaterally instituted its proposal. *Id.* But the labor dispute remained very much alive, even though negotiations had ceased. No agreement had yet been reached. The time "immediately after a collective-bargaining negotiation" described by the Supreme Court was still within an *ongoing* labor dispute. In this case, by contrast, the MSAA's two-week tail occurred after the conclusion of the labor dispute.

An impasse in [\*\*16] negotiations, like the one in *Brown*, "may occur several times during the course of a single labor dispute, since the bargaining process is not over when the first impasse is reached. . ." *Id. at 246*. Moreover, during such an impasse in negotiations, "[t]he multiemployer bargaining unit ordinarily remains intact. . . . The duty to bargain survives; employers must stand ready to resume collective bargaining." *Id. at 244*. This situation contrasts sharply with the one now before us in which the challenged conduct during the tail period occurred after a new CBA had already been successfully negotiated, and the labor dispute was over.

*Brown* does not provide any basis for applying the exemption to an agreement among employers that persists after a new CBA has been successfully negotiated. In holding that the exemption may not apply to agreements that are "sufficiently distant in time and circumstances from the collective-bargaining process," the Supreme Court pointed to two specific examples illustrating such distance: decertification of a union, and an "extremely long" impasse accompanied by instability or "defunctness" of a multiemployer bargaining [\*\*17] unit. *Id. at 250*. Both examples involve the collapse of collective bargaining in a way that terminates the process. The multiemployer negotiations with the union do not merely cease temporarily under such circumstances; rather, the process is entirely over due to the unraveling of the collective bond holding together the parties on one side of the negotiation. The Court's citation of these examples lends further support to our view that *HN8*[] the exemption is ill-suited for actions taken after termination or successful completion of the collective bargaining process.

Defendants argue that the tail serves national labor policy because they can more effectively maintain their unified front in dealing with the unions *during* negotiations if they know they will have some protection from competition *after* a labor dispute and while they await the return of their former customers. Nothing in the record supports Defendants' assertions [\*1187] that the collective bargaining process could not function, or would even be substantially impaired, without this tail provision. The Supermarkets believed that some of their customers were likely to stay away for many months after the strike's [\*\*18] conclusion. (Cox Decl. P 8; Schroeder Decl. P 11). Indeed, one of Defendants' witnesses declared that six months after the strike's conclusion, consumers still had not

returned to their pre-strike shopping patterns. (Schroeder Decl. P 15). The two-week tail thus did not do away with the economic impact the Supermarkets faced when recovering from the loss of their customers. The fact that they suffered lingering economic impact *despite the tail*, and they nevertheless have a new CBA with the unions in place, illustrates that it was not necessary to the collective bargaining process for the employers to be buffered from the effects of changed shopping patterns. See [Brown, 518 U.S. at 237-38](#).

Once the Supermarkets succeeded in negotiating their agreement with the unions, national labor policy ceased to serve as a justification for the challenged conduct.<sup>6</sup> Their concerns about customers' post-strike shopping preferences are not matters of labor law, but primarily matters of competition. Under national economic policy favoring competition, the problem of regaining customers who stray to competitors is uniquely within each business's own, separate ability to solve. [\[\\*\\*19\]](#) They can devise discounting opportunities, promotions, special services and all manner of creative enticements designed to lure customers back, just as they did to win customers from competitors in the pre-strike period. We are aware of no case that has ever held, or even suggested, that a tail period like that in Defendants' MSAA should fall within the ambit of the nonstatutory labor exemption.

We conclude that the revenue-sharing tail provision was not sufficiently temporally connected to the collective bargaining process to favor application of the exemption because the conduct at issue transpired not merely at an impasse in negotiations, [\[\\*\\*20\]](#) but after the bargaining process itself had concluded successfully. The timing of this conduct weighs against application of the exemption to the tail period.

On the other hand, the timing of the revenue sharing *during* the strike occurred within the context of an ongoing collective bargaining process. Negotiations were still underway during the strike, and no CBA had yet been reached. The timing of this part of the challenged conduct weighs in favor of applying the exemption.

## 2. Connection to Lawful Operation of the Bargaining Process

The next consideration set forth in [Brown](#) focuses on the nature of the employers' conduct. We examine whether the subject of the employers' agreement was sufficiently connected to the collective bargaining process.

The challenged provisions of the MSAA reallocate revenues among competitors during and after the strike period. The matter thus falls within Congress's core concerns in enacting the Sherman Act. See [Apex Hosiery Co. v. Leader, 310 U.S. 469, 487-88, 84 L. Ed. 1311, 60 S. Ct. 982 \(1940\)](#) (discussing the kind of restraint at which the Sherman Act is aimed), [492-93](#) (discussing [HN10](#)<sup>↑</sup> [\[\\*1188\]](#) antitrust laws being directed at conduct that "suppress[es] . . . [\[\\*\\*21\]](#) . competition in the marketing of goods and services. . . .") & [495 n.16](#) (discussing the antitrust laws' emphasis on "competitive conditions in the industry."). The revenue-sharing terms of the MSAA implicate labor policy at best *indirectly* by purportedly encouraging the employers to maintain their unity in bargaining; however, they *directly* affect market competition by freezing these competitors' relative market shares<sup>7</sup> [\[\\*\\*22\]](#) at pre-strike levels and redistributing revenue from one competitor to another pursuant to a fixed formula. The potential anticompetitive effects of such conduct do not follow naturally from the elimination of competition over wages, hours and working conditions, see [Connell, 421 U.S. at 625](#), and are not primarily directed at the labor

<sup>6</sup> By this we do not mean to suggest that national labor policy supports use of a revenue-sharing agreement during a strike. See discussion *infra* Part IV.B.2. We simply point out that [HN9](#)<sup>↑</sup> once the strike is over and a new CBA is agreed upon, there is not even an arguable case for reliance on the collective bargaining process to justify an exemption from the antitrust laws.

<sup>7</sup> We use the phrase "relative market shares" in a very specific sense. Defendants shared revenue based on each chain's individual share of the aggregated, pre-strike sales. While this did not necessarily constitute apportionment of the entire market for groceries in Southern California, by its own terms it sought to maintain each competitor's portion of their aggregated share of that total market.

market.<sup>8</sup> Rather, the potential effects of the revenue sharing are directed at Defendants' own competitive relationship with one another and have no direct connection to any term being negotiated with the unions.

[\*\*23] Defendants argue that revenue sharing promotes national labor policy because revenue sharing is necessary for them to effectively resist union "whipsawing" (i.e., selective picketing of one employer within a multiemployer bargaining unit in order to sever that employer's economic interest from that of the other employers). Thus, the challenged conduct is necessary to maintain relatively equal bargaining power.

Defendants' argument is based on a faulty premise. [HN11](#) While national labor policy encourages collective bargaining, it does not require, imply or ensure that the parties to the bargaining process must have equality of bargaining position at all times. In essence, Defendants argue that in order to allow them to fend off any potential adverse bargaining tactic by the unions, the employers must be able to not only formulate appropriate counter-measures, but also have such measures categorically immunized from antitrust scrutiny. While we do not question that a negotiating party should be able to take appropriate action to respond to opposing tactics, we do not agree that such action should be protected categorically from antitrust scrutiny merely because it is helpful to the [\*\*24] negotiating [[\\*1189](#)] position of a party to the bargaining process. National labor policy has never promised parties engaged in collective bargaining that they will be shielded from economic duress during (and after) a labor dispute. In fact, labor law seems to presume that sometimes the playing field may be uneven. See generally [NLRB v. Ins. Agents' Int'l Union, 361 U.S. 477, 489-90, 4 L. Ed. 2d 454, 80 S. Ct. 419 \(1960\)](#). Congress has not conferred upon the National Labor Relations Board ("NLRB") the power to create an "'ideal' or balanced' state of collective bargaining." [Id. at 499-500](#). As the Supreme Court long ago recognized, the risk of some economic hardship to both sides is built into the collective bargaining process, and that hardship (or, at least the threat of it) is ultimately part of what drives negotiations by bringing both parties to the table to compromise. See [id. at 489-90](#). But just because use of or resistance to economic pressure may be permissible under labor law does not mean that the collective bargaining process is itself compromised if any or all such actions are not exempt from antitrust scrutiny.<sup>9</sup>

<sup>8</sup> Before *Brown*, courts generally limited the application of the exemption to agreements whose anticompetitive restraints fell primarily and directly on the labor market. See [Brown v. Pro Football, Inc., 311 U.S. App. D.C. 89, 50 F.3d 1041, 1051 \(D.C. Cir. 1995\)](#), aff'd [518 U.S. 231, 135 L. Ed. 2d 521, 116 S. Ct. 2116 \(1996\)](#) ("[T]he case for applying the exemption is strongest where a restraint on competition operates primarily in the labor market and has no anti-competitive effect on the product market."); [Mid-Am. Reg'l Bargaining Ass'n v. Will County Carpenters District Council, 675 F.2d 881, 893 \(7th Cir. 1982\)](#) ("Thus, a complaint must allege conduct operating as a direct restraint upon the business market in order to avoid application of the nonstatutory exemption."); [Consol. Express, Inc. v. N.Y. Shipping Ass'n, 602 F.2d 494, 513 \(3rd Cir. 1979\)](#), vacated on other grounds, [448 U.S. 902, 65 L. Ed. 2d 1131, 100 S. Ct. 3040 \(1980\)](#) ("The term nonstatutory exemption . . . is a shorthand description of an interpretation of the Sherman Act, making that statute inapplicable to restraints imposed in the interest of lawful union monopoly power in the labor market."). *Brown* did not negate or implicitly overrule this nexus between exempted conduct and the labor market. See [Connell, 421 U.S. at 622](#) ("[T]he nonstatutory exemption offers no . . . protection when a union and a nonlabor party agree to restrain competition in a business market.").

<sup>9</sup> Defendants cite two out-of-circuit cases for the proposition that employer revenue-sharing agreements like this one are protected by the nonstatutory labor exemption. In the first, the Second Circuit upheld a joint strike insurance plan against an antitrust challenge. [Kennedy v. Long Island R.R., 319 F.2d 366, 374 \(2d Cir. 1963\)](#). However, the applicability of the nonstatutory labor exemption was not before, and was not considered by, the court. The court focused instead upon whether the insurance policy was a substantive violation of the antitrust laws. Of course, whether the challenged MSAA provisions violate the antitrust laws is not before us on this motion. Thus, *Kennedy* offers us no guidance here.

Defendants also rely upon a case in which several airlines joined together in a mutual aid pact. [Air Line Pilots Ass'n Int'l v. Civ. Aeronautics Bd., 163 U.S. App. D.C. 451, 502 F.2d 453 \(D.C. Cir. 1974\)](#). This case does not assist our inquiry because the court declined to address the antitrust issue due to the plaintiff's failure to exhaust an administrative remedy. [Id. at 457](#). Further, *Air Line Pilots* involved an explicit statutory exemption in the Federal Aviation Act, not the implicit nonstatutory exemption now before us. [Id. at 457](#) & n.14 (citing 49 U.S.C. § 1384 (1974), which relieved the potential defendant "from the operation of the antitrust laws" (repealed by the [Civil Aeronautics Board Sunset Act of 1984, PL 98-443](#))).

[\*\*25] The [HN12](#) methods used in labor negotiations are not immune from antitrust attack simply because the goal is legal. See [Connell, 421 U.S. at 625](#). Here, there is no showing that the Supermarkets and the unions cannot bargain collectively if revenue-sharing provisions like those in the MSAA were subject to antitrust scrutiny.

Defendants also argue there is fundamentally no difference between mutual aid agreements that provide for joint action locking out union employees, or shutting down production, see, e.g., [Clune v. Publishers' Ass'n, 214 F. Supp. 520, 522 \(S.D.N.Y. 1963\)](#), aff'd 314 F.2d 343 (2d Cir. 1963) (per curiam), and mutual aid agreements providing for the sharing of revenue. They go so far as to contend that the revenue-sharing provisions in their MSAA are analytically indistinguishable from lockout agreements as both are defensive tools used to combat whipsawing. Because revenue sharing purportedly keeps the employers' economic interests aligned, Defendants contend that without it, picketed stores would be pressured to accede to the unions' demands through the threat of losing customers who prefer to shop at non-picketed stores. [\*\*26] Like a lockout, revenue sharing theoretically strengthens employers' resolve to stand together through the strike. See [Brown, 518 U.S. at 245](#) (discussing [NLRB v. Brown, 380 U.S. 278, 289, 13 L. Ed. 2d 839, 85 S. Ct. 980 \(1965\)](#)), in which the Supreme [\*1190] Court held that hiring replacement workers during a lockout was calculated to "preserv[e] the integrity of the multiemployer bargaining unit."). "Labor law permits employers, after impasse, to engage in considerable joint behavior, including joint lockouts and replacement hiring." *Id.* Defendants also contend that revenue sharing has no more effect on the market than a lockout, which decreases production and thereby affects the availability of goods and services to consumers. For these reasons, Defendants argue that the rationale of the decisions sanctioning other kinds of employer mutual aid pacts, such as lockout agreements, dictates that the nonstatutory labor exemption should apply to Defendants' revenue sharing in this case.

While Defendants' argument may have superficial appeal, a closer examination of the nature of the mutual aid at issue reveals that there are significant differences between a lockout, or a production stoppage, [\*\*27] and revenue sharing. Employer lockouts are the flip-side of employee strikes. Congress statutorily recognized the use of lockouts as a lawful economic weapon in labor disputes. [NLRB v. Truck Drivers Local Union No. 449 \("the Buffalo Linen Case"\), 353 U.S. 87, 92-93, 1 L. Ed. 2d 676, 77 S. Ct. 643 \(1957\)](#) ("The unqualified use of the term 'lock-out' in several sections of the [Taft-Hartley Act](#) is statutory recognition that there are circumstances in which employers may lawfully resort to the lockout as an economic weapon."). The Taft-Hartley Act uses "strike" and "lock-out" jointly, as alternate forms of the same concept (i.e., a work stoppage induced by a labor dispute). See [id. at 92 n.16](#) (citing [29 U.S.C. § 158\(d\)\(4\)](#) ("no resort to *strike or lock-out*' during 60-day notice period"); [29 U.S.C. § 173\(c\)](#) ("Director of Mediation Service to seek to induce parties to settle dispute peacefully without resort to *strike, lock-out, or other coercion*'"); [29 U.S.C. § 176](#) ("appointment of board of inquiry by President when threatened or actual *strike or lock-out*' creates a national emergency"); [29 U.S.C. § 178](#) [\*\*28] ("power to enjoin '*strike or lock-out*' in case of national emergency")) (emphasis added). Though the Supreme Court has not expressly passed on whether an "employer lockout is the corollary of the employees' statutory right to strike," [id. at 93 n. 19](#), we conclude that it functions as such in light of the statutory linkage of the two. See [id. at 92 n.16](#). [HN13](#) The statutory linkage of strikes and lockouts demonstrates that they are two sides of the same coin under national labor policy.

Viewing lockouts as the analog of strikes, we look to the historical relationship between strikes and the Sherman Act to understand why this sort of mutual aid is immune from antitrust review. In 1924, the Supreme Court considered whether a strike against manufacturers gave rise to an antitrust claim against the union or its members. [United Leather Workers' Int'l Union v. Herkert & Meisel Trunk Co., 265 U.S. 457, 68 L. Ed. 1104, 44 S. Ct. 623 \(1924\)](#). The employers charged that the union's strike obstructed the manufacture and shipment of goods to be sold in interstate commerce. [Id. at 462](#). Chief Justice Taft, writing for the majority, reasoned that the "mere reduction [\*\*29] in the supply of an article [in] commerce [through the] prevention of its manufacture is ordinarily an *indirect and remote obstruction* to that commerce." [Id. at 471](#) (emphasis added). It only *directly* obstructs commerce when "the necessary effect upon such commerce . . . is to enable those preventing the manufacture to monopolize its supply or control its price, or discriminate as between its would-be purchasers. . . ." *Id.*

Similarly, in [Apex Hosiery, 310 U.S. at 481-83](#), a hosiery manufacturer [\*1191] sought to recover antitrust damages from a union for losses the manufacturer suffered from a strike at its factory. The Supreme Court recognized that the strike "naturally and inevitably" caused the cessation of production and shipment of goods. *Id.*

at 484. However, it questioned whether this was the *kind* of restraint on trade that the Sherman Act sought to prevent. Id. at 487. It concluded that the Sherman Act does not police interference with the movement of goods and services. Id. at 490. Rather, it polices "'trusts' and . . . combinations' of businesses and of capital organized and directed [\*\*30] to control of the market by *suppression of competition in the marketing of goods and services*. . . ." Id. at 492-93 (emphasis added). Its emphasis is on "competitive conditions in the industry." Id. at 495 n.16. The Supreme Court reviewed the common law doctrines of restraint, including conduct such as fixing prices, dividing market territories, and restricting production, all of which tend to raise prices and suppress competition. Id. at 497. It held that the strike had no effect on prices of hosiery in the market, and did not have as its purpose the restraint of competition. Id. at 501. It reasoned that under the Clayton Act, labor is not a commodity or article of commerce, and therefore restraints on the employees' services to the employer are not restraints of trade or commerce. Id. at 503.

**HN14** [↑] The same way a strike restrains the employees' provision of services to the employer, a lockout restrains the employers' purchase of those services from the employees. Both are fundamentally restraints on *labor*. Specifically, they are restraints on the labor market governed by a particular CBA. Though [\*\*31] such restraints may *indirectly* affect commerce by restricting production or sales of goods or services to consumers, see United Leather Workers, 265 U.S. at 471, they are not the *kind* of restraints at which the Sherman Act is aimed. Apex Hosiery, 310 U.S. at 487. The work stoppage, whether initiated by the employers in a lockout or by the employees in a strike, does not restrict competition in the market *among competitors in the industry*.

This distinction in the nature of the restraint is illustrated in Clune, 214 F. Supp. at 529-31, a case in which all the city newspaper publishers stopped production and thereby ceased "purchasing" the labor of printing pressmen who had targeted some of the newspapers with a strike. Relying on United Leather Workers, 265 U.S. at 471, the district court concluded that this production stoppage was analogous to the reduction in the supply of an article in commerce that would result from an employee strike. See Clune, 214 F. Supp. at 530-31. The court extended the rationale for exempting strikes from the Sherman Act to the employers' production stoppage. [\*\*32] Like a strike or lockout, this production stoppage directly restrained labor, and had an indirect effect on commerce, but "such results [were] not the direct interference with interstate commerce which the Sherman Anti-Trust Act forbids." Id. at 529 (quoting United States v. San Francisco Elec. Contractors Ass'n, 57 F.Supp. 57, 60-61 (N.D. Cal. 1944)).

The foregoing demonstrates why Defendants are mistaken in their contention that the revenue-sharing agreement at issue in this case is analytically indistinguishable from lockouts. While lockouts restrain labor (by halting the employers' purchase of the employees' services), and thereby indirectly affect commerce, the MSAA's revenue-sharing provisions do not affect the availability of labor, but instead guarantee, during (and for two weeks after) the [\*1192] strike, that each of the Supermarkets will be entitled to its pre-strike percentage share of their aggregate sales. As such the challenged provisions affect primarily matters of competition in the product market. This consideration weighs against applying the exemption to the Supermarkets' challenged conduct.

### 3. Connection to Mandatory Subjects of [\*\*33] Negotiations

It is undisputed that the revenue-sharing provisions of the MSAA do not concern mandatory subjects of collective bargaining (*i.e.*, wages, hours or working conditions). The lack of any connection to the core activities of collective bargaining weighs against application of the nonstatutory labor exemption to any of the revenue-sharing provisions of the MSAA.

### 4. Effect on Parties Not Involved in the Collective Bargaining

The final consideration of the Brown analysis focuses on whether the employers' agreement concerned only parties to the collective bargaining relationship. Ralphs, Vons and Albertson's were involved in negotiating a CBA as a single, multiemployer bargaining unit. They were therefore indisputably parties to the collective bargaining process.

Food 4 Less, however, was not part of the Supermarkets' multiemployer bargaining unit. Food 4 Less had its own, separate CBA with the unions which, unlike the Ralphs/Vons/Albertson's CBA that expired on October 5, 2003, did

not expire until February 28, 2004, and was subsequently extended to April 4, 2004.<sup>10</sup> Additionally, representatives of the Ralphs/Vons/Albertson's multiemployer bargaining unit [\*\*34] would have no role in negotiating Food 4 Less's future CBA with its unions. (MSAA at P 8(D)). Nevertheless, the revenue-sharing provisions of the MSAA obligated Food 4 Less to share its revenue with the Supermarkets in return for an agreement from Vons and Albertson's to do likewise were Food 4 Less to experience a strike in its future labor negotiations.<sup>11</sup> (See MSAA at P 8(A)).

The parties have presented conflicting evidence as to the entity status of Food 4 Less.<sup>12</sup> This [\*\*35] factual dispute is not material to our inquiry on this motion because our focus here is not on whether the employers' agreement affects independent corporate entities, but rather on whether it affects parties outside the collective bargaining relationship. The existence of a separate Food 4 Less CBA resolves that question. As a matter of *labor law*, [\*1193] the revenue sharing provision involved a party outside the collective bargaining relationship. It is the potential conflict between labor and antitrust laws that is at issue here, not the law of business associations. Food 4 Less (however defined) was not a member of the Ralphs/Vons/Albertson's multiemployer collective bargaining unit.

[\*\*36] Defendants also contend that Food 4 Less should not be considered a party outside the Ralphs/Vons/Albertson's multiemployer collective bargaining unit because some of the terms of Food 4 Less's own CBA were tied to terms in Ralphs's contract with the unions. Specifically, Food 4 Less's employees received health and welfare benefits equal to 75 percent of the value of those benefits in Ralphs/Vons/Albertson's CBA. Additionally, Food 4 Less's CBA recognized the experience level obtained by certain classes of workers who had previously worked under the Ralphs/Vons/Albertson's CBA. However, the linkage of Food 4 Less's employees' benefits and service credits to Ralphs's CBA does not make Food 4 Less a "party" to the Ralphs/Vons/Albertson's collective bargaining unit for purposes of the present analysis. This contractual linkage was incidental to the collective bargaining relationship. Indeed, the MSAA itself restricted its members from participating in Food 4 Less's own future negotiations with the unions. (MSAA at P 8(D) ("[T]he Management Committee will have no direct role with respect to Food4Less' [sic] conduct of its negotiations with the UFCW locals."))

Defendants argue [\*\*37] that inclusion of third parties does not weigh against application of the exemption. They rely on [Kennedy, 319 F.2d at 372-74](#). As we previously noted,<sup>13</sup> Defendants' reliance on *Kennedy* is misplaced inasmuch as the Second Circuit did not consider the applicability of the nonstatutory labor exemption.

Defendants also rely on [Amalgamated Meat Cutters & Butchers Workmen v. Wetterau Foods, Inc., 597 F.2d 133 \(8th Cir. 1979\)](#). There, a wholesale supplier provided a supermarket with temporary replacement workers in order to enable the supermarket to remain open during a strike. The union sued, alleging a violation of the Sherman Act. However, the agreement affected only labor, in the same way that a strike or lockout would. The court in *Wetterau Foods* specifically recognized that "[d]efining the boundaries of [the nonstatutory labor exemption] has not proved

<sup>10</sup> The record contains two separate collective bargaining agreements between Food 4 Less and UFCW locals. (See Pl.'s Exs. 2-3). Both agreements ran from February 27, 2000 through February 28, 2004. (*Id.*). As the differences between these two agreements are not salient to the present dispute, we refer to them as a single agreement.

<sup>11</sup> Food 4 Less never received the benefit of this reciprocal revenue-sharing provision, however, as it was able to avert a strike when negotiating its own CBA. (Supp. Schroeder Decl. PP 2-5).

<sup>12</sup> The State proffered the Food 4 Less CBA that was executed by an entity referred to as Food 4 Less of California, Inc. which appears to be a corporate entity distinct from Ralphs. (Pl.'s Exs. 2-3). In fact, Food 4 Less is sometimes treated as a separate entity in The Kroger Company's public filings with the Securities and Exchange Commission, and in the corporate hierarchy. (See Pl.'s Exs. 1, 49-51). Defendants submitted evidence demonstrating that Food 4 Less is merely a dba of Ralphs, and "Food 4 Less of California" is a dormant subsidiary whose name was used in error on Food 4 Less's CBA. Defendants also demonstrated that Food 4 Less's administrative structure is closely tied to Ralphs's own operations, and that Food 4 Less had an interest in the Ralphs/Vons/Albertson's CBA because Food 4 Less's own contract would be affected by it. (Schroeder Decl. PP 3-5, 7, 14; Defs.' Exs. I & J).

<sup>13</sup> See discussion *supra* n.9.

an easy task. A court must balance the degree of interference with federal [\*\*38] labor policy with the magnitude of the restraint of trade and whether the restraint directly or indirectly affects market prices and free competition for the consuming public." *Id. at 136.*

In analyzing this factor, we note that Food 4 Less's status as a party outside the Ralphs/Vons/Albertson's collective bargaining unit cannot be disconnected from its status as a competitor of the stores within that bargaining unit such as Vons and Albertson's. Unlike the wholesale supplier who was not a competitor of the store engaged in the labor dispute in *Wetterau Foods*, Food 4 Less competes with at least two of the Supermarkets.<sup>14</sup> The [\*1194] involvement of this competitor who operates under a separate CBA weighs against Defendants. We conclude that this consideration militates against extending the limited nonstatutory labor exemption to this revenue-sharing agreement.

## [\*\*39] C.

### Other Considerations

#### 1. Defendants' Proposed Parity Rule

At oral argument, Defendants argued that as a matter of parity, as long as an agreement among employers is designed to counter a union tactic protected by the statutory labor exemption, it should receive a corresponding immunity from the nonstatutory exemption. (Reporter's Transcript ("RT") at 34:6-10). Defendants claim that because revenue sharing was a tactic adopted to combat whipsawing, the nonstatutory immunity should apply to the challenged provisions.

Defendants purportedly derive this rule from *Brown*'s statement that the Court's decision "is not intended to insulate from antitrust review every joint imposition of terms by employers, for an agreement among employers could be sufficiently distant in time and in circumstances from the collective-bargaining process that a rule permitting antitrust intervention would not sufficiently interfere with that process." *Brown, 518 U.S. at 250*. (See RT 19:20 (arguing that this language was the controlling portion of *Brown*); RT 24:9-15 (arguing that the "specific issues of bargaining" discussed in the sentence laying out the four [\*\*40] considerations do not limit the exemption)). According to Defendants, concerted employer activity that is related to bona fide efforts to counter union labor tactics is sufficiently close in time and circumstances to the collective bargaining process to warrant application of the exemption.

This argument is flawed for a number of reasons. First, the language Defendants quote from *Brown* is a caveat on the Court's holding, not the holding or its rationale. The structure of the opinion makes clear that timing and circumstance are not the only relevant considerations. Defendants' reading ignores the proper context of the Court's discussion. The Court announced its holding and rationale as follows:

For these reasons, we hold that the implicit ("nonstatutory") antitrust exemption applies to the employer conduct at issue here. That conduct took place during and immediately after a collective-bargaining

<sup>14</sup> Defendants also cite a district court case from the Southern District of New York for the proposition that inclusion of Food 4 Less in the MSAA does not preclude application of the exemption. See *Sage Realty Corp. v. ISS Cleaning Servs. Group, Inc., 936 F. Supp. 130, 137-39 (S.D.N.Y. 1996)*. The primary holding of the case was that the plaintiff suffered no antitrust injury. *Id. at 136-37*. The district court's analysis of the applicability of the exemption sheds no light on the relevant considerations set forth in *Brown*. See *id. at 137-38*. Significantly, it offers no guidance whatsoever on the implications of involvement of a competitor, like Food 4 Less, who is not a member of the multiemployer bargaining unit. See *id. at 138 n.7* (noting that the defendants' actions had no anticompetitive effect on the market). We do not find *Sage Realty*'s analysis of the exemption persuasive in a situation, like ours, in which the conduct at issue involved an employer who is purportedly a horizontal competitor of the members of the multiemployer bargaining unit.

negotiation. It grew out of, and was directly related to, the lawful operation of the bargaining process. It involved a matter that the parties were required to negotiate collectively. And it concerned only the parties to the collective-bargaining relationship.

*Id.* [\*\*41] The next sentence, which Defendants cite, set forth a limitation on the holding and its fact-based inquiry: "Our holding is not intended to insulate . . . every joint imposition of terms by employers. . . ." *Id.* Defendants mistake the Court's fact-based limitation of its holding for the holding itself.

By failing to address the full rationale for the holding in *Brown*, Defendants ignore whether the agreement "involve[s] a matter that the parties were required to negotiate collectively" and whether it "concern[s] only the parties to the collective-bargaining relationship," two considerations important to the Court's decision. [\*1195] *Id.* We are not persuaded by any formulation of a test that simply ignores considerations the Supreme Court has deemed relevant.

Second, Defendants' reading of the nonstatutory exemption as requiring a *per se* parity rule represents a fundamental misunderstanding of the interplay between the statutory and nonstatutory exemptions. [HN15](#)[<sup>14</sup>] The nonstatutory exemption is not a mere equalization of the specific immunities afforded to organized labor by Congress in the Clayton and [Norris-LaGuardia Acts](#), but rather is a judicially-created exemption that is necessary [\*\*42] for an entirely different statutory scheme—the [National Labor Relations Act \("NLRA"\)](#)—to function as Congress intended. As the Supreme Court explained:

[HN16](#)[<sup>15</sup>] The basic sources of organized labor's exemption from federal antitrust laws are §§ 6 and 20 of the Clayton Act, [15 U.S.C. § 17](#) and [29 U.S.C. § 52](#), and the Norris-LaGuardia Act, [29 U.S.C. §§ 104, 105](#), and [113](#). These statutes declare that labor unions are not combinations or conspiracies in restraint of trade, and exempt specific union activities, including secondary picketing and boycotts, from the operation of the antitrust laws. They do not exempt concerted action or agreements between unions and nonlabor parties. The Court has recognized, however, that a proper accommodation between the congressional policy favoring collective bargaining under the NLRA and the congressional policy favoring free competition in business markets requires that some union-employer agreements be accorded a limited nonstatutory exemption from antitrust sanctions.

[Connell](#), [421 U.S. 621-22](#) (citations omitted). See also [Brown](#), [518 U.S. at 236](#) [\*\*43] (citing various provisions of the NLRA, [29 U.S.C. §§ 151, 153, 158](#), as sources of policy that form the basis of the nonstatutory exemption); [Allen Bradley Co. v. Local Union No. 3, IBEW](#), [325 U.S. 797, 801-06, 89 L. Ed. 1939, 65 S. Ct. 1533 \(1945\)](#) (discussing history and purpose of statutory exemption); [United States v. Hutcheson](#), [312 U.S. 219, 230-31, 85 L. Ed. 788, 61 S. Ct. 463\(1941\)](#) (same).

[HN17](#)[<sup>16</sup>] While *Brown* extended the nonstatutory exemption to encompass certain employer-only agreements, it did not fundamentally alter the dynamics of the relationship between the nonstatutory and statutory exemptions. See [Brown](#), [518 U.S. 237-38](#) (holding that employers are entitled to the nonstatutory exemption over agreements that are "necessary to make the statutorily authorized collective-bargaining process work as Congress intended."). Therefore, any application of the implicit nonstatutory exemption must be limited to those instances where the exemption is necessary to carry out Congress's intent as expressed in national labor policy. Defendants' interpretation of the exemption impliedly invites us to legislate an extension of the nonstatutory exemption to include a strict rule of [\*\*44] parity that Congress has not chosen to embrace. We decline Defendants' invitation.<sup>15</sup>

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<sup>15</sup> Defendants also imply that because lockouts, which are afforded the nonstatutory immunity, are "responses" to strikes, revenue sharing, which is a "response" to selective picketing, should be similarly immune. The syllogism is false. "Responsiveness" is not the touchstone of the nonstatutory immunity. As we addressed above, see *supra* discussion Part IV.B.2, lockouts warrant immunity because their primary and direct restraint falls on the labor market. The same cannot be said of the revenue sharing scheme in the MSAA.

In conclusion, we find no support for Defendants' proposed rule of parity in the statutory scheme, case law or policy considerations [**\*1196**] underlying the labor and antitrust laws. Nor can we discern any rationale for adopting such rule in lieu of weighing the four considerations set forth in *Brown*.

## 2. Defendants' Proposed Reliance on the NLRB

Defendants argue that an antitrust court should not police [**\*\*45**] the tactics used in collective bargaining because the NLRB already has authority to review their conduct, and the specter of an antitrust court's additional involvement would impair the functioning of that process. See *Brown*, 518 U.S. at 242 (noting that the NLRB, rather than antitrust courts, has "primary responsibility for policing the collective-bargaining process."). After oral argument, Defendants filed copies of several recent NLRB letter opinions in which the Board found that an allegedly similar mutual strike assistance agreement used by some of the Supermarkets in a different labor dispute did not violate the NLRA.

This argument misapprehends our role in this action. We do not purport to decide what is appropriate action under labor law. However, Congress has not vested the NLRB with responsibility to enforce the Sherman Act, review anticompetitive effects upon the market, or harmonize the nation's labor laws with the Sherman Act. The NLRB is charged with reviewing different aspects of such conduct. See *Ins. Agents*, 361 U.S. at 498-99 (discussing NLRB's responsibility for reviewing whether parties' conduct evidences a good-faith desire to [**\*\*46**] come to an agreement). Just as the NLRA serves a purpose different from that of the Sherman Act, our role in determining the applicability of the nonstatutory labor exemption is different from the NLRB's inquiry into whether a labor practice is unfair under national labor policy. We thus cannot agree with Defendants that the NLRB's decision about the permissibility of such conduct as a matter of labor law is a sufficient condition for applying the nonstatutory labor exemption in the face of an antitrust challenge. In fact, Supreme Court precedent is to the contrary. See *Connell*, 421 U.S. at 625 (holding that a union's conduct was not immune from antitrust sanctions simply because its goal is lawful). See also P. Areeda & H. Hovenkamp, *Antitrust Law* P 256e (2002) **HN18**[] ("[M]ere lawfulness under the labor laws is not sufficient to create an antitrust immunity. Labor policy may be indifferent as to certain conduct, and then no labor policy purpose is served by immunizing it if it is anticompetitive.").

V

## Conclusion

We have considered the harmonizing principle that underlies the nonstatutory labor exemption to the antitrust laws, and have carefully weighed [**\*\*47**] the relevant considerations noted in *Brown*. Overall, the challenged revenue-sharing provision of the MSAA is not sufficiently connected to the subject matter of the collective bargaining process, or to matters required to be negotiated collectively. Defendants' revenue-sharing agreement directly implicates competition among competitors in an industry by redistributing revenue earned at certain companies to others that were less successful during the strike, and by freezing each Defendant's relative market share at pre-strike levels, not only during a strike, but also for at least two weeks after successful completion of the bargaining process. This redistribution of revenue included a competitor that was not part of the multiemployer bargaining unit. The challenged provisions' potential anticompetitive effects do not follow naturally from the collective bargaining process, and they are neither necessary to, nor implied [**\*1197**] by, the functioning of that process. As labor law has not been shown to be impaired by subjecting this sort of revenue sharing to antitrust scrutiny, there is no conflict between antitrust and labor laws that requires reconciliation by application of the exemption. [**\*\*48**] We thus hold that the challenged provisions are not protected from potential antitrust liability by the limited nonstatutory labor exemption. **HN19**[] The incidental benefits that revenue sharing affords to employers in their labor negotiations "cannot be utilized as a cat's-paw to pull employers' chestnuts out of the antitrust fires." *United States v. Women's Sportswear Mfrs. Ass'n*, 336 U.S. 460, 464, 93 L. Ed. 805, 69 S. Ct. 714 (1949) (Jackson, J.).

Alternatively, we hold that the exemption also cannot be applied to this revenue-sharing agreement because of the involvement of Food 4 Less, a competitor that was not part of the multiemployer collective bargaining unit, and the inclusion of the tail period that took the employers' conduct entirely outside the collective bargaining process.

Defendants' motion for summary judgment is DENIED.

**IT IS SO ORDERED.**

Dated: May 25, 2005

GEORGE H. KING

United States District Judge

ATTACHMENT

Appendix A-Paragraph 6 of the MSAA

The revenue-sharing terms of paragraph 6(A) of the MSAA are set forth verbatim in this appendix.

6. CPA CALCULATIONS OF COST-SHARING PAYMENTS. The CPA shall compute the amount of cost-sharing, if any, due to/from each **[\*\*49]** of the employers as set forth below. An example of this calculation is attached hereto as Exhibit A. The computations shall be as follows:

A. Revenue Sharing

- (i) For the Pre-Strike Base Period, the CPA will compute each Employer's percentage share ("the Pre-strike Sales Share") of the Employers' combined average weekly sales for stores in the Covered Area.
- (ii) For the Strike/Lockout Period, the CPA will compute the dollar amount of increase or decrease in each Employer's average weekly sales as compared to that Employer's average weekly sales in the Pre-Strike Base Period ("Dollar Change in Sales").
- (iii) For the Strike/Lockout Period, the CPA will compute the total dollar change in average weekly sales for all Employers ("Total Weekly Sales Lost") by combining each Employer's Dollar Change in Sales.
- (iv) The CPA will compute a presumed redistribution of lost sales ("The Dollar Sales Redistribution") by multiplying the Total Average Weekly Sales lost figure by each Employer's Pre-Strike Sales Share.
- (v) The CPA will compute the dollar difference for each Employer between the Employer's Dollar Change in Sales and the Dollar Sales Redistribution. The resulting **[\*\*50]** amount shall be identified as the ("Sales Sharing Amount") [sic].
- (vi) The CPA will compute a presumed redistribution of lost sales ("the Dollar Sales Redistribution") by multiplying the Total Average Weekly Sharing Amount by fifteen percent (15%) and then multiplying the result by the number of weeks in the Strike/Lockout Period. (See Exhibit A attached hereto.) The Employer(s) due reimbursement under this section is/are the one(s) whose total average weekly sales lost during the Strike/Lockout **[\*1198]** period [sic] exceeds the redistributed amount.



## Dixie Gas & Food, Inc. v. Shell Oil Co.

United States District Court for the Northern District of Illinois, Eastern Division

May 25, 2005, Decided ; May 25, 2005, Filed

Case No. 03 C 8210

### **Reporter**

2005 U.S. Dist. LEXIS 12010 \*; 2005-1 Trade Cas. (CCH) P74,854; 57 U.C.C. Rep. Serv. 2d (Callaghan) 976

DIXIE GAS & FOOD, INC.; ZAINAB, INC. dba HOMEWOOD SHELL; BW SERVICES, INC. dba ORLAND PARK SHELL; SAINT SEBASTIAN, INC. dba SHELL MINI MART; HAISAG, INC. dba HAZEL CREST SHELL; GOPI CORP. dba GOPI SHELL; and JET, INC. dba GARFIELD SHELL, Plaintiffs, v. SHELL OIL COMPANY; EQUILON ENTERPRISES LLC dba SHELL OIL PRODUCTS US; and EQUIVA SERVICES LLC, Defendants.

**Subsequent History:** Summary judgment granted by, Claim dismissed by [Dixie Gas & Food, Inc. v. Shell Oil Co., 2008 U.S. Dist. LEXIS 16823 \(N.D. Ill., Mar. 3, 2008\)](#)

## **Core Terms**

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plaintiffs', Franchise, motion to dismiss, prices, non-conformity, allegations, counts, practices, economic duress, damages, franchisees, notice, Robinson-Patman Act, stations, dealer, buyer, declaratory judgment, franchise agreement, products, fuels, wagon, tank, price discrimination, good faith, parties, renewal, seller

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Robinson-Patman Act > Claims

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > General Overview

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

### **HN1[] Robinson-Patman Act, Claims**

There is no heightened pleading standard for antitrust claims.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > Coverage > General Overview

## **HN2[] Robinson-Patman Act, Claims**

To succeed on a Robinson-Patman Act price discrimination claim, plaintiffs must allege that: (i) more than one sale of commodities occurred; (ii) by the same seller; (iii) to different purchasers; (iv) at different prices among competitors; and (v) that the discrimination had a prohibited effect on competition. [15 U.S.C.S. § 13\(a\)](#).

Business & Corporate Law > Distributorships & Franchises > Assignments & Transfers

## **HN3[] Distributorships & Franchises, Assignments & Transfers**

[815 Ill. Comp. Stat. 705/6](#) explicitly prohibits various practices only in connection with the offer or sale of any franchise made in the state.

Torts > ... > Prospective Advantage > Intentional Interference > Elements

Torts > Business Torts > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

## **HN4[] Intentional Interference, Elements**

To win on a claim for interference with a prospective economic advantage under Illinois law, a plaintiff must show: (1) his reasonable expectation of entering into a valid business relationship; (2) the defendant's knowledge of the plaintiff's expectancy; (3) purposeful interference by the defendant that prevents the plaintiff's legitimate expectancy from ripening into a valid business relationship; and (4) damages to the plaintiff resulting from such interference.

Commercial Law (UCC) > Sales (Article 2) > Subject Matter > General Overview

Energy & Utilities Law > Oil & Petroleum Products > Gasoline Fuels > Gasoline Dealers & Distributors

Commercial Law (UCC) > Sales (Article 2) > General Overview

Commercial Law (UCC) > ... > Contract Provisions > Contract Terms > General Overview

Commercial Law (UCC) > ... > Contract Terms > Gap Filler Provisions > General Overview

Commercial Law (UCC) > ... > Contract Terms > Gap Filler Provisions > Open Price

## **HN5[] Sales (Article 2), Subject Matter**

810 Ill. Comp. Stat. 2-305(b) says that an open price term in a contract that is to be set by one party unilaterally must be set by that party in good faith: Open Price Term (2) A price to be fixed by the seller or by the buyer means a price for him to set in good faith.

Business & Corporate Compliance > ... > Sales of Goods > Remedies > General Overview

Contracts Law > ... > Sales of Goods > Breach, Excuse & Repudiation > General Overview

Commercial Law (UCC) > ... > Standards of Performance & Liability > Breach, Excuse & Repudiation > General Overview

Commercial Law (UCC) > ... > Breach, Excuse & Repudiation > Acceptance of Goods > General Overview

Commercial Law (UCC) > ... > Breach, Excuse & Repudiation > Notice Requirements > General Overview

Commercial Law (UCC) > ... > Breach, Excuse & Repudiation > Notice Requirements > Notice of Breach

Commercial Law (UCC) > ... > Standards of Performance & Liability > Performance > General Overview

Commercial Law (UCC) > ... > Buyer Remedies > Damages > General Overview

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

Business & Corporate Compliance > ... > Remedies > Buyer's Damages & Remedies > General Overview

Business & Corporate Compliance > ... > Sales of Goods > Performance > General Overview

#### **HN6** [] **Sales of Goods, Remedies**

810 Ill. Comp. Stat. 5/2-714 provides. Buyer's Damages for Breach in Regard to Accepted Goods. (1) Where the buyer has accepted goods and given notification (subsection (3) of Section 2-607) he may recover as damages for any non-conformity of tender. 810 Ill. Comp. Stat. 5/2-607(3) states that where a tender has been accepted (a) the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of the breach or be barred from any remedy.

Business & Corporate Compliance > ... > Contracts Law > Breach > Breach of Warranty

Contracts Law > ... > Sales of Goods > Warranties > General Overview

Commercial Law (UCC) > ... > Standards of Performance & Liability > Performance > General Overview

Contracts Law > ... > Sales of Goods > Breach, Excuse & Repudiation > General Overview

#### **HN7** [] **Breach, Breach of Warranty**

810 Ill. Comp. Stat. 2-714 non-conformity typically is associated with breaches of warranty or other claims arising from a physical non-conformity of the goods received as opposed to a non-conformity related to price. However, Illinois courts have found 810 Ill. Comp. Stat. 2-714 non-conformities for non-warranty related contractual breaches.

Civil Procedure > ... > Declaratory Judgments > Federal Declaratory Judgments > Discretionary Jurisdiction

Civil Procedure > Judgments > Declaratory Judgments > General Overview

Civil Procedure > ... > Declaratory Judgments > Federal Declaratory Judgments > General Overview

#### **HN8** [] **Federal Declaratory Judgments, Discretionary Jurisdiction**

Under the Declaratory Judgment Act, [28 U.S.C.S. § 2201 et seq.](#), federal courts have discretion to decline to hear a declaratory judgment action, even though it is within their jurisdiction. Declaratory judgment is appropriate, among other instances, where, the controversy has ripened to a point where one of the parties could invoke a coercive remedy (i.e. a suit for damages or an injunction) but has not done so.

**Counsel:** [\*1] For Dixie Gas & Food, Inc., Zainab, Inc., BW Services, Inc., Caspian Petroleum Co., Saint Sebastian Inc., Haisag Inc, Gopi Corp, Jet Inc, Plaintiffs: Timothy John Coffey, Attorney at Law, Chicago, IL; William L Taylor, Taylor & Powell, LLC, Alexandria, VA; Nikki Fong, Thomas P Bleau, Bleau Fox & Associates, Los Angeles, CA; Timothy John Coffey, Law Office of Timothy J. Coffey, Glen Ellyn, IL.

For Shell Oil Company, Equilon Enterprises, LLC, Equiva Services, LLC, Defendants: David M Harris, Dawn Ann Morville Johnson, Greensfelder, Hemker & Gale, PC, St Louis, MO; Emily C Singley, Greensfelder, Hemker & Gale, P.C., Belleville, IL; James Thomas O'Neill, James T. O'Neill, Attorney at Law, Chicago, IL.

**Judges:** Judge Gottschall.

**Opinion by:** Joan B. Gottschall

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

The plaintiffs in this action are several operators of Shell-branded gas station/mini mart businesses in Northern Illinois: Dixie Gas & Food, Inc., Zainab, Inc. dba Homewood Shell; BW Services, Inc. dba Orland Park Shell; Saint Sebastian, Inc. dba Shell Mini Mart; Haisag, Inc. dba Hazel Crest Shell; Gopi Corp. dba Gopi Shell; and Jet, Inc. dba Garfield Shell. The defendants are Shell Oil Company, [\*2] Equilon Enterprises LLC dba Shell Oil Products US, and Equiva Services LLC<sup>1</sup> (collectively, "Shell"). Plaintiffs allege that they are all Shell franchisees, and that Shell has engaged in violations of federal [antitrust law](#) as well as various Illinois laws.

Before the court is Shell's motion to dismiss all nine counts of plaintiffs' complaint under [Fed. R. Civ. P. 12\(b\)\(6\)](#). For the reasons discussed below, Shell's motion to dismiss is granted as to counts 1, 3 (only with respect to plaintiff Haisag, Inc.), 4, 6, 8, and 9, and denied as to counts 2, 3 (except as to plaintiff Haisag, Inc.); 5, and 7.

### **Jurisdiction**

Plaintiffs allege federal question jurisdiction for violations of the [\*3] Robinson-Patman Price Discrimination Act, [15 U.S.C. §13](#) ("Robinson-Patman Act"), as well as diversity jurisdiction. The remaining eight counts of the complaint allege state law claims.

### **Count 2 (Robinson-Patman Act)**

As it is the basis for federal question jurisdiction in this case, the court first analyzes the sufficiency of plaintiffs' pleading as to their Robinson-Patman Act claims in count 2 of the complaint. Plaintiffs' count 2 alleges that Shell has engaged in price discrimination with respect to sales of motor vehicle fuels, in violation of the Robinson-Patman Act.

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<sup>1</sup> Plaintiffs allege that Equilon and Equiva Services are related to and controlled by Shell Oil Company, and that all defendants are jointly and severally liable for the acts complained of in this lawsuit. Defendants do not contest this characterization in their motion to dismiss.

As an initial matter, Shell's motion to dismiss implies that plaintiffs must meet a heightened pleading standard for their antitrust allegations, asserting that plaintiffs' Robinson-Patman Act claims are "vague and confusing," that plaintiffs "summarily" assert injury to themselves and to competition, and that plaintiffs' price discrimination claim "is so lacking in particularity" that it should be dismissed. Unfortunately for Shell, [HN1](#) there is no heightened pleading standard for antitrust claims. [\*Hammes v. Aamco Transmissions, Inc.\*, 33 F.3d 774, 782 \(7th Cir. 1994\)](#) [\*4] (noting that the Supreme Court has disallowed lower courts from imputing rule to antitrust claims that they must be pled with particularity).

[HN2](#) To succeed on a Robinson-Patman Act price discrimination claim, plaintiffs must allege that: (i) more than one sale of commodities occurred; (ii) by the same seller; (iii) to different purchasers; (iv) at different prices among competitors; and (v) that the discrimination had a prohibited effect on competition. [15 U.S.C. § 13\(a\)](#); [\*Goodloe v. Nat'l Wholesale Co.\*, No. 03C7176, 2004 U.S. Dist. LEXIS 13630, at \\*26 \(N.D. Ill July 3, 2004\)](#), citing [\*Kundrat v. Chicago Bd. Options Exch., Inc.\*, No. 01C7456, 2002 U.S. Dist. LEXIS 16908, at \\*18 \(N.D. Ill. Sept. 6, 2002\)](#), and [\*Windy City Circulating Co., Inc. v. Charles Levy Circulating Co.\*, 550 F. Supp. 960, 966 \(N.D. Ill. 1982\)](#).

Under this standard, plaintiffs have provided adequate allegations to support their Robinson-Patman Act claim. Plaintiffs have alleged that Shell engaged in more than one sale of motor vehicle fuels (Complaint P22, 65-66); the "same motor vehicle fuels" are the commodities that were priced discriminatorially [\*5] (Complaint P61); that Shell actually discriminated in price between competing vendors without mitigating justification (Complaint P62 - 64); and that this alleged discriminatory pricing has caused injury to plaintiffs in particular and to competition generally (Complaint P65, 67-70). For good measure, plaintiffs have included other allegations (apparently under the assumption that they should plead facts to support all elements required to prove a Robinson-Patman violation), including that the allegedly discriminatory sales occurred in interstate commerce. (Complaint P66.) Shell's motion to dismiss count 2 is denied.

## Count 1 (Economic Duress)

In count 1 plaintiffs seek damages based on their allegations that they were forced into signing franchise renewal agreements through tactics by Shell that constitute economic duress under Illinois law. (Complaint PP31 -59); see [\*Alexander v. Standard Oil Co.\*, 97 Ill. App. 3d 809, 423 N.E.2d 578, 582-83, 53 Ill. Dec. 194 \(Ill. App. Ct. 1981\)](#). Shell first argues that this theory is preempted by the remedial scheme of the Petroleum Marketing Practices Act, [15 U.S.C. §§ 2801, et seq.](#) ("PMPA") that governs the franchisee/franchisor [\*6] relationship after a franchise agreement has been terminated or non-renewed. [15 U.S.C. § 2806](#). This theory has been explicitly rejected by the Seventh Circuit. [\*Dersch Energies, Inc. v. Shell Oil Co.\*, 314 F.3d 846 \(7th Cir. 2002\)](#). As was the case in *Dersch Energies*, the parties here do not dispute that plaintiffs did renew their franchise agreements (if under protest), which divests plaintiffs of the ability to proceed under the PMPA's provisions regarding unlawful termination or non-renewal. This does not bar them from bringing state law causes of action attacking formation of the contract: In fact, *Dersch Energies* specifically notes that state law economic duress claims are allowed as to petroleum franchise agreements. [\*Dersch Energies\*, 314 F.3d at 862](#) (where plaintiff actually renewed petroleum franchise agreement, she is "entitled to bring a state law claim . . . such as economic duress").

Shell also asserts that plaintiffs' economic duress claim is identical to the "constructive termination" theory that has been rejected in PMPA cases by the Seventh Circuit. [\*Jet, Inc. v. Shell Oil Co.\*, 381 F.3d 627 \(7th Cir. 2004\)](#), [\*7] affirming [\*Jet, Inc. v. Shell Oil Co.\*, No. 02C2289, 2002 U.S. Dist. LEXIS 22951 \(N.D. Ill. Nov. 22, 2002\)](#). This argument is a red herring; plaintiffs' economic duress claim is brought under state law, not the PMPA, making *Jet* inapplicable. [\*Jet\*, 381 F.3d at 630](#) (holding that where franchisees actually renewed their franchise agreements, they could not state a claim "for wrongful renewal under the PMPA").

Shell also argues that there is no Illinois cause of action allowing an award of damages on an economic duress claim; rather, the theory of economic duress is available only to support avoidance of obligations undertaken as a result of actionable economic pressure. Shell's main case is [\*Shields Enters. v. First Chicago Corp.\*, 975 F.2d 1290 \(7th Cir. 1992\)](#), which directly supports this position. See also [\*Tibor Mach. Prods. v. Freudenberg-Nok, No.\*](#)

[94C7635, 1996 U.S. Dist. LEXIS 2360, at \\*6 \(N.D. Ill. Feb. 29, 1996\)](#). Shell is correct in pointing out that plaintiffs have requested only damages, not avoidance of their franchise agreements, and have thus failed to state a claim under a theory of economic duress. Count [\*8] 1 is dismissed with prejudice. [Shields Enters., 975 F.2d at 1297](#) (affirming dismissal with prejudice of claim based on non-existent Illinois cause of action for damages based on economic duress).

### Count 3 (Fraud)

Count 3 is brought by all plaintiffs except for Gopi, Inc. dba Gopi Shell, and claims damages for common-law fraud. Shell argues that plaintiffs have failed to allege fraud with the specificity required by [Fed. R. Civ. Pro. 9\(b\)](#). Citing the familiar "who, what, when, where, and how" pleading standard for fraud in the Seventh Circuit, Shell claims that the complaint alleges only generally that plaintiffs were misled by-Shell's representatives into believing that no rent relief measures were available from Shell to franchisees, when in fact Shell did have contemporaneous rent-relief programs available.<sup>2</sup> [DiLeo v. Ernst & Young, 901 F.2d 624, 627 \(7th Cir. 1990\)](#) (describing who, what, when, where, and how pleading standard for fraud). Contrary to Shell's arguments, plaintiffs have pled fraud with the specificity required by [Rule 9\(b\)](#). For example, plaintiffs allege:

in the case of plaintiffs [\*9] Dixie Gas & Food, Inc., Zainab, Inc. dba Homewood Shell, and BW Services, Inc. dba Hickory Hills Shell, their principals, Abdul Basit and Waseem Ahmed met with Jeff Root [whom plaintiffs allege to be one of "their Equilon representatives"] at the Hickory Hills Shell service station in or about the late summer or fall of 1998 and complained to him about the high contract rents. They were told that nothing could be done about it, and they could either accept the new contract rents or give up the service stations.

(Complaint PP 75, 75(a)). This is typical of the level of specificity provided as to all plaintiffs who allege fraud, and includes each necessary allegation to complete the "who, what, when, where and how" formula. (Complaint PP75(a)-(e).) Further supporting allegations are to be found throughout the complaint. Thus, Shell's motion to dismiss count 3 is denied with respect to all plaintiffs alleging fraud, with the exception of plaintiff Haisag, Inc. dba Hazel Crest Shell ("Haisag"), as to which no approximate dates of alleged misrepresentation are specifically alleged. [Ackerman v. Northwestern Mut. Life Ins. Co., 172 F.3d 467, 470 \(7th Cir. 1999\)](#) [\*10] (emphasizing importance of "when" component of pleading fraud). For this reason, Shell's motion to dismiss count 3 is granted as to Haisag only.

### [\*11] Counts 4 & 5 (Illinois Franchise Disclosure Act)

Next, Shell asserts that counts 4 and 5 must be dismissed because they fail to allege facts sufficient to establish that the Plaintiff is a franchisee within the meaning of the Illinois Franchise Disclosure Act, [815 ILCS 705/1, et seq.](#) ("Franchise Act"). Shell asserts that to have standing under the Franchise Act, plaintiffs must plead allegations to support all elements establishing that plaintiffs meet the Franchise Act's definition of "franchisee" (a multi-part test according to Shell), and also argues that allegations going to each element of the claimed statutory violation must be pled to avoid dismissal. The court rejects this argument, which attempts to apply state fact pleading standards in federal court where notice pleading is the law. [Bennett v. Schmidt, 153 F.3d 516, 518\(7th Cir. 1998\)](#) ("[Federal]

<sup>2</sup> Count 3 is based on allegations that each plaintiff was eligible for an "Interim Rent Challenge" (a Shell program allowing for a reduction in lease rates for franchisees who complained of high rents), that Shell intentionally withheld information from plaintiffs about the Interim Rent Challenge, and affirmatively misrepresented to plaintiffs that Shell had no procedure available to franchisees to challenge allegedly excessive rental rates. (Complaint PP 76-85.) In addition to its [Rule 9](#) argument, Shell claims (without citation to authority) that there can be no claim for damages based on these facts, essentially because such damages would be speculative. This argument fails. While plaintiffs may face a difficult challenge in proving the extent of damages, their allegations are sufficient to state a claim. See, e.g., [McHugh v. Westpac Banking Corp., Nos. 93C3058, 93C3059, 1995 U.S. Dist. LEXIS 11397, at \\*6 \(N.D. Ill. Aug. 8, 1995\)](#) (noting that allegations of lost business opportunities are sufficient to support a claim for Illinois common law fraud).

complaints need not plead law or match facts to every element of a legal theory."). Plaintiffs have adequately pled standing under the Franchise Act; throughout their complaint plaintiffs allege that they are franchisees of Shell, and that the defendant Shell entities [\*12] are franchisors. Shell's standing argument fails, and as to Count 5 (alleging inter-franchisee price discrimination prohibited by [815 ILCS 705/18](#)), Shell makes no other argument. Shell's motion to dismiss is denied with respect to Count 5.

With respect to count 4 (alleging fraudulent business practices prohibited by [815 ILCS 705/6](#)), however, Shell's motion to dismiss is granted. While plaintiffs do not need to plead factual allegations going to each and every element of a [section 705/6](#) claim, they do need to plead enough to state a claim under the plain language of the statute. [HN3](#)[ [Section 705/6](#)] explicitly prohibits various practices only "in connection with the offer or sale of any franchise made in this State." [815 ILCS 705/6](#). While count 4 sets forth many alleged actions of Shell that may (or may not) rise to the level of fraudulent practices under [section 705/6](#), it fails to allege that these actions were undertaken in connection with the offer or sale of any of plaintiffs' franchises. The closest plaintiffs come to alleging fraud in connection with an offer or sale of one of plaintiffs' franchises [\*13] is in P96(h) of the complaint:

Plaintiffs are informed and believe, and based thereon allege, that SHELL, EQUIVA and EQUILON have violated § [815 ILCS 705/6](#) [sic] by . . . (h) failing to disclose that Defendants would attempt to discourage prospective buyers of Plaintiffs' franchises in an attempt to eliminate independent franchisees, such as Plaintiffs, and other unfair business practices designed at forcing franchisees to "walk away" from their stations and/or reducing the goodwill value of Plaintiffs' stations so that it could exercise a right of first refusal at an artificially low purchase price.

This general language, free of references to any particular proposed offers or sales of the franchises at issue in this litigation, is inadequate to allege fraudulent practices by Shell in connection with an actual offer or sale of a franchise. On this basis, Shell's motion to dismiss count 4 is granted.

## **Count 6 (Illinois Deceptive Trade Practices Act)**

Plaintiffs' count 6 alleges that certain Shell business practices complained of throughout the complaint also violate Illinois' Uniform Deceptive Trade Practices Act, [815 ILCS 510/1 \[\\*14\] , et seq.](#) ("IUDTPA"). Here, as in [Industry Specialty Chems., Inc. v. Cummins Engine Co., Inc.](#), 902 F.Supp. 805, 812-13 (N.D. Ill. 1995), "conspicuously absent from plaintiff's complaint is an allegation that defendants misrepresented [plaintiffs'] products as their own, or confused the public as to the source or sponsors of their products." In other words, while Shell's business practices toward plaintiffs may be actionable under other statutes or common law, plaintiffs fail to allege anywhere in the complaint that Shell has attempted to pass off any products, or has otherwise created any likelihood of confusion as to the source of any products, and so have failed to state a claim under the IUDTPA. [McGraw-Edison Co. v. Walt Disney Productions](#), 787 F.2d 1163, 1175 (7th Cir. 1986) ("Under the Illinois Deceptive Trade Practices Act a defendant is liable only if the plaintiff can establish a likelihood of confusion between the parties' products.") Shell's motion to dismiss plaintiffs' count 6 is granted.

## **Count 7 (Interference With Prospective Economic Advantage)**

Plaintiff Caspian Petroleum Co. dba Orland Park Shell ("Caspian") is the only [\*15] plaintiff bringing count 7, alleging interference with prospective economic advantage. Caspian claims that through delaying tactics and other unspecified interference, Shell interfered with Caspian's attempt to sell its franchise to a qualified prospective purchaser.

[HN4](#)[ To win on a claim for interference with a prospective economic advantage under Illinois law, a plaintiff must show: "(1) his reasonable expectation of entering into a valid business relationship; (2) the defendant's knowledge of the plaintiff's expectancy; (3) purposeful interference by the defendant that prevents the plaintiff's legitimate expectancy from ripening into a valid business relationship; and (4) damages to the plaintiff resulting from such interference." [Fellhauer v. City of Geneva](#), 142 Ill. 2d 495, 568 N.E.2d 870, 878, 154 Ill. Dec. 649 (Ill. 1991). Again,

a plaintiff in federal court need not allege facts going to each of these elements in detail, and here Caspian has alleged enough to assert its claim, stating that: it had a qualified prospective buyer and a signed contract to sell its franchise, that it notified Shell of the expected sale (by requesting Shell's approval), that Shell interfered with the prospective sale [\*16] for the purpose of scuttling the sale, and that this (among other things) has resulted in Caspian's inability to sell its station for a reasonable price. (Complaint PP124-30.) Shell's motion to dismiss count 7 is denied. *Telewizja Polska USA, Inc. v. EchoStar Satellite Corp., No. 02C3293, 2004 U.S. Dist. LEXIS 17936, at \*35-36 (N.D. Ill. Sep. 3, 2004)*.

### **Count 8 (Illinois Uniform Commercial Code)**

In count 8 plaintiffs (with the exception of Caspian and Haisag) allege that Shell has at various times since 1998 violated [section 2-305](#) of Illinois' Uniform Commercial Code, [810 ILCS 5/2-101, et seq.](#) [HN5](#) [Section 2-305\(1\)\(b\)](#) says that an open price term in a contract that is to be set by one party unilaterally must be set by that party in good faith: "[§2-305](#). Open Price Term. . . . (2) A price to be fixed by the seller or by the buyer means a price for him to set in good faith." Plaintiffs claim that "dealer tank wagon prices" (which appears to mean the wholesale prices at which Shell sells motor fuel to retail service stations) are open price terms of the dealer agreements between the complaining plaintiffs and Shell (Complaint P133), [\*17] that Shell did not set these prices in good faith or according to reasonable commercial standards (Complaint P134), and that it unjustifiably provided preferred tank wagon pricing to company-owned and/or other preferred dealers. (Complaint P135.) When taken as true, these allegations are sufficient to state a claim that Shell did not set an open price term (dealer tank wagon prices) in good faith. [810 ILCS 5/2-305\(1\)\(b\)](#). Unfortunately for plaintiffs, however, the inquiry does not stop there - plaintiffs have failed to allege that they gave required notice to Shell of its alleged breaches.

[HN6](#) [810 ILCS 5/2-714](#) mandates that plaintiffs needed to provide Shell with notification of Shell's alleged pricing breaches: "[§ 2-714](#). Buyer's Damages for Breach in Regard to Accepted Goods. (1) Where the buyer has accepted goods and given notification (subsection (3) of [Section 2-607](#)) he may recover as damages for any non-conformity of tender . . . . [Subsection \(3\) of 810 ILCS 5/2-607](#) states that "where a tender has been accepted (a) the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller [\*18] of the breach or be barred from any remedy."

The court notes that it is not immediately obvious that plaintiffs' acceptance of the allegedly overpriced fuels qualifies as acceptance of "non-conforming" goods under [section 2-714](#). [HN7](#) [Section 2-714](#) non-conformity typically is associated with breaches of warranty or other claims arising from a physical non-conformity of the goods received as opposed to a "non-conformity" related to price. See, e.g., *Klockner, Inc. v. Federal Wire Mill Corp.*, 663 F.2d 1370, 1380 (7th Cir. 1981) (breach of warranty counterclaim). However, Illinois courts have found [section 2-714](#) non-conformities for non-warranty related contractual breaches. See, e.g., *Franklin Grain & Supply Co. v. Ingram*, 44 Ill. App. 3d 740, 358 N.E.2d 922, 925, 3 Ill. Dec. 379 (Ill. App. Ct. 1976) (late delivery of goods ordered). Neither of the parties has cited a case directly holding that price can constitute a [section 2-714](#) non-conformity, nor has the court located one. The closest case on point is *Tudor v. Jewel Food Stores, Inc.*, 681 N.E.2d 6, 10-11, 288 Ill. App. 3d 207, 224 Ill. Dec. 24 (Ill. App. Ct. 1997), in which the Illinois Appellate Court affirmed the dismissal of a grocery store customer's claim under [\*19] [section 2-714](#) that the defendant had overcharged her for groceries because the plaintiff failed to provide notice to defendants of non-conformities of marked prices versus prices charged, as required by [section 2-714](#). The *Tudor* court did not reflect explicitly on whether price could stand as a non-conformity under [section 2-714](#), but merely noted that plaintiff had failed to present the notice required under [section 2-607](#) and affirmed dismissal on that ground. In the absence of contrary authority, the court accepts *Tudor*'s implication that a breach of a contractual price term can qualify as a non-conformity under [section 2-714](#).

The court also notes that the Uniform Commercial Code Comment attached to [section 2-714](#) states that "the 'non-conformity' referred to in subsection (1) includes not only breaches of warranties but also any failure of the seller to perform according to his obligations under the contract." As discussed, one of Shell's (alleged) obligations (as implied by [section 2-305\(1\)\(b\)](#)) under each of the contracts with plaintiffs was to sell fuel to plaintiffs according to dealer tank wagon prices that were set in good faith. [810 ILCS 5/2-305\(1\)\(b\)](#) [\*20]. Plaintiffs apparently accepted

all dealer tank wagon deliveries and do not allege that they have ever provided notice to Shell of its alleged dealer tank wagon pricing breaches. Filing this lawsuit did not serve as proper notice. [Tudor, 681 N.E.2d at 10-11](#) ("Only a consumer buyer who suffers a personal injury may satisfy the [section 2-607](#) notice requirement by filing a complaint against the seller.") Plaintiffs do not claim that they provided any pre-lawsuit notice to Shell of the alleged nonconformities in pricing, and attempt to dismiss Shell's argument with a single irrelevant sentence. For these reasons, Shell's motion to dismiss count 8 is granted. [Klockner, 663 F.2d at 1380](#) (affirming judgment against purchaser's breach of warranty counterclaim on grounds that purchaser failed to provide pre-lawsuit notice of claimed breach under [section 2-607\(5\)\(a\)](#).)

### **Count 9 (Declaratory Judgment as to All Counts)**

Count 9 of the complaint essentially duplicates plaintiffs' other counts, except that instead of requesting damages, plaintiffs request declarations of the parties' rights and obligations under various agreements, as well as declarations [\*21] that Shell violated the statutes and common law rights under which plaintiffs claim for damages and other relief in counts 1-8. [HN8](#) Under the Declaratory Judgment Act, [28 U.S.C. § 2201 et seq.](#), "federal courts have discretion to decline to hear a declaratory judgment action, even though it is within their jurisdiction." [Tempco Elec. Heater Corp. v. Omega Eng'g, Inc., 819 F.2d 746, 747 \(7th Cir. 1987\)](#). Tempco notes that declaratory judgment is appropriate, among other instances, where, "the controversy has ripened to a point where one of the parties could invoke a coercive remedy (i.e. a suit for damages or an injunction) but has not done so." [Tempco, 819 F.2d at 749](#). In distinction, here there is a suit for damages underway (via counts 1-8) based on the same issues raised in count 9. Thus, the process for determination on the merits is underway in this suit, and the additional declaratory judgment action requested by plaintiffs is redundant. [Amari v. Radio Spirits, Inc., 219 F. Supp. 2d 942, 944 \(N.D. Ill. 2002\)](#), citing [Associated Mills, Inc. v. Regina Co., Inc., 675 F. Supp. 446, 448 \(N.D. Ill. 1987\)](#); [\*22] [Wireless Marketing Corp. v. Cherokee, Inc., No. 98C1406, 1998 U.S. Dist. LEXIS 16114 \(N.D. Ill. Oct. 6, 1998\)](#); [Resource Asset Mgmt., Inc. v. Continental Stock Transfer & Trust Co., 896 F. Supp. 782, 785 \(N.D. Ill. 1995\)](#) (dismissing declaratory judgment action where larger, more comprehensive substantive action was pending in same district); [Biosite, Inc. v. Xoma Ltd., 168 F. Supp. 2d 1161, 1165 \(N.D. Cal. 2001\)](#) (dismissing declaratory judgment action where similar substantive action involving more claims was pending in same district before same judge).

Additionally, fairness to the parties and judicial economy weigh in favor of dismissal of the declaratory judgment count here. [Amari, 219 F. Supp.2d at 944](#). Both parties will be able to have the substantive merits of their positions decided without plaintiffs' declaratory judgment claims, and the litigation will be made more efficient by eliminating the unnecessary declaratory judgment count. [Id. at 944-45](#). For these reasons, the court declines to exercise jurisdiction to hear count 9, and Shell's motion to dismiss count 9 is granted.

### **Leave [\*23] to Amend Complaint**

As to most counts, plaintiffs have requested in their response to Shell's motion to dismiss that they be allowed to amend their complaint as to any counts that are dismissed. Each of these requests is denied without prejudice. If plaintiffs would like to amend their complaint in light of this opinion (or for any other reason), they may do so in conformance with the applicable rules of the court within thirty days of the date of this Memorandum Opinion and Order.

Dated: May 25, 2005

ENTER:

Joan B. Gottschall

United States District Judge

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## **Confederated Tribes of Siletz Indians of Or. v. Weyerhaeuser Co.**

United States Court of Appeals for the Ninth Circuit

December 6, 2004, Argued and Submitted, Portland, Oregon ; May 31, 2005, Filed

Nos. 03-35669 and 03-35984

### **Reporter**

411 F.3d 1030 \*; 2005 U.S. App. LEXIS 9897 \*\*

CONFEDERATED TRIBES OF SILETZ INDIANS OF OREGON; SMOKEY POINT HARDWOOD, INC., Plaintiffs, ROSS-SIMMONS HARDWOOD LUMBER COMPANY, INC., Plaintiff-Appellee, v. WEYERHAEUSER COMPANY, Defendant-Appellant.

**Subsequent History:** Later proceeding at *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 126 S. Ct. 714, 163 L. Ed. 2d 566, 2005 U.S. LEXIS 8568 (U.S., 2005)

US Supreme Court certiorari granted by *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 126 S. Ct. 2965, 165 L. Ed. 2d 948, 2006 U.S. LEXIS 4908 (U.S., 2006)

Vacated by, Remanded by *Weyerhaeuser Co. v. Ross-Simmons Hardwood Lumber Co.*, 127 S. Ct. 1069, 166 L. Ed. 2d 911, 2007 U.S. LEXIS 1333 (U.S., Feb. 20, 2007)

**Prior History:** [\*\*1] Appeal from the United States District Court for the District of Oregon. D.C. No. CV-00-01693-OMP. Owen M. Panner, Senior District Judge, Presiding.

[Confederated Tribes of Siletz Indians of Or. v. Weyerhaeuser Co., 2003 U.S. Dist. LEXIS 25830 \(D. Or., Oct. 27, 2003\)](#)

**Disposition:** AFFIRMED.

## **Core Terms**

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sawlogs, prices, predatory, costs, bidding, overbidding, new trial, monopolization, barriers, anticompetitive conduct, probability, damages, attorney's fees, competitors, consumers, lumber, alder, monopoly power, hardwood, cases, matter of law, market power, jury's finding, award damages, achievement, recoupment, substantial evidence to support, market share, predation, buy-side

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

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Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

## **HN1** [down] Antitrust & Trade Law, Sherman Act

Section 2 of the Sherman Act, [15 U.S.C.S. § 2](#), provides in part that every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of an antitrust violation.

Civil Procedure > Appeals > Standards of Review > De Novo Review

## **HN2** [down] Standards of Review, De Novo Review

The appellate court applies a de novo standard of review to legal issues.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN3** [down] Monopolies & Monopolization, Actual Monopolization

Monopoly power exercised on the buy-side of the market is called "monopsony" power, and can violate [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#). Both sides of the market affect allocative efficiency, and hence consumer welfare. Antitrust laws are thus concerned with competition on the buy-side of the market as much as on the sell-side of the market.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > Predatory Pricing

Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview

Evidence > Burdens of Proof > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

## **HN4** [down] Anticompetitive & Predatory Practices, Predatory Pricing

In Brooke Group, the United States Supreme Court created a high standard of liability, holding that a plaintiff bringing a claim under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), based on predatory sell-side pricing must show

that: (1) the prices complained of are below an appropriate measure of its rival's costs; and (2) a dangerous probability existed that the rival would later recoup its investment in below-cost prices once it stopped such pricing. Thus, to establish liability under Brooke Group, a plaintiff must show that its competitor operated at a loss and was likely to recoup its losses.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Trials > Jury Trials > Province of Court & Jury

## **HN5** Antitrust & Trade Law, Sherman Act

The issue of whether specific conduct is anticompetitive in violation of the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), is one of law.

Governments > Courts > Judicial Precedent

## **HN6** Courts, Judicial Precedent

An appellate court must view its decisions in light of intervening United States Supreme Court decisions closely on point.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview

Civil Procedure > Judgments > Relief From Judgments > General Overview

Civil Procedure > Judgments > Relief From Judgments > Motions for New Trials

Civil Procedure > Appeals > Standards of Review > Abuse of Discretion

## **HN7** Standards of Review, De Novo Review

The appellate court generally reviews a district court's ruling on a motion for a new trial for an abuse of discretion. However, where the motion for a new trial rests solely on the ground that the jury instructions misstated the law, the appellate court reviews the district court's denial of the motion for a new trial de novo.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

411 F.3d 1030, \*1030L2005 U.S. App. LEXIS 9897, \*\*1

Civil Procedure > Judgments > Relief From Judgments > General Overview

Civil Procedure > Judgments > Relief From Judgments > Motions for New Trials

## **HN8** [down] Actual Monopolization, Monopoly Power

In *Eastman Kodak*, the United States Supreme Court held that a defendant violates the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), by using monopoly power to foreclose competition, to gain a competitive advantage, or to destroy a competitor.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > Trials > Judgment as Matter of Law > General Overview

## **HN9** [down] Standards of Review, De Novo Review

The appellate court reviews the district court's denial of a motion for judgment as a matter of law de novo.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Trials > Judgment as Matter of Law > General Overview

Evidence > Inferences & Presumptions > General Overview

Civil Procedure > ... > Standards of Review > Substantial Evidence > General Overview

## **HN10** [down] Antitrust & Trade Law, Sherman Act

To uphold a jury's verdict, the appellate court must find that substantial evidence supports it. Substantial evidence is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion. When reviewing the record as a whole, the appellate court must draw all reasonable inferences in favor of the nonmoving party, keeping in mind that credibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of a judge. In reviewing a defendant's entitlement to judgment as a matter of law in the antitrust context, the appellate court presumes that a reasonable jury knows and understands the law, the facts of the case, and the realities of the market.

Antitrust & Trade Law > Sherman Act > General Overview

Evidence > Burdens of Proof > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

## **HN11** [down] Antitrust & Trade Law, Sherman Act

To establish attempted monopolization under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), a plaintiff must demonstrate that the defendant: (1) engaged in predatory or anticompetitive conduct; (2) had a specific intent to monopolize; and

(3) a dangerous probability of the defendant's achievement of monopoly power in the relevant market existed. Additionally, the plaintiff must show causal antitrust injury.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Civil Procedure > Appeals > Standards of Review > General Overview

Civil Procedure > ... > Standards of Review > Substantial Evidence > General Overview

#### **HN12** [blue icon] **Monopolies & Monopolization, Attempts to Monopolize**

Where the district court instructs the jury separately regarding monopolization and attempted monopolization, and the jury enters separate liability verdicts on each of the counts, the appellate court can affirm the judgment if substantial evidence supports the jury's verdict as to either claim.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

Civil Procedure > ... > Standards of Review > Substantial Evidence > Sufficiency of Evidence

#### **HN13** [blue icon] **Actual Monopolization, Anticompetitive & Predatory Practices**

Anticompetitive or predatory acts are those that tend to exclude or restrict competition on some basis other than efficiency.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Evidence > Burdens of Proof > General Overview

#### **HN14** [blue icon] **Monopolies & Monopolization, Attempts to Monopolize**

Attempted monopolization requires proof of intent to monopolize or eliminate competition. Anticompetitive conduct alone can satisfy the specific intent requirement if the conduct forms the basis for a substantial claim of restraint of trade or is clearly threatening to competition or clearly exclusionary.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Evidence > Burdens of Proof > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

#### **HN15** [blue icon] **Monopolies & Monopolization, Attempts to Monopolize**

Monopoly power is the power to control prices or exclude competition. In determining whether there is a dangerous probability of monopolization, the court considers the relevant market and the defendant's ability to lessen or destroy competition in that market. To control prices unilaterally, the defendant must have obtained market power. A plaintiff can demonstrate that the defendant had market power either by presenting direct evidence of the injurious exercise of that power or by presenting circumstantial evidence that defined the relevant market, demonstrated that the defendant held a dominant share of the market, and showed that significant barriers to entry into and expansion within the market exist.

[Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview](#)

[Evidence > Burdens of Proof > General Overview](#)

[Evidence > Inferences & Presumptions > General Overview](#)

[Evidence > Inferences & Presumptions > Inferences](#)

## **[HN16](#) [blue icon] **Monopolies & Monopolization, Attempts to Monopolize****

Market share alone does not raise an inference of a dangerous probability of achieving monopoly power if there are low entry barriers or other evidence of a defendant's inability to control prices or exclude competitors. Entry barriers are additional long-run costs that were not incurred by incumbent firms but must be incurred by new entrants, or factors in the market that deter entry while permitting incumbent firms to earn monopoly returns. Such barriers may include legal license requirements, control of an essential resource, entrenched buyer preferences, and higher capital costs for new entrants. Entry barriers that justify a finding of market power must be capable of constraining the normal operation of the market to the extent that the problem is unlikely to be self-correcting. The entry of new competitors does not necessarily demonstrate a lack of barriers to entry. If new entrants are insufficient to take significant business away from the predator, they are unlikely to represent a challenge to the predator's market power.

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

[Civil Procedure > Appeals > Standards of Review > General Overview](#)

[Civil Procedure > Remedies > Damages > General Overview](#)

## **[HN17](#) [blue icon] **Private Actions, Remedies****

The appellate court gives substantial deference to a jury's damages award. In antitrust cases, the appellate court accepts a degree of uncertainty when evaluating damages awards because of the inherent difficulty of ascertaining business damages when the vagaries of the marketplace usually deny the court sure knowledge of what a plaintiff's situation would have been in the absence of the defendant's antitrust violation. The appellate court will affirm the jury's damages award if it is not based upon speculation or guesswork. It is sufficient if a reasonable basis of computation is afforded, although the result be only approximate.

[Civil Procedure > Appeals > Standards of Review > Abuse of Discretion](#)

[Antitrust & Trade Law > ... > Private Actions > Costs & Attorney Fees > General Overview](#)

[Civil Procedure > Remedies > Costs & Attorney Fees > General Overview](#)

Civil Procedure > Appeals > Standards of Review > General Overview

Civil Procedure > Appeals > Standards of Review > Clearly Erroneous Review

## **HN18** [blue icon] **Standards of Review, Abuse of Discretion**

The appellate court upholds a district court's award of attorneys' fees unless it abused its discretion or committed a clear error of law.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > Predatory Pricing

Civil Procedure > Trials > Judgment as Matter of Law > General Overview

Evidence > Burdens of Proof > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

## **HN19** [blue icon] **Anticompetitive & Predatory Practices, Predatory Pricing**

Brooke Group does not apply in a predatory bidding case because the benefit to consumers and stimulation of competition are less likely to result here than in predatory pricing cases. A plaintiff bringing a claim under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), based on predatory overbidding in a relatively inelastic market need not show that the defendant operated at a loss and that a dangerous probability of the defendant's recoupment of those losses existed to succeed on its claim.

**Counsel:** Stephen V. Bomse, M. Laurence Popofsky and Heather N. Leal, Heller Ehrman White & McAuliffe LLP, San Francisco, California, for the appellant.

Michael E. Haglund, Haglund, Kelley, Horngren & Jones, LLP, and Roy Pulvers, Lindsay, Hart, Neil & Weigler, LLP, Portland, Oregon, for the appellee.

**Judges:** Before: Thomas G. Nelson and Johnnie B. Rawlinson, Circuit Judges, and William W Schwarzer, \* Senior District Judge. Opinion by Judge T.G. Nelson.

**Opinion by:** Thomas G. Nelson

## **Opinion**

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[\*1033] T.G. NELSON, Circuit Judge:

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\* he Honorable William W Schwarzer, Senior United States District Judge for the Northern District of California, sitting by designation.

Ross-Simmons Hardwood Lumber Company brought this action against Weyerhaeuser Company for antitrust violations under [Section 2 of the Sherman Act](#).<sup>1</sup> [\*1034] Ross-Simmons alleged that Weyerhaeuser monopolized and attempted to monopolize the Pacific Northwest input market for alder sawlogs through its purchases of sawlogs. Ross-Simmons prevailed in a jury trial on both its monopolization [\*\*2] and attempted monopolization claims. After trebling the jury's damages award, the court entered judgment for Ross-Simmons and denied Weyerhaeuser's motion for judgment as a matter of law or for a new trial. The court also awarded attorneys' fees and costs to Ross-Simmons. Weyerhaeuser appeals the court's denial of its motion for judgment as a matter of law or for a new trial, and seeks reversal of the judgment. Weyerhaeuser also separately appeals the district court's award of attorneys' fees and costs to ensure that any reversal of the judgment or remand for a new trial would also result in reversal of the award of attorneys' fees and costs. We have jurisdiction under [28 U.S.C. § 1291](#), and we affirm.

### [\*\*3] I. BACKGROUND

The forests west of the Cascade Mountains in Oregon and Washington contain sufficient hardwood to support the only concentration of hardwood sawmills in the western United States. These mills are part of what is often called the "alder industry" after the area's predominant hardwood species, which accounts for 95% of the annual Pacific Northwest hardwood lumber production. The three principal players in the alder portion of the hardwood industry are: (1) timberland owners and loggers who supply alder sawlogs; (2) production facilities, including sawmills, that buy sawlogs and process them into finished alder lumber; and (3) purchasers who buy hardwood lumber from production facilities. Both parties in this case fall under the second category: they operate sawmills.

The plaintiff-appellee, Ross-Simmons Hardwood Lumber Company, was a pioneer in the alder lumber business, starting in 1962. It operated its mill in Longview, Washington continuously until it went out of business in 2001. From 1990 to 1997, Ross-Simmons experienced modest prosperity, but from 1998 to 2001, its production declined. From 1998 to 2001, sawlog prices increased while finished lumber prices [\*\*4] decreased. This was unusual: historically, the price of alder sawlogs fluctuated with the price of finished lumber. Because its materials costs went up and its production went down, Ross-Simmons incurred losses totaling nearly \$ 4.5 million, forcing it to shut down in 2001. Ross-Simmons blamed its failure on Weyerhaeuser.

The defendant-appellant, Weyerhaeuser Company, was established in 1900. In 1980, it acquired Northwest Hardwoods, Inc. (also "Weyerhaeuser"), and now owns six hardwood sawmills in the Pacific Northwest. Weyerhaeuser is one of the largest manufacturers of hardwood lumber in the world. From 1998 to 2001, the period in which Ross-Simmons's profits dropped, Weyerhaeuser's share of the Pacific Northwest market for alder sawlogs was approximately 65%.

Ross-Simmons alleged that Weyerhaeuser artificially increased sawlog prices to drive Ross-Simmons and other competitors out of business. At trial, Ross-Simmons offered testimony and other evidence to prove that Weyerhaeuser attempted to eliminate competitors by driving up sawlog prices and restricting access to sawlogs through: (1) predatory overbidding (i.e., paying a higher price for sawlogs than necessary); (2) overbuying [\*\*5] (i.e., buying more sawlogs than it needed); (3) entering restrictive or exclusive agreements with sawlog suppliers; and (4) making misrepresentations to state officials in order to obtain sawlogs from state forests. Weyerhaeuser attributed Ross-Simmons's failure [\*1035] to substandard equipment, inefficient operations, poor management, and inadequate capital investment.

The court instructed the jury on the applicable law, including the elements of both monopoly and attempted monopoly, the law regarding anticompetitive conduct in the form of predatory overbidding, and the issue of damages. With respect to overbidding, the court instructed the jury that, if it found that Weyerhaeuser paid higher

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<sup>1</sup> [15 U.S.C. § 2](#).  [Section 2 of the Sherman Act](#) provides, in relevant part, that "every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty" of an antitrust violation. *Id.*

prices than necessary for sawlogs, the jury could regard that as an anticompetitive act. The jury found for Ross-Simmons on both the monopolization and attempted monopolization claims, and awarded damages of \$ 26,256,406. After trebling the damages award, the court entered judgment in the amount of \$ 78,769,218 against Weyerhaeuser. The court then denied Weyerhaeuser's motion for judgment as a matter of law or for a new trial, and awarded attorneys' fees and costs to Ross-Simmons.

Weyerhaeuser appeals [\*\*6] the judgment, arguing that: (1) it is entitled to judgment as a matter of law because it had no market power in the alder sawlog market and the alleged anticompetitive acts were not actionable under § 2 of the Sherman Act, (2) it is entitled, in the alternative, to a new trial because the jury instructions misstated the law of predatory overbidding, and (3) it is entitled to reversal of the judgment because Ross-Simmons's damages theory was speculative. Weyerhaeuser also appeals the court's grant of attorneys' fees and costs to Ross-Simmons so that any reversal of the judgment or remand for a new trial would also result in reversal of the award of attorneys' fees and costs.

## II. ANALYSIS

Weyerhaeuser's challenges to the court's denial of its motion for judgment as a matter of law or for a new trial present us with a legal question of first impression: whether the prerequisites set forth in *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*<sup>2</sup> for establishing liability in sell-side predatory pricing cases apply in cases where a defendant engages in buy-side predatory bidding by raising the cost of inputs. We address this legal issue at the outset, HN2[<sup>↑</sup>] applying a de novo [\*\*7] standard of review.<sup>3</sup> For the reasons discussed below, we conclude that *Brooke Group* does not control in the buy-side predatory bidding context at issue here.

Our conclusion that *Brooke Group* does not apply here disposes of Weyerhaeuser's challenge regarding a new trial due to erroneous jury instructions in its entirety. The court properly instructed the jury regarding predatory overbidding. Our holding that *Brooke Group* is inapplicable also partially resolves Weyerhaeuser's challenge regarding judgment as a matter of law. Because Weyerhaeuser further contends that the evidence was insufficient to support the jury's verdict, we must examine that contention, however. After doing so, we conclude that substantial evidence did support the jury's finding of attempted monopolization. Thus, we affirm [\*\*8] the court's denial of Weyerhaeuser's motion for judgment as a matter of law or for a new trial.

Two issues remain unresolved after we address the issue related to *Brooke Group*. They are: (1) damages, and (2) attorneys' fees and costs. We resolve them as follows. First, we uphold the jury's award of damages because it was based upon an appropriate estimate of damages. Second, [\*1036] we conclude that the court properly granted attorneys' fees and costs in favor of Ross-Simmons. Accordingly, we affirm.

### A. ISSUES RELATED TO BROOKE GROUP

#### 1. Inapplicability of *Brooke Group*

HN3[<sup>↑</sup>] Monopoly power exercised on the buy-side of the market is called "monopsony" power, and can violate § 2 of the Sherman Act.<sup>4</sup> [\*\*9] Both sides of the market affect allocative efficiency, and hence consumer welfare.<sup>5</sup>

<sup>2</sup> [509 U.S. 209, 125 L. Ed. 2d 168, 113 S. Ct. 2578 \(1993\)](#).

<sup>3</sup> [Los Angeles Mem'l Coliseum Comm'n v. Nat'l Football League, 791 F.2d 1356, 1360 \(9th Cir. 1986\)](#) (stating that we review questions of law de novo).

<sup>4</sup> See [United States v. Syufy Enters., 903 F.2d 659, 663 n.4 \(9th Cir. 1990\)](#) ("Syufy II"); ROGER D. BLAIR & JEFFREY L. HARRISON, MONOPSONY: ANTITRUST LAW AND ECONOMICS at 68-81 (1993) (discussing monopsonist behavior that violates the Sherman Act).

Antitrust laws are thus concerned with competition on the buy-side of the market as much as on the sell-side of the market.<sup>6</sup>

[\*\*10] Weyerhaeuser argues that, regardless of whether a case involves sell-side predatory pricing or buy-side predatory bidding, the same standard of liability should apply. Weyerhaeuser invites the court to borrow the standard of liability set forth in *Brooke Group*, a sell-side predatory pricing case. [HN4](#)<sup>7</sup> In *Brooke Group*, the Court created a high standard of liability, holding that a plaintiff bringing a claim under [§ 2 of the Sherman Act](#) based on predatory sell-side pricing must show that: (1) "the prices complained of are below an appropriate measure of its rival's costs," and (2) "a dangerous probability" existed that the rival would later "recoup[] its investment in below-cost prices" once it stopped such pricing.<sup>8</sup> Thus, to establish liability under *Brooke Group*, a plaintiff had to show that its competitor operated at a loss and was likely to recoup its losses. Weyerhaeuser contends that the same standard should apply in buy-side predatory bidding cases. Specifically, Weyerhaeuser argues that the jury instructions were erroneous because the court did not instruct the jury that overbidding for sawlogs could be anticompetitive conduct only if Weyerhaeuser operated at a [\*\*11] loss and a dangerous probability of its recouping of losses existed.<sup>9</sup> Similarly, Weyerhaeuser argues that, as a matter of law,<sup>9</sup> the alleged predatory overbidding [**\*1037**] was not actionable anticompetitive conduct under the Sherman Act because Ross-Simmons did not satisfy the two *Brooke Group* requirements. We reject Weyerhaeuser's arguments regarding the applicability of *Brooke Group*.

[\*\*12] The *Brooke Group* Court established a high liability standard for sell-side predatory pricing cases because of its concern with the facts that consumers benefit from lower prices and that cutting prices often fosters competition.<sup>10</sup> The Court stated that "low prices benefit consumers regardless of how those prices are set, and so long as they are above predatory levels, they do not threaten competition."<sup>11</sup> The Court further recognized that above-cost pricing is either "competition on the merits, or is beyond the practical ability of a judicial tribunal to control without courting intolerable risks of chilling legitimate price-cutting."<sup>12</sup> As a result, the Court did not want to make the standard of liability "so low that antitrust suits themselves became a tool for keeping prices high."<sup>13</sup>

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<sup>5</sup> See BLAIR & HARRISON, *supra* note 5, at 36-61 (explaining the social welfare losses that result when a dominant buyer or collusive buyers set a non-optimal price for inputs).

<sup>6</sup> See, e.g., *Mandeville Island Farms, Inc. v. Am. Crystal Sugar Co.*, 334 U.S. 219, 227, 235-36, 92 L. Ed. 1328, 68 S. Ct. 996 (1948) (explaining that price fixing by a buyer's cartel violates §§ 1 and [2 of the Sherman Act](#)); *Am. Tobacco Co. v. United States*, 328 U.S. 781, 801-04, 90 L. Ed. 1575, 66 S. Ct. 1125 (1946) (stating that a conspiracy to increase prices of cheaper tobacco and thereby drive out manufacturers of lower-priced cigarettes violated [§ 2 of the Sherman Act](#)); *Reid Bros. Logging Co. v. Ketchikan Pulp Co.*, 699 F.2d 1292, 1298 n.5 (9th Cir. 1983) (discussing that a conspiracy to bid more for logs to drive competitors out was anticompetitive conduct); *National Macaroni Mfrs. Ass'n v. FTC*, 345 F.2d 421, 426-27 (7th Cir. 1965) (holding that an agreement of macaroni producers to reduce the amount of durum wheat purchased as an input for pasta production was per se unlawful); see also Blair & Harrison, *supra* note 5, at 68-81 (discussing cases).

<sup>7</sup> *Brooke Group*, 509 U.S. at 222, 223-24.

<sup>8</sup> The relevant jury instruction, as finally formulated, stated:

One of Plaintiffs' contentions in this case is that the Defendant purchased more logs than it needed or paid a higher price for logs than necessary, in order to prevent the Plaintiffs from obtaining the logs they needed at a fair price. If you find this to be true, you may regard it as an anticompetitive act.

<sup>9</sup> *Los Angeles Land Co. v. Brunswick Corp.*, 6 F.3d 1422, 1425 (9th Cir. 1993) (stating that [HN5](#)<sup>10</sup> the issue of "whether specific conduct is anticompetitive in violation of the Sherman Act is one of law").

<sup>10</sup> *Brooke Group*, 509 U.S. at 223, 226.

<sup>11</sup> *Id. at 223* (internal quotation marks and citation omitted).

<sup>12</sup> *Id.* (citation omitted).

[\*\*13] We recognize that in buy-side predatory bidding cases, as in sell-side predatory pricing cases, the price level itself is the anticompetitive weapon. However, an important factor distinguishes predatory bidding cases from predatory pricing cases: benefit to consumers and stimulation of competition do not necessarily result from predatory bidding the way they do from predatory pricing.<sup>14</sup> We turn now to the short-term and long-term effects of predatory bidding.

[\*\*14] In a predatory bidding scheme, a firm pays more for materials in the short term, and thereby attempts to squeeze out those competitors who cannot remain profitable when the price of inputs increases.<sup>15</sup> [\*\*15] No consumer benefit results during this predation period if the firm raises or maintains the same price level for its finished [\*1038] products. Although consumers might temporarily benefit if a firm lowered prices during the predation period, a reduction in prices would place even greater pressure on competitors, thereby increasing the threat to competition arising from the predatory bidding.<sup>16</sup> Thus, even though a short-term benefit to consumers might occur in some predatory bidding situations, serious concerns about the threat to competition would concurrently arise in those situations. Moreover, predatory bidding claims do not directly challenge a firm's decision to cut prices; instead, they focus on a firm's decision to raise the cost of inputs. Therefore, the concerns the *Brooke Group* Court expressed about depriving consumers of the temporary benefit of low prices do not necessarily apply when predatory bidding is at issue.<sup>17</sup>

In the long run, to carry out a predatory bidding scheme successfully, a firm would have to recoup the higher costs it had paid for its materials. If it succeeded in driving out competition, during this recoupment period the firm would likely pay less for its materials while charging consumers a higher price.<sup>18</sup> [\*\*16] The firm would have little incentive to pass on the benefit of lower input prices to consumers when it possessed greater market power and needed to recoup the higher costs it had paid for its materials. Thus, the overall effect of a predatory bidding scheme would result in harm to consumers.<sup>19</sup>

<sup>13</sup> [Id. at 226-27.](#)

<sup>14</sup> See [Wash. Alder LLC v. Weyerhaeuser Co., 2004 U.S. Dist. LEXIS 15269, 2004 WL 1717650, at \\*1 \(D. Or. July 27, 2004\)](#) ("Consumers don't benefit from higher raw material prices, or by logs rotting in the lumber yard. Nor is deliberately driving log prices up, simply to deprive competitors of logs, likely to be confused with legitimate competition."); John B. Kirkwood, *Buyer Power and Exclusionary Conduct: Should Brooke Group Set the Standards for Buyer-Induced Price Discrimination and Predatory Bidding?*, 72 ANTI-TRUST L.J. 625, 655 (2005) ("It seems indisputable that any negative impact of a predatory bidding case on downstream price competition is less direct and less certain than the impact of a predatory pricing case, which is a direct assault on a seller's decision to lower prices to its customers."); *id.* at 667 (stating that "because predatory bidding cases attack a firm's decision to increase prices, not reduce them, they do not represent a direct assault on price cutting"); Richard O. Zerbe, Jr., *Monopsony and the Ross-Simmons Case: A Comment on Salop and Kirkwood*, 72 ANTITRUST L.J. 717, 724 (2005) (stating that consumer harm can be presumed in the instant case because it involves "a limited, relatively inelastic, resource-based input market [for alder logs] and a much broader output market"). *But see* Steven C. Salop, *Anticompetitive Overbuying by Power Buyers*, 72 ANTITRUST L.J. 669, 702 (2005) (stating that "the difficulty of distinguishing an anticompetitive overbuying strategy from a competitive purchase expansion can be similar to the difficulties in predatory pricing matters" and that in some situations, "it may be difficult for a court to know whether the firm is attempting to predate or simply competing in the input market with rivals who are also purchasing the inputs").

<sup>15</sup> Kirkwood, *supra* note 15, 72 ANTITRUST L.J. at 652.

<sup>16</sup> In this case, the price of finished lumber decreased while the cost of sawlogs increased during the alleged predation period. It is unclear from the record whether lumber prices decreased because of a decision Weyerhaeuser made, or for other reasons.

<sup>17</sup> See [Brooke Group](#), 509 U.S. at 223, 226-27.

<sup>18</sup> See Kirkwood, *supra* note 15, 72 ANTITRUST L.J. at 653.

<sup>19</sup> We note that the recoupment phase of a predatory bidding scheme mirrors the recoupment phase of a predatory pricing scheme. See *id.*

Although in some situations rising input prices might encourage new companies to enter the supply side of the market and expand output, thereby increasing innovation and efficiency so that consumers benefit in the long run through price decreases and product improvements, this is not such a situation. The nature of the input supply at issue here does not readily allow for market expansion. The evidence shows that, during the alleged predation period, the supply of alder sawlogs remained relatively stable or declined. Nothing suggests this situation will change -- alder sawlogs are "a natural resource of limited annual supply in a relatively inelastic market." <sup>20</sup> Thus, at least in this case, predatory bidding is less likely than predatory pricing to result in a benefit to consumers or the stimulation of competition. As a result, the concerns that led the *Brooke Group* Court to establish a high standard of liability in the predatory pricing context do [\[\\*\\*17\]](#) not carry over to this predatory bidding context with the same force. Therefore, the standard for liability in this predatory bidding case need not be as high as in predatory pricing cases. Accordingly, we hold that the high standard of liability in *Brooke Group* does not apply here because this case involves predatory bidding in a relatively inelastic market, not predatory pricing.

Our decision in *Reid Bros. Logging Co. v. Ketchikan Pulp Co.*<sup>21</sup> [\[\\*\\*19\]](#) provides further support for our holding today that the prerequisites in *Brooke Group* do not apply [\[\\*1039\]](#) here. Although the Supreme Court decided *Brooke Group* after we decided *Reid Bros.*,<sup>22</sup> *Brooke Group* involved a different factual situation and did not overrule *Reid Bros.*<sup>23</sup> In *Reid Bros.*, we affirmed a finding [\[\\*\\*18\]](#) of liability under [§ 1 of the Sherman Act](#) that was based in part on a predatory buying claim.<sup>24</sup> The plaintiff in *Reid Bros.* argued that the defendants conspired to bid preclusively on timber sales at higher prices than necessary to block the plaintiff from buying necessary timber.<sup>25</sup> The defendants argued that the district court erred by finding predatory bidding when there was no evidence that the high prices paid for timber would prevent the defendants from covering their marginal costs on the ultimate sale of the processed timber.<sup>26</sup> We rejected the defendants' argument and held that such a "blind application of a numerical test would only frustrate the intent of the Sherman Act."<sup>27</sup> This statement that a rigid, numerical test should not apply when a buy-side overbidding scheme was at issue further supports our holding that *Brooke Group* is inapplicable here. Thus, our conclusion that *Brooke Group* does not apply is consistent with our precedent. We now turn to the effect our conclusion has on Weyerhaeuser's arguments for a new trial and for judgment as a matter of law.

## 2. New Trial

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<sup>20</sup> See Zerbe, *supra* note 15, 72 ANTITRUST L.J. at 722 (explaining that the alder sawlog market is "highly inelastic," in part because the alder harvest is a byproduct of the more important softwood harvest).

<sup>21</sup> [699 F.2d 1292](#).

<sup>22</sup> See **United States v. Gay**, [967 F.2d 322, 327 \(9th Cir. 1992\)](#) (stating that [HN6](#) we must view our decisions in light of intervening Supreme Court decisions closely on point).

<sup>23</sup> See *Brooke Group*, [509 U.S. at 214-16](#).

<sup>24</sup> *Reid Bros.*, [699 F.2d at 1297-98](#). [Section 1 of the Sherman Act](#) prohibits "every contract, combination . . . , or conspiracy[] in restraint of trade or commerce." [15 U.S.C. § 1](#).

<sup>25</sup> See *Reid Bros.*, [699 F.2d at 1297-98](#).

<sup>26</sup> *Id. at 1298 n.5*.

<sup>27</sup> *Id.*

**HN7** [↑] We generally review a court's ruling on a motion for a new trial for an abuse of discretion.<sup>28</sup> However, because Weyerhaeuser's motion for a new trial rested solely on the ground that the jury instructions misstated the law regarding Ross-Simmons's overbidding claim, we review the court's denial of the motion for a new trial de novo.<sup>29</sup> [\*\*21] Because we hold today that *Brooke Group* does not govern in this case, the court did not need to instruct the jury that overbidding for sawlogs [\*\*20] could be anticompetitive conduct only if Weyerhaeuser operated at a loss and a dangerous probability of Weyerhaeuser's recoupment of its losses existed. The instructions as a whole provided sufficient guidance regarding how to determine whether conduct was anticompetitive.<sup>30</sup>

[\*\*22] [\*\*1040] Moreover, the instructions were consistent with **HN8** [↑] Supreme Court precedent stating that a defendant violates the Sherman Act by using monopoly power "to foreclose competition, to gain a competitive advantage, or to destroy a competitor."<sup>31</sup> Thus, the jury instructions "fairly and adequately covered the issues presented, correctly stated the law, and were not misleading."<sup>32</sup> Accordingly, we affirm the court's denial of Weyerhaeuser's motion for a new trial.

### 3. Judgment as a Matter of Law

**HN9** [↑] "We review [the] district court's denial of [the] motion for judgment as a matter of law de novo."<sup>33</sup> Our holding regarding the inapplicability of *Brooke Group* [\*\*23] resolves one of the issues related to Weyerhaeuser's challenge to the denial of judgment as a matter of law: Weyerhaeuser's contention that, as a matter of law, the

<sup>28</sup> [Janes v. Wal-Mart Stores Inc., 279 F.3d 883, 886 \(9th Cir. 2002\)](#).

<sup>29</sup> [Costa v. Desert Palace, Inc., 299 F.3d 838, 858 \(9th Cir. 2002\)](#) (en banc) (stating that "we generally review the formulation of instructions for an abuse of discretion, but whether an instruction misstates the law is a legal issue reviewed de novo"), aff'd, [539 U.S. 90, 156 L. Ed. 2d 84, 123 S. Ct. 2148 \(2003\)](#). Whether we review the denial of a new trial under the abuse of discretion standard or de novo standard matters little here because "[a] district court by definition abuses its discretion when it makes an error of law." See [Del Monte Dunes at Monterey, Ltd. v. City of Monterey, 95 F.3d 1422, 1426 \(9th Cir. 1996\)](#) (quoting [Koon v. United States, 518 U.S. 81, 100, 135 L. Ed. 2d 392, 116 S. Ct. 2035 \(1996\)](#)), aff'd, [526 U.S. 687, 143 L. Ed. 2d 882, 119 S. Ct. 1624 \(1999\)](#).

<sup>30</sup> The court instructed the jury regarding anticompetitive conduct as follows:

Anti-competitive conduct is conduct that has the effect of wrongly preventing or excluding competition, or frustrating or impairing the efforts of other firms to compete for customers within the relevant market, making it very difficult or impossible for competitors to engage in fair competition. Not everything that enables a company to gain or maintain a monopoly is anti-competitive.

In deciding whether conduct is anti-competitive, you should consider whether the conduct lacks a valid business purpose, or unreasonably or unnecessarily impedes the efforts of other firms to compete for raw materials or customers, or if the anticipated benefits of the conduct flow primarily from its tendency to hinder or eliminate competition. Anti-competitive conduct does not include ordinary means of competition, such as offering better products or services, exercising superior skill or business judgment, utilizing more efficient technology, better marketing, or exercising natural competitive advantages such as unique geographic access to raw materials or markets.

....

One of Plaintiffs' contentions in this case is that the Defendant purchased more logs than it needed or paid a higher price for logs than necessary, in order to prevent the Plaintiffs from obtaining the logs they needed at a fair price. If you find this to be true, you may regard it as an anti-competitive act.

<sup>31</sup> [Eastman Kodak Co. v. Image Tech. Servs., Inc., 504 U.S. 451, 482-83, 119 L. Ed. 2d 265, 112 S. Ct. 2072 \(1992\)](#) (quoting [United States v. Griffith, 334 U.S. 100, 107, 92 L. Ed. 1236, 68 S. Ct. 941 \(1948\)](#)).

<sup>32</sup> See [Mockler v. Multnomah County, 140 F.3d 808, 812 \(9th Cir. 1998\)](#) (internal quotation marks and citation omitted).

<sup>33</sup> [Janes, 279 F.3d at 886](#) (italics omitted).

alleged predatory overbidding could not be actionable anticompetitive conduct under [§ 2 of the Sherman Act](#) because Ross-Simmons did not show that Weyerhaeuser operated at a loss and that a dangerous probability of Weyerhaeuser's recoupment of its losses existed. Because *Brooke Group* does not apply in this case, Ross-Simmons did not have to meet the high standard of liability in *Brooke Group* before relying upon predatory overbidding to satisfy the anticompetitive conduct requirement. Our holding regarding *Brooke Group* does not resolve Weyerhaeuser's argument that Ross-Simmons's evidence was insufficient to support the jury's verdict, however. Accordingly, we now turn to the issue of whether substantial evidence supports the jury's verdict.<sup>34</sup> We conclude that the record contains substantial evidence.

[\*\*24] "Substantial evidence is such relevant evidence as a reasonable mind might accept as adequate to support a conclusion."<sup>35</sup> When reviewing the record as a whole, we must draw all reasonable inferences in favor of the nonmoving party, keeping in mind that "credibility determinations, the weighing of the evidence, and [\*1041] the drawing of legitimate inferences from the facts are jury functions, not those of a judge."<sup>36</sup> In reviewing a defendant's entitlement to judgment as a matter of law in the antitrust context, we presume that "a reasonable jury . . . know[s] and understand[s] the law, the facts of the case, and the realities of the market."<sup>37</sup>

[HN11](#) [↑] To establish attempted monopolization under [\*\*25] [§ 2 of the Sherman Act](#),<sup>38</sup> [\*\*26] Ross-Simmons had to demonstrate that Weyerhaeuser: (1) engaged in predatory or anticompetitive conduct, (2) had a specific intent to monopolize, and (3) a dangerous probability of Weyerhaeuser's achievement of monopoly power in the relevant market existed.<sup>39</sup> Additionally, Ross-Simmons had to show causal antitrust injury.<sup>40</sup> We first examine whether the record contains substantial evidence of anticompetitive conduct.

#### a. Anticompetitive conduct

[HN13](#) [↑] Anticompetitive or predatory acts are those that tend to exclude or restrict competition "on some basis other than efficiency."<sup>41</sup> The record contains substantial evidence of over-bidding for sawlogs to support the jury's finding of anticompetitive conduct. The evidence shows that during the period of alleged predation: (1) sawlog prices increased while prices for finished lumber decreased, (2) Weyerhaeuser had a dominant share of the market

<sup>34</sup> [HN10](#) [↑] To uphold the jury's verdict, we must find that substantial evidence supports it. *Gilbrook v. City of Westminster*, 177 F.3d 839, 856 (9th Cir. 1999).

<sup>35</sup> [Syufy Enters. v. Am. Multicinema, Inc.](#), 793 F.2d 990, 992 (9th Cir. 1986) (internal quotation marks and citation omitted) ("Syufy I").

<sup>36</sup> [Anderson v. Liberty Lobby, Inc.](#), 477 U.S. 242, 255, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986).

<sup>37</sup> See [Brooke Group](#), 509 U.S. at 243.

<sup>38</sup> [HN12](#) [↑] Because the court instructed the jury separately regarding monopolization and attempted monopolization, and the jury entered separate liability verdicts on each of the counts, we can affirm the judgment if substantial evidence supports the jury's verdict as to either claim. See [Del Monte Dunes](#), 95 F.3d at 1426 (stating that the court could affirm the judgment on either of two alleged violations when the district court instructed the jury that it should award damages to the plaintiff if it found for the plaintiff on any alleged violation). We conclude below that substantial evidence supports the jury's verdict on the attempted monopolization claim. Therefore, we do not address the monopolization claim.

<sup>39</sup> [Spectrum Sports, Inc. v. McQuillan](#), 506 U.S. 447, 456, 122 L. Ed. 2d 247, 113 S. Ct. 884 (1993); [Rebel Oil Co. v. Atlantic Richfield Co.](#), 51 F.3d 1421, 1432-33 (9th Cir. 1995).

<sup>40</sup> [Rebel Oil](#), 51 F.3d at 1433. Weyerhaeuser does not address this element, presumably because if Ross-Simmons's theory that high sawlog prices drove it out of business is viable, Ross-Simmons has satisfied the injury element. Thus, we do not discuss it.

<sup>41</sup> See [Aspen Skiing Co. v. Aspen Highlands Skiing Corp.](#), 472 U.S. 585, 605, 86 L. Ed. 2d 467, 105 S. Ct. 2847 (1985) (internal quotation marks and citation omitted).

for alder sawlogs and an ability to control alder sawlog prices, (3) Weyerhaeuser suffered declining profits due to the high prices it was paying for raw materials, **[\*\*27]** and (4) Weyerhaeuser employed a strategy of raising sawlog prices. Based on this evidence, the jury could reasonably have concluded that Weyerhaeuser engaged in anticompetitive conduct by overbidding for sawlogs. We need not analyze whether substantial evidence supports the other alleged anticompetitive acts because the evidence of predatory overbidding sufficiently supports the finding that Weyerhaeuser engaged in anticompetitive conduct.<sup>42</sup> We now turn to the issue of whether substantial **[\*1042]** evidence supports the jury's finding of specific intent.

**[\*\*28] b. Specific intent**

**HN14**  Attempted monopolization requires proof of intent to monopolize or eliminate competition.<sup>43</sup> The record contains substantial evidence of specific intent to eliminate competition based on: (1) Weyerhaeuser's anticompetitive conduct itself, (2) the testimony of Weyerhaeuser's employees, and (3) Weyerhaeuser's business projections regarding sawlog prices.

Anticompetitive conduct alone can satisfy the specific intent requirement if the conduct "form[s] the basis for a substantial claim of restraint of trade" or is "clearly threatening to competition or clearly exclusionary."<sup>44</sup> As discussed above, Ross-Simmons offered evidence that Weyerhaeuser overpaid for sawlogs while its profits declined. Weyerhaeuser's overbidding for sawlogs clearly threatened competition because it restricted competitors' access to the limited supply of sawlogs. Thus, Weyerhaeuser's conduct on its own supports a reasonable inference of specific intent to eliminate **[\*\*29]** competition.

The testimony of Weyerhaeuser's employees further showed that Weyerhaeuser intended to control prices and eliminate competition. One of Weyerhaeuser's former senior analysts, Eugene Novak, acknowledged on the stand that Weyerhaeuser had the power -- and was aware of its power -- to influence prices in the alder sawlog market. Novak also authored a memorandum regarding the costs of sawlogs and lumber in which he stated that the increase in sawlog prices despite Weyerhaeuser's predominant market share made no sense. Novak estimated that, due to the excessive prices Weyerhaeuser paid for sawlogs, it "had given up some \$ 40 to \$ 60 million dollars in the last three years." He testified that his boss, Vicki McInnally, who was a member of the senior management team, **[\*\*30]** told him that "that was the strategy that [Weyerhaeuser] designed." A former sales manager for Weyerhaeuser, Cliff Chulos, also testified that "it was taken as a given by everyone that [Weyerhaeuser] could influence price; that [Weyerhaeuser] had to be a major influence." Thus, the testimony in the record supports the finding that Weyerhaeuser specifically intended to eliminate competition.

Moreover, Weyerhaeuser's business projections about sawlog prices indicated that it planned to lower the prices it paid for sawlogs after acquiring a greater market share as a result of decreased competition. Weyerhaeuser tracked competitors' profit margins and estimated the potential effects of targeted increases in sawlog costs on the ability of low-margin competitors to survive. Such evidence also supports an inference that Weyerhaeuser sought to foreclose competition rather than simply to increase its own business.<sup>45</sup> Thus, when viewed in its entirety, the evidence sufficiently supports a finding of specific intent to control prices and eliminate competition. We now turn to

<sup>42</sup> See *Coastal Abstract Serv., Inc. v. First Am. Title Ins. Co.*, 173 F.3d 725, 736 (9th Cir. 1999) (affirming judgments of liability on defamation claims where two of the three statements upon which jury verdicts were based were not actionable as a matter of law). The other alleged anticompetitive acts were: overbuying sawlogs, entering into exclusive agreements for sawlogs, and making misrepresentations to state officials to obtain sawlogs from state forests.

<sup>43</sup> *Spectrum Sports*, 506 U.S. at 456.

<sup>44</sup> *Twin City Sportservice, Inc. v. Charles O. Finley & Co.*, 676 F.2d 1291, 1309 (9th Cir. 1982); see *Spectrum Sports*, 506 U.S. at 459 (stating that unfair tactics can suffice to prove intent to monopolize).

<sup>45</sup> See IIIA AREEDA & HOVENKAMP, *ANTITRUST LAW*, P 805b at 340 n.10 (2d ed. 2002) ("In a perfectly competitive market[,] a firm makes price and output decisions without regard to the likely responses of others.").

the question of whether substantial evidence supports the finding that a dangerous probability of Weyerhaeuser's [\*\*31] achievement of monopoly power existed.

[\*1043] c. Dangerous probability of achieving monopoly power

**HN15** [+] Monopoly power is the "power to control prices or exclude competition." <sup>46</sup> In determining whether there is a dangerous probability of monopolization, we consider "the relevant market and the defendant's ability to lessen or destroy competition in that market." <sup>47</sup> To control prices unilaterally, Weyerhaeuser had to have obtained market power. <sup>48</sup> Ross-Simmons could demonstrate that Weyerhaeuser had market power either by presenting direct evidence of the injurious exercise of that power or by presenting circumstantial evidence that: defined the relevant market, demonstrated that the defendant held a dominant share of the market, and showed that significant barriers to entry into and expansion within [\*\*32] the market exist. <sup>49</sup> We hold that substantial evidence supports the jury's finding that a dangerous probability of Weyerhaeuser's achievement of monopoly power existed.

The record contains some direct evidence that could support the jury's finding that a dangerous probability of Weyerhaeuser's achievement of monopoly power existed. The testimony from Weyerhaeuser's employees showed that Weyerhaeuser had the power to influence prices and had used its power to raise the price of sawlogs. This direct evidence of Weyerhaeuser's injurious exercise of market power is substantial enough by itself to support the jury's [\*\*33] finding of a dangerous probability of achieving monopoly power. We nonetheless examine the circumstantial evidence as well because that evidence provides additional support for the jury's finding.

(i) Market share

Weyerhaeuser does not dispute Ross-Simmons's data that, during the relevant time period, Weyerhaeuser's share of the relevant market was approximately 65%. Weyerhaeuser's business records showed that its share was 64% in 1998, with projected increases. We have held a 44% market share sufficient as a matter of law to support a finding of market power for attempted monopolization. <sup>50</sup> Thus, we conclude that Weyerhaeuser's approximately 65% market share supports a finding of market power.

**HN16** [+] Market share alone, however, does not raise an inference of a dangerous [\*\*34] probability of achieving monopoly power if there are "low entry barriers or other evidence of a defendant's inability to control prices or exclude competitors." <sup>51</sup> We therefore turn to the issue of whether significant barriers to entry and expansion existed.

(ii) Barriers to entry and expansion

<sup>46</sup> [United States v. Grinnell Corp., 384 U.S. 563, 571, 16 L. Ed. 2d 778, 86 S. Ct. 1698 \(1966\)](#) (internal quotation marks and citation omitted).

<sup>47</sup> [Spectrum Sports, 506 U.S. at 456](#). Weyerhaeuser does not dispute that the relevant market consists of the market for alder sawlogs in the Pacific Northwest.

<sup>48</sup> See [Rebel Oil, 51 F.3d at 1434](#).

<sup>49</sup> *Id.*

<sup>50</sup> [Id. at 1438](#); see also [Oahu Gas Serv., Inc. v. Pac. Res., Inc., 838 F.2d 360, 366-67 \(9th Cir. 1988\)](#) (finding a declining 68 market share sufficient to establish market power for an actual monopolization claim).

<sup>51</sup> [Syufy II, 903 F.2d at 664](#) (citations omitted).

"Entry barriers are additional long-run costs that were not incurred by incumbent firms but must be incurred by new entrants, or factors in the market that deter entry while permitting incumbent firms to earn monopoly returns."<sup>52</sup> Such [**\*1044**] barriers may include legal license requirements, control of an essential resource, entrenched buyer preferences, and higher capital costs for new entrants.<sup>53</sup> Entry barriers that justify a finding of market power must "be capable of constraining the normal operation of the market to the extent that the problem is unlikely to be self-correcting."<sup>54</sup> We conclude that the high capital costs new entrants faced and the [**\*\*35**] limited availability of sawlogs were barriers to entry that justified an inference of monopoly power.

At the outset, we address Weyerhaeuser's argument that the entry of four new mills during the alleged predation period demonstrated a lack of barriers to entry. We have held that the entry of new competitors does not necessarily demonstrate a lack of barriers to entry.<sup>55</sup> If new entrants are "insufficient to take *significant* business away from the predator, they are unlikely to represent a challenge to the predator's market power."<sup>56</sup> The evidence did not show that the four new entrants took significant business from Weyerhaeuser or that they had a significant market share. In fact, evidence suggests that Weyerhaeuser's market share actually *increased* even though the [**\*\*36**] four new mills entered the market.<sup>57</sup> Moreover, the evidence indicates that, as soon as the new entrants came into the market, they had to pay the sawlog prices Weyerhaeuser set. Thus, the evidence does not show that the four new entrants could take enough business away from Weyerhaeuser to allow the market to correct itself.<sup>58</sup> As a result, the entry of new competitors did not foreclose the possibility that barriers to entry existed. We now turn to the issue of whether higher capital costs and limited sawlog availability were barriers to entry.

Ross-Simmons offered expert testimony to support the proposition that the higher capital costs associated with entering [**\*\*37**] the market constituted a barrier to entry. The record contains evidence that the advent of expensive new machines and product-grading, which did not exist when Weyerhaeuser entered the market, made market entry less feasible because new entrants had difficulty matching the necessary technology. The need for this new technology raised the cost of entering the market to \$ 20-\$ 25 million. While Weyerhaeuser also had to incur costs for machinery and product-grading, it was able to do so over time without bearing the burden of heavy front-end costs to gain entry into the market. Thus, substantial evidence supports the inference that higher capital costs were a barrier to entry.

With respect to the availability of raw materials, Weyerhaeuser argues that there were sufficient sawlogs available for all competitors if they could afford to buy them. However, Weyerhaeuser purchased approximately 65% of the available sawlogs during the period of alleged predation. The evidence further shows that Weyerhaeuser raised the price of sawlogs and entered into exclusive agreements that restricted competitors' access to sawlogs. By thus controlling or influencing a number of the available sawlog sources, [**\*\*38**] Weyerhaeuser restricted access to the already limited sawlog supply.<sup>59</sup> Weyerhaeuser's [**\*1045**] dominance in the market for sawlogs, its overbidding

<sup>52</sup> [Rebel Oil, 51 F.3d at 1439](#) (internal citations and quotation marks omitted).

<sup>53</sup> [Id.; Brunswick, 6 F.3d at 1428.](#)

<sup>54</sup> [Rebel Oil, 51 F.3d at 1439](#) (citation omitted).

<sup>55</sup> [Id. at 1440.](#)

<sup>56</sup> *Id.* (emphasis added).

<sup>57</sup> This increase in Weyerhaeuser's market share was likely due to the fact that although four new mills opened to compete with Weyerhaeuser during the alleged period of predation, thirty-one other competitors went out of business.

<sup>58</sup> See [id. at 1439](#).

<sup>59</sup> See [Syufy II, 903 F.2d at 667](#) (stating that an incumbent's control over a scarce commodity might give it a "substantial structural advantage").

practices, and its restrictive arrangements together support the inference that the limited supply of sawlogs was a barrier to entry.

The evidence shows that significant barriers to entry existed in the sawlog market in the form of high capital costs and limited raw materials, and that Weyerhaeuser had a dominant share of the market. Moreover, the record contains direct evidence of Weyerhaeuser's injurious exercise of market power. Therefore, we hold that substantial evidence supports the jury's finding that a dangerous probability of Weyerhaeuser's achievement of monopoly power existed.

Because substantial evidence shows that Weyerhaeuser engaged in anticompetitive conduct through predatory overbidding, intended [\*\*39] specifically to eliminate competition, and a dangerous probability of Weyerhaeuser's achievement of monopoly power existed, we uphold the jury's verdict against Weyerhaeuser on the attempted monopolization claim. Accordingly, we affirm the court's denial of Weyerhaeuser's motion for judgment as a matter of law.

## B. REMAINING ISSUES

Two issues remain for our consideration: (1) damages, and (2) attorneys' fees and costs. For the reasons stated below, we uphold both the jury's damages award and the court's grant of fees and costs to Ross-Simmons.

### 1. Damages

**HN17** We give substantial deference to a jury's damages award.<sup>60</sup> In antitrust cases, we accept a degree of uncertainty when evaluating damages awards because of the inherent "difficulty of ascertaining business damages" when "the vagaries of the marketplace usually deny us sure knowledge of what [a] plaintiff's situation would have been in the absence of the defendant's antitrust violation."<sup>61</sup> We will affirm the jury's damages award if it is not based upon "speculation or guesswork."<sup>62</sup> "It is sufficient if a reasonable basis of computation is afforded, although the result be only approximate."<sup>63</sup> We conclude that [\*\*40] the jury based its award upon an appropriate estimate of damages.

Ross-Simmons's models for estimating damages properly relied upon the fundamental assumption that Weyerhaeuser maintained artificially high costs in the sawlog market during the damages period. Ross-Simmons's estimates were based either on testimony regarding Weyerhaeuser's annual loss in profits due to higher sawlog costs or on a decade's worth of data regarding Weyerhaeuser's [\*\*41] average profit margin prior to the predatory period. The models accounted for changing market conditions by: (1) using data for actual sales and production of finished lumber, which took into account any reduced market demand or decrease in market prices for finished lumber, and (2) assuming that Weyerhaeuser could have controlled sawlog costs to maintain its previous profit [**\*1046**] margins relative to the price of lumber. The evidence, as discussed above, supports the assumption that Weyerhaeuser had such control. Thus, we conclude that Ross-Simmons's damages models were not speculative, but provided a reasonable basis for computing damages. Accordingly, we uphold the jury's award of damages.

<sup>60</sup> *Del Monte Dunes*, 95 F.3d at 1435; see *Los Angeles Mem'l*, 791 F.2d at 1360.

<sup>61</sup> *J. Truett Payne Co. v. Chrysler Motors Corp.*, 451 U.S. 557, 566-67, 68 L. Ed. 2d 442, 101 S. Ct. 1923 (1981); see *Bigelow v. RKO Radio Pictures, Inc.*, 327 U.S. 251, 264-65, 90 L. Ed. 652, 66 S. Ct. 574 (1946); *Eastman Kodak Co. v. S. Photo Materials Co.*, 273 U.S. 359, 379, 71 L. Ed. 684, 47 S. Ct. 400 (1927).

<sup>62</sup> *Bigelow*, 327 U.S. at 264.

<sup>63</sup> *S. Photo*, 273 U.S. at 379.

## 2. Attorneys' Fees and Costs

**HN18** [↑] We uphold a court's award of attorneys' fees unless it abused its discretion or committed a clear error of law.<sup>64</sup> Because we affirm the jury's verdict of liability for attempted monopolization, Ross-Simmons remains a prevailing party entitled to attorneys' fees and costs. Thus, the district court properly granted attorneys' fees and costs to Ross-Simmons.

## [\*\*42] III. CONCLUSION

We conclude that **HN19** [↑] *Brooke Group* does not apply in this predatory bidding case because benefit to consumers and stimulation of competition are less likely to result here than in predatory pricing cases. A plaintiff bringing a claim under *§ 2 of the Sherman Act* based on predatory overbidding in a relatively inelastic market need not show that the defendant operated at a loss and that a dangerous probability of the defendant's recoupment of those losses existed to succeed on its claim. Substantial evidence supports the jury's finding that Weyerhaeuser was liable for attempted monopolization. Therefore, we affirm the court's denial of Weyerhaeuser's motion for judgment as a matter of law or for a new trial. The jury based its damages award upon a reasonable estimate of damages. Therefore, we affirm the jury's damages award. Finally, because we affirm the jury's verdict, we also affirm the court's award of attorneys' fees and costs to Ross-Simmons.

**AFFIRMED.**

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<sup>64</sup> *Hasbrouck v. Texaco, Inc.*, 879 F.2d 632, 635 (9th Cir. 1989).

## Shaw v. United States

United States District Court for the Eastern District of New York

May 31, 2005, Decided

03-CV-3016 (ADS) (ARL)

**Reporter**

371 F. Supp. 2d 265 \*; 2005 U.S. Dist. LEXIS 10479 \*\*; 2005-1 Trade Cas. (CCH) P74,820

EDWARD SHAW, Petitioner, - against - UNITED STATES OF AMERICA, Respondent.

**Disposition:** **[\*\*1]** Petitioner's motion to set aside or vacate judgment of conviction pursuant to [28 U.S.C. § 2255](#) denied; Pursuant to *Rule 22(b) of Federal Rules of Appellate Procedure* and [28 U.S.C. § 2253\(c\)\(2\)](#), a certificate of appealability DENIED, as Petitioner fails to make a substantial showing of a denial of a constitutional right.

### **Core Terms**

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bid, auction, antitrust, co-conspirators, conspiracy, guilty plea, commerce, ineffective assistance of counsel, sentence, counsel's performance, relevant market

### **LexisNexis® Headnotes**

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Criminal Law & Procedure > Habeas Corpus > Review > Burdens of Proof

Criminal Law & Procedure > Sentencing > Corrections, Modifications & Reductions > General Overview

Criminal Law & Procedure > Postconviction Proceedings > Motions to Set Aside Sentence

Criminal Law & Procedure > Postconviction Proceedings > Motions to Vacate Judgment

Criminal Law & Procedure > ... > Jurisdiction > Cognizable Issues > Sentences

Criminal Law & Procedure > ... > Custody Requirement > Custody Determinations > Satisfaction of Custody

Criminal Law & Procedure > Habeas Corpus > Procedure > General Overview

#### **HN1 [blue icon] Review, Burdens of Proof**

Pursuant to [28 U.S.C.S. § 2255](#), a federal prisoner in custody may move the court which imposed the sentence to vacate, set aside or correct the sentence on the basis that it was imposed in violation of the Constitution or laws of the United States, or that the court was without jurisdiction to impose such sentence, or that the sentence was in excess of the maximum authorized by law, or is otherwise subject to collateral attack. [28 U.S.C.S. § 2255](#). The burden of proof is on the petitioner to establish his constitutional claims by a preponderance of the evidence.

371 F. Supp. 2d 265, \*265L<sup>2005 U.S. Dist. LEXIS 10479, \*\*1</sup>

Constitutional Law > ... > Fundamental Rights > Criminal Process > Assistance of Counsel

Criminal Law & Procedure > ... > Jurisdiction > Cognizable Issues > Ineffective Assistance of Counsel

Criminal Law & Procedure > Postconviction Proceedings > Motions to Set Aside Sentence

Criminal Law & Procedure > ... > Jurisdiction > Cognizable Issues > General Overview

## **HN2** [down] **Criminal Process, Assistance of Counsel**

Although generally a petitioner who has failed to raise an issue on direct appeal may not do so in a [28 U.S.C.S. § 2255](#) petition claims of ineffective assistance of counsel may be brought for the first time in a [§ 2255](#) petition. Such is the case because such claims would not likely be made on direct appeal by an attorney who had represented the petitioner at trial based upon that attorney's own incompetence. In addition, the district court is the forum best suited to developing the facts necessary to determining the adequacy of representation.

Civil Procedure > Parties > Pro Se Litigants > General Overview

Criminal Law & Procedure > Habeas Corpus > Procedure > General Overview

## **HN3** [down] **Parties, Pro Se Litigants**

With regard to a petition for a federal writ of habeas corpus, if the petitioner is proceeding pro se his submissions must be liberally construed in favor of the petitioner.

Constitutional Law > ... > Fundamental Rights > Criminal Process > Assistance of Counsel

Criminal Law & Procedure > Counsel > Effective Assistance of Counsel > Tests for Ineffective Assistance of Counsel

## **HN4** [down] **Criminal Process, Assistance of Counsel**

To establish ineffective assistance of counsel, a petitioner must demonstrate: (1) that his counsel's performance fell below an objective standard of reasonableness under prevailing professional norms; and (2) that counsel's deficient performance prejudiced the defense.

Constitutional Law > ... > Fundamental Rights > Criminal Process > Assistance of Counsel

Criminal Law & Procedure > Counsel > Effective Assistance of Counsel > Tests for Ineffective Assistance of Counsel

## **HN5** [down] **Criminal Process, Assistance of Counsel**

With regard to the two part test for determining ineffective assistance of counsel, in evaluating the first prong of this test, the court must indulge in a strong presumption that counsel's conduct falls within the wide range of reasonable professional assistance, bearing in mind that there are countless ways to provide effective assistance in any given case and that even the best criminal defense attorneys would not defend a particular client in the same way. As for the second prong, to show prejudice, a defendant must demonstrate that there is a reasonable probability that, but for counsel's unprofessional performance, the outcome of the proceeding would have been different. A reasonable

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probability is a probability sufficient to undermine confidence in the outcome. The court's central concern is not with "grading counsel's performance" but with discerning whether despite the strong presumption of reliability, the result of the particular proceeding is unreliable because of a breakdown in the adversarial process that our system counts on to produce just results.

Constitutional Law > ... > Fundamental Rights > Criminal Process > Assistance of Counsel

Criminal Law & Procedure > Counsel > Effective Assistance of Counsel > Tests for Ineffective Assistance of Counsel

#### **HN6** [+] **Criminal Process, Assistance of Counsel**

Because it is all too tempting for a defendant to second-guess counsel's assistance after conviction, the United States Court of Appeals for the Second Circuit has instructed that a reviewing court should be "highly deferential" in assessing counsel's performance. Although the test for ineffective assistance of counsel contains two prongs, the United States Supreme Court specifically noted that federal district courts need not address both components if a petitioner fails to establish either one. In particular, a court need not determine whether counsel's performance was deficient before examining the prejudice suffered by the defendant as a result of the alleged deficiencies.

Constitutional Law > ... > Fundamental Rights > Criminal Process > Assistance of Counsel

Criminal Law & Procedure > ... > Defendant's Rights > Right to Counsel > Effective Assistance of Counsel

Criminal Law & Procedure > Counsel > Effective Assistance of Counsel > Tests for Ineffective Assistance of Counsel

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Criminal Law & Procedure > ... > Defendant's Rights > Right to Counsel > General Overview

#### **HN7** [+] **Criminal Process, Assistance of Counsel**

It is well-established that a defendant's *Sixth Amendment* right to effective assistance of counsel includes the right to representation by conflict-free counsel. In addition, prejudice will be presumed when a defendant shows (1) an actual conflict of interest that, (2) adversely affected his counsel's performance.

Antitrust & Trade Law > Clayton Act > Penalties

Criminal Law & Procedure > Criminal Offenses > Miscellaneous Offenses > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > General Overview

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > Sherman Act

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > General Overview

371 F. Supp. 2d 265, \*265L<sup>2005 U.S. Dist. LEXIS 10479, \*\*1</sup>

## [\*\*HN8\*\*](#) [blue download icon] Clayton Act, Penalties

A relevant market and an antitrust injury are not required elements to prove a criminal violation of [§ 1](#) of the Sherman Act, [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > Sherman Act > Claims

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > General Overview

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > Sherman Act

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > General Overview

Criminal Law & Procedure > Trials > Burdens of Proof > Prosecution

## [\*\*HN9\*\*](#) [blue download icon] Sherman Act, Claims

[Section 1](#) of the Sherman Act by its terms makes unlawful: every contract combination, or conspiracy, in restraint of trade. [15 U.S.C.S. § 1](#). To prove a criminal violation of this section, the government must establish: (1) an agreement to a joint action such as a conspiracy formed by two or more entities; (2) that the defendant knowingly joined this conspiracy; (3) the agreement unreasonably restrained trade or commerce; and (4) that the conspiracy concerned goods or services in interstate commerce.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > Per Se Violations

## [\*\*HN10\*\*](#) [blue download icon] Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

With regard to the Sherman Act, certain activities including bid-rigging are so anticompetitive that they constitute "per se" violations of the [antitrust law](#). Where two or more persons agree that one will submit a bid for a project higher or lower than the others or that one will not submit a bid at all, then there has been an unreasonable restraint of trade which violates the Sherman Antitrust Act.

Antitrust & Trade Law > Sherman Act > General Overview

Criminal Law & Procedure > Trials > Burdens of Proof > Prosecution

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## **HN11** [ ] Antitrust & Trade Law, Sherman Act

With regard to the Sherman Act, "per se" bid rigging activity is presumed to be an unreasonable restraint on trade and therefore illegal because of its pernicious effect on competition and lack of any redeeming virtue. In this type of case, the government must only prove the existence of an agreement to partake in the "per se" illegal activity, and that the activity in question concerns goods or services in interstate commerce. The commerce requirement of the Sherman Act may be satisfied: (1) where the defendant's conduct directly interferes with the flow of goods in the stream of commerce (the "in commerce" test); or (2) where the defendant's conduct has a substantial effect on interstate commerce (the "effect on commerce" test).

**Counsel:** EDWARD SHAW, Petitioner, Pro se, Brooklyn, New York.

UNITED STATES DEPARTMENT OF JUSTICE, ANTITRUST DIVISION, New York, New York, By: Debra Brookes, Attorney, John W. McReynolds, Attorney.

ROSLYNN R. MAUSKOPF, UNITED STATES ATTORNEY, EASTERN DISTRICT OF NEW YORK, Central Islip, New York, By: AUSA Tanya Y. Hill.

**Judges:** ARTHUR D. SPATT, United States District Judge.

**Opinion by:** ARTHUR D. SPATT

## **Opinion**

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### **[\*267] MEMORANDUM OF DECISION AND ORDER**

This case involves charges that the petitioner Edward Shaw ("Shaw" or the "Petitioner") took part in a bid-rigging conspiracy in violation of the Sherman Antitrust Act, [15 U.S.C. § 1](#) (the "Sherman Act"). On April 30, 2002, pursuant to a Cooperation Agreement (the "Agreement"), the Petitioner pleaded guilty to a one-count information [\[\\*2\]](#) charging him with conspiring to rig bids in violation of the [Sherman Act](#).

Presently before the Court is a motion by the petitioner to set aside or vacate the judgment of conviction pursuant to [28 U.S.C. § 2255](#) ("[Section 2255](#)") on the ground of ineffective assistance of counsel. For the reasons stated below, Shaw's petition is without merit and is denied.

### **I. BACKGROUND**

On October 18, 2002, the Court accepted Shaw's plea of guilty to the one count information that was previously taken by United States Magistrate Judge Arlene R. Lindsay. He was also sentenced to three years probation, with special conditions that he serve four months home detention and undergo gambling therapy. According to the Government, on November 5, 2002, Shaw filed a notice of appeal. This appeal was withdrawn in May 2003.

In the instant petition, Shaw claims that he received ineffective assistance of counsel in violation of the [Sixth Amendment](#) because: (1) his attorney Frederick Schurr, Esq. ("Schurr"), disclosed confidential communications to the Government that was allegedly used against him; and (2) Schurr recommended that he plead guilty despite the absence of evidence of a [\[\\*3\]](#) "relevant market" and an "antitrust injury."

A. The Nature of the Conspiracy

In or about January 2001, the Government uncovered a five-year long bid-rigging conspiracy involving Shaw and a number of other co-conspirators affecting public auctions conducted by the Nassau and Suffolk County Sheriffs' Offices. This scheme involved an agreement that the individuals would not bid against each other [\*268] during the official auction. Rather, the group set a pre-determined price at which one designated individual was to bid on the auctioned property on the group's behalf instead of each member of the group bidding competitively against each other. In cases where at least three bids were required, two other conspirators would first submit intentionally low bids, thus enabling the designated bidder to win the property with a subsequent bid. Because the final bid was less than that which would have resulted had there been legitimate competitive bidding, this scheme prevented the respective creditors from receiving the maximum value of the auctioned properties.

The Government's investigation revealed that if the designated bidder won the particular item during the official auction, the co-conspirators [\*\*4] would then hold a second, private "knock-out" auction. During the knock-out auction, the group would bid against one another to determine who would ultimately own the property. When a co-conspirator reached his dollar limit for a particular item, he stopped bidding and was "knocked out" of the private auction. The "knocked out" individual would receive a payoff from the winner of the knock-out auction that was based on his last bid before being knocked-out. After reimbursing the designated bidder in the official action, and compensating the other conspirators, the winner of the knock-out auction would take the item. The price that the winner of the item ultimately paid for the item was less than what would have been paid had there been legitimate competitive bidding at the official auction.

The Government's investigation further revealed that, when a third-party interested in bidding on an item appeared at the official auction, one of the co-conspirators, usually Shaw, would demand a cash payment from the third party in exchange for an agreement that the group would not bid against that outside party. To induce the third party to agree, Shaw would threaten to intentionally bid up [\*\*5] the price of the property so that the third-party would pay more for the property. The cash payment by the third party was then divided among the group members.

According to Shaw's petition, in January 2001, a special agent of the FBI came to his home and accused him of violating the Sherman Anti-Trust Act. The special agent advised Shaw to contact him after he retained a lawyer. Shaw subsequently contacted Norman Langer, Esq. ("Langer"). Langer had often hired Shaw to attend auctions in order to bid on property belonging to Langer's clients that was being sold at auction to collect on judgments against them.

The Government has attached as an exhibit to their opposition papers a letter dated July 31, 2003 from Schurr to John W. McReynolds, Attorney, Department of Justice, Antitrust Division. In this letter, Schurr explains that on January 26, 2001, he contacted the Special Agent and set January 29, 2001 as the date for a full disclosure by the Government of all the evidence against Shaw. At the January 29, 2001 meeting with McReynolds and Debra C. Brookes, Attorney, Department of Justice Antitrust Division, Schurr heard audio taped recordings made by a government undercover agent [\*\*6] which revealed that Shaw told the undercover agent that he and his co-conspirators would not bid the price up in exchange for \$ 300.00. Schurr also learned that the Government intended to seek indictment against Shaw and his co-conspirators for "mail fraud, tax evasion, fixing auctions, conspiracy, and violation of the Sherman Antitrust Act." Also at this meeting, the Government suggested the possibility of Shaw cooperating with the government in exchange for a 5K1.1 [\*269] cooperation letter to reduce his exposure to incarceration.

After several meetings with Schurr, Shaw decided to cooperate with the Government. On February 20, 2001, Shaw and Schurr met with McReynolds, Brookes, Assistant United States Attorney ("AUSA") Tanya Hill, as well as two FBI Special Agents at which Shaw narrated in complete detail the nature of the Conspiracy with the hope of obtaining a 5K1.1 letter.

## B. The Plea and Sentencing Proceeding

On April 30, 2002, Shaw pleaded guilty before Magistrate Judge Lindsay to a one count information charging him with conspiring to rig bids in violation of 15 U.S.C. § 1. Schurr represented Shaw at the plea allocution. At this court

proceeding, [\*\*7] the Petitioner stated that he reviewed the Agreement with his attorney and understood the terms and conditions of the Agreement. Shaw also stated that he understood the charge against him. Shaw also explained in detail how he and the other co-conspirators agreed to manipulate the public auctions in the manner described above. Shaw also stated that he knew that he was bidding on property that came across state lines and that by entering this agreement he was "influencing the bidding process." Of importance in the determination of this motion, is the Petitioner's statement that as of that time, he was satisfied with his legal representation.

On October 18, 2002, this Court accepted the Petitioner's guilty plea and sentenced Shaw to three years' probation, with special conditions that he serve four months home detention and undergo gambling therapy.

## II. DISCUSSION

Shaw contends that the judgement of conviction entered against him as a result of his plea of guilty was the result of ineffective assistance of counsel in violation of his *Sixth Amendment* rights because: (1) his attorney Frederick Schurr, Esq., disclosed confidential communications to the prosecution which was used [\*\*8] against him; and (2) Schurr erred in failing to properly research the facts of this case so as to ascertain that he was not guilty of the crime charged because the Government lacked proof that there was a "relevant market" causing an "antitrust injury."

### A. Standard of Review

**HN1**[] Pursuant to [section 2255](#), a federal prisoner in custody "may move the court which imposed the sentence to vacate, set aside or correct the sentence" on the basis that it "was imposed in violation of the Constitution or laws of the United States, or that the court was without jurisdiction to impose such sentence, or that the sentence was in excess of the maximum authorized by law, or is otherwise subject to collateral attack . . ." [28 U.S.C. § 2255](#). The burden of proof is on petitioner to establish his constitutional claims by a preponderance of the evidence. See [Triana v. United States, 205 F.3d 36, 40 \(2d Cir.\)](#), cert. denied, 531 U.S. 956, 148 L. Ed. 2d 292, 121 S. Ct. 378 (2000); see also [Whitaker v. Meachum, 123 F.3d 714, 716 \(2d Cir. 1997\)](#).

**HN2**[] Although generally a petitioner who has failed to raise an issue on direct appeal may not do so in a [§ 2255](#) petition, [\*\*9] see [Underwood v. U.S., 166 F.3d 84, 87 \(2d Cir. 1999\)](#), claims of ineffective assistance of counsel may be brought for the first time in a [section 2255](#) petition. [Frederick v. Warden, Lewisburg Correctional Facility, 308 F.3d 192, 197 n. 6 \(2d Cir. 2002\)](#). Such is the case because such claims "would not likely be made on direct appeal [\*270] by an attorney who had represented the petitioner at trial based upon that attorney's own incompetence." [Riascos-Prado v. United States, 66 F.3d 30, 34-35 \(2d Cir. 1995\)](#). In addition, "the district court [is] the forum best suited to developing the facts necessary to determining the adequacy of representation . . ." [United States v. Doe, 365 F.3d 150, 153 \(2d Cir. 2004\)](#) (quoting [Massaro v. United States, 538 U.S. 500, 504-05, 123 S. Ct. 1690, 155 L. Ed. 2d 714 \(2003\)](#)).

Finally, the Court is mindful that **HN3**[] the petitioner is proceeding *pro se* and that his submissions must be liberally construed in favor of the petitioner. See [Chang v. U.S., 250 F.3d 79, 86 n. 2 \(2d Cir. 2001\)](#).

### B. Ineffective Assistance of Counsel

**HN4**[] To establish ineffective [\*\*10] assistance of counsel, a petitioner must demonstrate: (1) that his counsel's performance fell below an objective standard of reasonableness under prevailing professional norms; and (2) that counsel's deficient performance prejudiced the defense. [Strickland v. Washington, 466 U.S. 668, 687-688, 104 S. Ct. 2052, 2064, 80 L. Ed.2d 674 \(1984\)](#); see also [Larrea v. Bennett, 368 F.3d 179, 183 \(2d Cir. 2004\)](#).

**HN5** In evaluating the first prong of this test, the Court must "indulge in a strong presumption that counsel's conduct falls within the wide range of reasonable professional assistance,' bearing in mind that 'there are countless ways to provide effective assistance in any given case' and that 'even the best criminal defense attorneys would not defend a particular client in the same way.'" *United States v. Aguirre*, 912 F.2d 555, 560 (2d Cir. 1990) (quoting *Strickland*, 466 U.S. at 689) (alterations in original); see also *Larrea*, 368 F.3d at 183. As for the second prong, to show prejudice, a defendant must demonstrate "that there is a reasonable probability that, but for counsel's unprofessional performance, [\*\*11] the outcome of the proceeding would have been different." *United States v. Levy*, 377 F.3d 259, 264 (2d Cir. 2004) (quoting *United States v. Gordon*, 156 F.3d 376, 379 (2d Cir. 1998)). "A reasonable probability is a probability sufficient to undermine confidence in the outcome." *Id.* (quoting *Strickland*, 466 U.S. at 694). "The court's central concern is not with 'grading counsel's performance' but with discerning 'whether despite the strong presumption of reliability, the result of the particular proceeding is unreliable because of a breakdown in the adversarial process that our system counts on to produce just results.'" *Aguirre*, 912 F.2d at 560 (2d Cir. 1990) (quoting *Strickland*, 466 U.S. at 696-97).

**HN6** Because "it is all too tempting for a defendant to second-guess counsel's assistance after conviction," *Strickland*, 466 U.S. at 689, the Second Circuit has instructed that a reviewing court should be "highly deferential" in assessing counsel's performance. See *Pratt v. Greiner*, 306 F.3d 1190, 1196 (2d Cir. 2002) (quoting *Strickland*, 466 U.S. at 689, 104 S. Ct. 2052). [\*\*12] Although the test for ineffective assistance of counsel contains two prongs, the Supreme Court specifically noted that federal district courts need not address both components if a petitioner fails to establish either one. *Strickland*, 466 U.S. at 697. In particular, "a court need not determine whether counsel's performance was deficient before examining the prejudice suffered by the defendant as a result of the alleged deficiencies." *Id.*

### 1. As to the claim that Frederick Schurr, Esq., disclosed confidential communications.

In his petition, Shaw explains that he is "morally certain that [Schurr] proceeded [\*271] to the Government, to share the information that [Shaw] told him, in order for the Government to make a colorable case against me, for him to try to justify the fifty thousand dollar fee." However, the Petition is lacking any specific details as to the content of the alleged disclosure; or the date, time, place, and to whom such disclosures were made. Nor does Shaw identify any facts or details that the Government had learned that was based on privileged information rather than information that the Government had obtained independently.

These conclusory [\*\*13] allegations are insufficient for the Court to conclude that Schurr disclosed any confidential communications to the Government. Nor can the Court conclude that Schurr's performance did not meet the objective standard of reasonableness under prevailing professional norms. Even assuming the alleged disclosures were made by Schurr, the Petitioner fails to satisfy his burden as to the second prong of the *Strickland* test, namely that the outcome of the proceeding would have been different, but for Schurr's performance

Reading Shaw's petition liberally as the court is required to do with all *pro se* petitions, Shaw may also be asserting an ineffective assistance of counsel claim based on an alleged conflict of interest. Shaw's petition is riddled with allegations that Schurr had a conflict of interest because "Schurr's purpose was to make certain that [Shaw] not mention . . . Langer's name" and that "Schurr's motive was to literally steal fifty thousand dollars from [him] under the guise of a legal fee."

**HN7** It is well-established that "[a] defendant's *Sixth Amendment* right to effective assistance of counsel includes the right to representation by conflict-free counsel." *United States v. Schwarz*, 283 F.3d 76, 90 (2d Cir. 2002). [\*\*14] In addition, prejudice will be presumed when a defendant shows "(1) an actual conflict of interest that (2) adversely affected his counsel's performance," *Id.* However, once again, Shaw's petition is lacking any details as to this alleged conflict; how the presumed conflict caused an "actual lapse in representation," *Locascio v. United States*, 395 F.3d 51, 56 (2d Cir. 2005) (internal quotation and citation omitted); and how the outcome of this case would have been any different. See *Cuyler v. Sullivan*, 446 U.S. 335, 348-50, 64 L. Ed. 2d 333, 100 S. Ct. 1708 (1980); *Eisemann v. Herbert*, 401 F.3d 102, 2005 U.S.App. LEXIS 4134, \*9-10 (2d Cir. 2005). Finally, with regard to Shaw's assertions that Schurr's legal fee in the amount of \$ 50,000 was excessive, the Court notes that a *Section*

2255 petition is not the proper forum for a fee dispute. Furthermore, the petition indicates that Shaw has filed a grievance with the Nassau County Bar Association with regard to these assertions against Schurr.

Accordingly, Shaw failed to demonstrate that Schurr had a conflict of interest that prejudiced the legal representation that he received, and this argument must similarly fail.

**2. As to [\*\*15] the claim that Schurr erred in recommending that he plead guilty despite the absence of evidence with regard to a "relevant market" or proof of an "antitrust injury."**

Shaw next argues that Schurr's representation violated the Sixth Amendment because he failed to properly research the elements of a criminal antitrust violation, and therefore erred in advising him to plead guilty. In particular, Shaw contends that Schurr failed to advise him that the Government would not have been able to establish that there was a "relevant [\*272] market" or an "antitrust injury." However, as set forth below, HN8[ a relevant market and an antitrust injury are not required elements to prove a criminal violation of Section 1 of the Sherman Act.

HN9[ Section 1 by its terms makes unlawful: "every contract combination . . ., or conspiracy, in restraint of trade . . ." 15 U.S.C. § 1. To prove a criminal violation of this section, the Government must establish: (1) an agreement to a joint action such as a conspiracy formed by two or more entities; (2) that the defendant knowingly joined this conspiracy; (3) the agreement unreasonably restrained trade or commerce; and (4) that the conspiracy concerned [\*16] goods or services in interstate commerce. See 3 L. Sands et al., Modern Federal Jury Instructions P58.04, Instr. 58 - 44 (2003); See United States v. Koppers Co., 652 F.2d 290, 295-96 (2d Cir. 1981), cert. denied, 454 U.S. 1083, 70 L. Ed. 2d 617, 102 S. Ct. 639 (1982); United States v. Gypsum Co., 438 U.S. 422, 435-43, 98 S. Ct. 2864, 57 L. Ed.2d 854 (1978); UCAR Intern., Inc. v. Union Carbide Corp., 2004 U.S. Dist. LEXIS 914, 2004 WL 137073, at \*16 (S.D.N.Y. Jan. 26, 2004).

Shaw also contends that there can be no antitrust crime because there was no evidence that he or his co-conspirators paid anything less than fair value for any of the property. Not so. If the co-conspirators had legitimately bid against each other during the "official auction," the sale price would presumably have been higher. Thus, Shaw's activities artificially and unlawfully reduced the price that the relevant items sold at auction. For that reason, HN10[ certain activities including bid-rigging are so anticompetitive that they constitute "per se" violations of the antitrust law. See Koppers Co., 652 F.2d at 294; see also United States v. W.F. Brinkley & Son Constr. Co., Inc., 783 F.2d 1157, 1161 (4th Cir. 1986) [\*\*17] ("Where two or more persons agree that one will submit a bid for a project higher or lower than the others or that one will not submit a bid at all, then there has been an unreasonable restraint of trade which violates the Sherman Antitrust Act."); Philip Morris Inc. v. Heinrich, 1996 U.S. Dist. LEXIS 9156, No. 95 Civ. 0328, 1996 WL 363156, at \*9 (June 28, 1996) ("Courts have specifically classified bid-rigging as a form of price fixing that constitutes a per se violation." (citing authorities)).

Such HN11[ "per se" bid rigging activity is presumed to be an unreasonable restraint on trade and therefore illegal because of its "pernicious effect on competition and lack of any redeeming virtue." Northern Pacific Railway Co. v. United States, 356 U.S. 1, 78 S. Ct. 514, 2 L. Ed. 2d 545 (1958). In this type of case, the Government must only prove the existence of an agreement to partake in the "per se" illegal activity, see Koppers Co., 652 F.2d at 296 n. 6, and that the activity in question concerns goods or services in interstate commerce. Hamilton Chapter of Alpha Delta Phi, Inc. v. Hamilton College, 128 F.3d 59, 66-67 (2d Cir. 1997) (Stating that the [\*18] commerce requirement of the Act may be satisfied: (1) "where the defendant's conduct directly interferes with the flow of goods in the stream of commerce (the 'in commerce' test); or (2) where the defendant's conduct has a substantial effect on interstate commerce (the 'effect on commerce' test) (citations omitted)). Therefore, Shaw's contention that Schurr erred by not properly advising him as to the elements of a criminal antitrust case is without merit.

The Court similarly finds Shaw's remaining arguments to be without merit. Accordingly, Shaw has failed to demonstrate ineffective assistance of counsel and his petition is denied in its entirety.

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Based on the foregoing, it is hereby

**ORDERED**, that the Petitioner's motion to set aside or vacate the judgment of conviction pursuant to [28 U.S.C. § 2255](#) is denied; and it is further

**ORDERED**, that pursuant to *Rule 22(b) of the Federal Rules of Appellate Procedure* and [28 U.S.C. § 2253\(c\)\(2\)](#), a certificate of appealability is **DENIED**, as the Petitioner fails to make a substantial showing of a denial of a constitutional [\\*\\*19](#) right. [Miller-El v. Cockrell, 537 U.S. 322, 336, 123 S. Ct. 1029, 1039, 154 L. Ed.2d 931 \(2003\); Lucidore v. New York State Div. of Parole, 209 F.3d 107, 112 \(2d Cir. 2000\)](#); and it is further

**ORDERED**, that the Clerk is directed to close this case.

**SO ORDERED.**

Dated: Central Islip, New York

May 31, 2005

ARTHUR D. SPATT

United States District Judge

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## Investors Corp. v. Bayer AG

Superior Court of Vermont, Chittenden County

June 1, 2005, Decided

No. 1011-04 Cncv

**Reporter**

2005 Vt. Super. LEXIS 92 \*

INVESTORS CORPORATION OF VERMONT v. BAYER AG, ET AL.

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**Subsequent History:** Motion granted by [\*Investors Corp. v. Bayer, 2005 Vt. Super. LEXIS 34 \(Vt. Super. Ct., Aug. 3, 2005\)\*](#)

**Prior History:** [\*In re Polychloroprene Rubber Antitrust Litig., 360 F. Supp. 2d 1348, 2005 U.S. Dist. LEXIS 1944 \(J.P.M.L., 2005\)\*](#)

## Core Terms

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purchasers, antitrust, damages, indirect, consumer, duplicate, putative class, consumer fraud, courts, suits, federal action, cases, unjust enrichment, consolidation, speculative, products, antitrust violation, finished product, anti trust law, necessary step, causation, prices, rubber, chain, steps

**Judges:** [\*1] Richard W. Norton, Judge.

**Opinion by:** NORTON

## Opinion

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### ENTRY

This matter concerns allegations of unfair trade practices. The plaintiff, Investors Corporation of Vermont, has sued the defendants for allegedly restraining trade of Ethylene Propylene Diene Monomer (EPDM), a component of Ethylene-propylene elastomers, which are the third-most common forms of synthetic rubber in the world. Investors Corporation seeks to form a class of all Vermont persons or business entities that indirectly purchased EPDM from the defendants from January 1994 through December 2002. Investors Corporation claims violations of [9 V.S.A. §§ 2453, 2465](#) (Vermont antitrust law) and [9 V.S.A. §§ 2453, 2461](#) (Vermont consumer fraud law), as well as unjust enrichment.

The defendants move to dismiss pursuant to V.R.C.P. 12(b)(6) for failure to state a claim upon which relief can be granted. The defendants argue that damages are too speculative given that the putative class of plaintiffs are mere indirect purchasers of downstream products, of which EPDM formed only a component part. In essence, the defendants' argument is that the putative class lacks standing under the Vermont antitrust and consumer fraud law.

In the alternative, the [\*2] defendants request that this court stay this action pending resolution of a federal action by direct purchasers of EPDM. This federal action has been consolidated in the U.S. District Court for the District of Connecticut. See *In re Ethylene Propylene Diene Monomer (EPDM) Antitrust Litig.*, 277 F. Supp. 2d 1373, 1373 (2003). The defendants argue that such a stay is warranted given the Vermont statute's directive that courts "take all necessary steps to avoid duplicate liability, including but not limited to the transfer or consolidation of all related actions." 9 V.S.A. § 2465(b).

A Rule 12(b)(6) motion "should not be granted unless it is beyond doubt 'that there exist no facts or circumstances that would entitle the plaintiff to relief.'" *Richards v. Town of Norwich*, 169 Vt. 44, 48, 726 A.2d 81 (quoting *Amiot v. Ames*, 166 Vt. 288, 291, 693 A.2d 675 (1997)). The court "assumes that all factual allegations pleaded in the complaint are true . . . accept[ing] as true all reasonable inferences that may be derived from plaintiff's pleadings." *Id. at 49*. "A court should be 'especially reluctant to dismiss' a cause of action on the basis of the pleadings when the theory of liability is novel or extreme unless, 'beyond [\*3] doubt, there [are] no circumstances or facts which plaintiff[] could prove which would entitle [her] to relief.'" *In re Judicial Review of A.G.*, 151 Vt. 167, 169, 559 A.2d 656 (1989) (quoting *Assoc. of Haystack Property Owners, Inc. v. Sprague*, 145 Vt. 443, 446-47, 494 A.2d 122 (1985)) (second and third alterations in original).

The Vermont Consumer Fraud Act provides broad remedies for consumers injured by unfair trade practices and antitrust violations. "The Act expressly states that any consumer, reinforced by the definition of consumer as 'any person,' who suffers injury may bring an action under the statute against a 'seller, solicitor or other violator.'" *Elkins v. Microsoft Corp.*, 174 Vt. 328, 331, 817 A.2d 9 (2002) (quoting 9 V.S.A. §§ 2453(a), 2461(b)). Moreover, "the express legislative intent behind the statute [is] to 'protect the public' against 'unfair or deceptive acts or practices' and to 'encourage fair and honest competition.'" *Id.* (quoting 9 V.S.A. § 2451). "In light of this purpose, . . . the VCFA is 'remedial in nature' and therefore must be construed 'liberally so as to furnish all the remedy and all the purposes intended.'" *Id.* (quoting *State v. Custom Pools*, 150 Vt. 533, 536, 556 A.2d 72 (1988)). "Of course, liberal [\*4] construction does not allow [courts] to stretch the language beyond legislative intent." *Id.*

In a recent ruling, this court held that a putative class of consumers did not have antitrust standing to sue Visa and Mastercard for alleged injuries they incurred by purchasing items from merchants who used financial services from these institutions. See *Fucile v. Visa U.S.A., Inc., No. S5160-03 CnC*, 2004 Vt. Super. LEXIS 42, [WL] (Dec. 27, 2004) (Norton, J.). Visa and Mastercard had settled a multidistrict class action from merchants who alleged that the defendants had tied debit card services with credit card services in violation of federal **antitrust law**. See *id.* 2004 Vt. Super. LEXIS 42, at \*2, [WL] at \*1 (citing *In re Visa Check/Mastermoney Antitrust Litig.*, 297 F. Supp. 2d 503 (E.D.N.Y. 2003)). The plaintiff, Fucile, argued that the inflated costs of these financial services were passed along to consumers by merchants who used them. In dismissing this complaint, this court adopted the antitrust standing principles articulated in *Associated General Contractors v. Calif. State Council of Carpenters*, 459 U.S. 519, 103 S. Ct. 897, 74 L. Ed. 2d 723 (1983), at least to the extent that these principles were consistent with Vermont law, which, unlike federal law, allows indirect [\*5] purchaser suits. Applying the *Associated General Contractors* factors, this court held that Fucile's injury was too attenuated and remote from the alleged antitrust violation and his damages were too speculative. *Fucile*, 2004 Vt. Super. LEXIS 42, at \*10, [WL] at \*4-5. Fucile therefore lacked antitrust standing.

Here, Investors Corporation stands in a different posture than Fucile. Unlike Fucile, Investors Corporation and the putative class purchased the item allegedly affected by the defendant's actions (i.e., EPDM), albeit in varied forms as a component of Ethylene-propylene elastomers. According to the complaint, EPDM comprises 80 to 85 percent of Ethylene-propylene elastomers. Financial services, by contrast, are not components of common consumer goods, except, perhaps, in an extraordinarily abstract sense. Given that EPDM is a significant component of the product that putative class members purchased, the injury in this case is not as attenuated and remote and the damages are not as speculative.

As this court stated in *Fucile*, the relevant factors from *Associated General Contractors* are (1) whether there is a causal connection between the antitrust violation and the alleged harm, 459 U.S. at 537; (2) the directness of the [\*6] injury, considering the "chain of causation," *id. at 540*; (3) whether the violator had an improper motive, *id. at*

[537](#) and n.35; (4) whether the plaintiff's injury was of a type that Congress sought to redress by providing a private remedy, [id. at 538](#); (5) whether the alleged damages are speculative, [id. at 542](#); and (6) whether the nature of the action will keep "the scope of complex antitrust trials within judicially manageable limits," [id. at 543](#).

Applying these factors to the instant case, there first exists a causal connection between the defendants' alleged price fixing and the putative class's injury. Because EPDM is a significant component part of the finished rubber products at issue, an increase in its price could have a ripple affect in the finished products, thereby increasing prices for the ultimate consumers.

The defendants argue that there are countless other inputs that determine the ultimate price of Ethylene-propylene elastomers, such as different marketing by third-party sellers, different forms of distribution, and different types of manufacturing. These multiple variables, the defendants argue, render injury and damages impossibly speculative, and therefore the causal [\[\\*7\]](#) chain cannot be established. This may or may not be true, and other courts have expressed strong concerns about stretching [antitrust law](#) to cover damages in cases like these. See, e.g., [Crouch v. Crompton Corp., Nos. 02 CVS 4375, 03 CVS 2514, 2004 WL 2414027, \\*18-25, 2004 NCBC 7, PP 71-86 \(N.C. Super. Ct. 2004\)](#) (analyzing complexity and costliness of adjudicating antitrust case based on rubber compounds and chemicals that form component of tire products at issue).<sup>1</sup> Indeed, the court in *Crouch* noted, citing a plea agreement from Canada, that at least in the case of tires, rubber compounds and chemicals form a mere 1 percent of the ultimate price of the finished product. [Id. \[WL\] at \\*20-21, 2004 NCBC 7, P 76](#) (citing *The Queen v. Crompton Corp.* [2004] F.C. --).

Such facts, however, are far afield Rule 12(b)(6) motion analysis. The court will be better suited to assess whether Investors Corporation will be able to prove causation based on the alleged antitrust violation at the class certification and summary judgment stages. At this point in the proceeding, however, the court is not confident in holding that Investors Corporation lacks an ability to show causation. See [Knevelbaard Dairies v. Kraft Foods, Inc., 232 F.3d 979, 989 \(9th Cir. 2000\)](#) (holding that "disputed claims of causation and injury cannot be decided on a Rule 12(b)(6) motion"). Hence, factors one and two weigh in favor of standing.

Second, the court can infer an improper motive based on Investors Corporation's allegations. The alleged price-fixing was a conspiracy throughout U.S. and European markets, evidenced by coordinated price hikes close in time and amount. Investors Corporation alleges that defendants met during the class period; discussed prices, customers, and markets; agreed to charge prices at certain levels; issued price announcements in conformance with these agreements; and allocated markets and customers in accordance [\[\\*9\]](#) with these agreements. One defendant, Crompton Corporation, has pleaded guilty to violating antitrust laws, and others have been contacted by antitrust authorities. These facts are enough to infer that the defendants had an improper motive to injure consumers like Investors Corporation and those in the putative class by allegedly fixing prices at artificially high levels. See [Sullivan v. Tagliabue, 828 F. Supp. 114, 117 \(D. Mass. 1993\)](#) (finding sufficient evidence to raise issue as to improper motive where plaintiff alleged that defendant sought to restrain and monopolize commerce and took action toward that goal). The third factor therefore weighs in favor of standing for Investors Corporation.

Third, the injury that Investors Corporation and the putative class suffered appears to be within the type of injury that the Legislature intended to address through the Vermont antitrust and consumer fraud law. If Investors Corporation can demonstrate that the increased EPDM prices affected the price of the goods purchased, then it will have established the type of injury to indirect purchasers that the Legislature intended to remedy by allowing indirect purchaser suits. The fourth factor weighs [\[\\*10\]](#) in favor of standing for Investors Corporation.

Finally, as the court noted above, the damages may be somewhat speculative, and this weighs slightly against standing. But the court is not confident at this stage that Investors Corporation will not be able to employ economic

<sup>1</sup> Of course, the court's concerns in *Crouch* were partially based on the lack of express statutory indirect purchaser standing in North Carolina or any definitive ruling by the North Carolina Supreme Court on indirect purchaser standing. [Id. \[WL\] at \\* 10-12, 2004 NCBC 7, PP 46-50](#). This is not the case in Vermont. See [9 V.S.A. § 2465\(b\); Elkins, 174 Vt. at 337-38](#) (holding that [§ 2465\(b\)](#) was mere clarification and Vermont consumer fraud law [\[\\*8\]](#) has always allowed indirect purchaser suits).

models to assess how the price of EPDM affected the price of downstream products. As the U.S. Court of Appeals for the Ninth Circuit has recognized, "Complex antitrust cases . . . invariably involve complicated questions of causation and damages." *Forsyth v. Humana, Inc.*, 114 F.3d 1467, 1478 (9th Cir. 1997). This case will likely prove to be no exception, but that is not reason enough to dismiss for lack of standing.

Considering this analysis, the court holds that Investors Corporation has standing to bring this antitrust and consumer fraud action. At the same time, however, the court does not wish to enunciate a bright-line rule regarding antitrust standing. As the Supreme Court of the United States noted in *Associated General Contractors*, standing determinations must ultimately rest on case-by-case analyses. *459 U.S. at 536-37 (1983)*. The court does not wish to suggest that in all cases where a product affected [\*11] by anti-competitive behavior is a component of a finished product, antitrust standing exists for the consumer of the finished product. There may well be cases where products form such an minuscule portion of the finished product that antitrust standing is lacking. Indeed, in an abstract and theoretical way, the financial services in *Fucile* were part of the consumer goods at issue in that these goods could not have ultimately fallen into the hands of all paying consumers without the transactional means that were affected by price fixing. But even if the court were to consider such transactional means to be a part of the consumer goods as EPDM is to finished rubber products, they form an entirely less significant portion of the consumer goods. Transactional means of acquiring goods, therefore, cannot provide grounds for standing to sue the entities that provided them.

The defendants also argue that Investors Corporation lacks standing to bring an unjust enrichment claim because Investors Corporation and members of the putative class did not directly confer any benefit to the defendants. Vermont law does not require that the enrichment be directly conferred from one party to another in [\*12] order for the latter party to have a colorable claim for unjust enrichment. "Under a quasi-contract theory of unjust enrichment, the law implies a promise to pay when a party receives a benefit and retention of the benefit would be inequitable." *Brookside Memorials, Inc. v. Barre City*, 167 Vt. 558, 559, 702 A.2d 47 (1997) (mem.).

As with the antitrust and consumer fraud claims, the link between purchases by Investors Corporation and the putative class and benefits to the defendants may be tenuous, but it is still properly alleged in the complaint. Moreover, because of the alleged antitrust and consumer fraud activities, it would be inequitable for the defendants to retain these benefits. Investors Corporation has therefore stated a valid unjust enrichment claim. The fact that Investors Corporation and the putative class did not deal directly with the defendants is not relevant, as long as the elements for unjust enrichment are pleaded. See *In re K-Dur Antitrust Litig.*, 338 F. Supp. 2d 517, 544-45 (D.N.J. 2004); *In re Cardizem CD Antitrust Litig.*, 105 F. Supp. 2d 618, 670-71 (E.D. Mich. 2000).

Finally, the defendants argue in the alternative that the court should stay this action pending resolution [\*13] of the federal direct purchaser action, contending that the Vermont Consumer Fraud Act's instruction that courts "take all necessary steps to avoid duplicate liability" suggests that a stay is appropriate. **Antitrust law** in the United States has an inherent problem of duplicate liability. Federal courts do not allow antitrust defendants to use a pass-on defense to show that the damages from anticompetitive behavior were ultimately absorbed by downstream purchasers. See *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 724-26, 97 S. Ct. 2061, 52 L. Ed. 2d 707 (1977). At the same time (and as a result of the no pass-on defense rule), federal courts also do not allow antitrust suits by indirect purchasers. See *id. at 730-35*. Therefore, defendants in federal court are liable for all damages, even if a plaintiff was able to relay the costs of anticompetitive activities to downstream consumers. Most states, including Vermont, however, have passed "*Illinois Brick Repealer*" laws, allowing indirect purchasers to recover for injuries related to antitrust violations. Donald I. Baker, *Federalism and Futility: Hitting the Potholes on the Illinois Brick Road*, 17-Fall Antitrust 14, 14 (2002). Because most state indirect purchaser antitrust [\*14] actions stem from federal direct purchaser actions, see Ronald W. Davis, *Indirect Purchaser Litigation: ARC America's Chickens Come Home to Roost on the Illinois Brick Wall*, 65 Antitrust L.J. 375, 376 (1997), damages will inevitably be assessed twice against an antitrust defendant: once by the direct purchasers for all damages, even those passed along down the distribution chain, and then again by the indirect purchasers for whatever damages were actually passed along the distribution chain. *Id.* at 397-98; Baker, *supra*, at 16-17; see also *Crouch v. Crompton Corp., Nos. 02 CVS 4375, 03 CVS 2514, 2004 WL 2414027, \*15-17, 2004 NCBC 7, PP 19160-65 (N.C. Super. Ct. 2004)* (discussing North Carolina cases triggered by events on federal level).

At first glance, the provision cited by the defendants would seem to combat this double recovery problem. But the very allowance of indirect purchaser antitrust suits gives rise to duplicate liability in the sense described above. Even if the court were to stay this action and await final resolution of the federal action, Investors Corporation and the putative class would still have a right to recover for injuries passed along to them from the direct [\*15] purchasers under Vermont's statutory scheme.

A more reasonable interpretation of the "all necessary steps" provision is that the legislature intended consolidation of cases within Vermont to avoid overlapping damages to various classes. Indeed, the "steps" that the legislature identified included "transfer or consolidation of all related actions." [9 V.S.A. § 2465\(b\)](#). Such steps would not address the duplicate liability that occurs with both federal direct purchaser and state indirect purchaser suits.

The court also notes that it could find no other state *Illinois Brick* repealer laws requiring stays in a case such as the instant action. Several state statutes include similar language, see, e.g., [740 Ill. Comp. Stat. 10/7-2](#) ("[I]n any case in which claims are asserted against a defendant by both direct and indirect purchasers, the court shall take all steps necessary to avoid duplicate liability for the same injury including transfer and consolidation of all actions."); [Minn. Stat. § 325D.57](#) ("In any subsequent action arising from the same conduct, the court may take any steps necessary to avoid duplicative recovery against a defendant"); [N.Y. Gen. Bus. Law § 340\(6\)](#) ("In any action in [\*16] which claims are asserted against a defendant by both direct and indirect purchasers, the court shall take all necessary steps to avoid duplicate liability including but not limited to the transfer and consolidation of all related actions."); [S.D. Codified Laws § 37-1-33](#) ("In any subsequent action arising from the same conduct, the court may take any steps necessary to avoid duplicative recovery against a defendant"), but state courts have not defined these provisions to require stays in circumstances like those in this case.

The court could find only one statute that expressly warrants stays pending resolution of out-of-state direct purchaser litigation, but such stays are only authorized where indirect purchasers have obtained a judgment or settlement "prior to the completion of a direct purchaser's action." [Haw. Stat. Ann. § 480-13\(c\)\(7\)](#). Hawaiian courts are required to delay disbursement of damage awards to indirect purchasers until the direct purchasers' suits are resolved, the statute of limitations has run, or "in such a manner that will minimize duplication of damages to the extent reasonable and practicable." *Id.* Even this statute seems to recognize that duplication of damages [\*17] will occur; it simply attempts to minimize such duplication. These statutes provide little guidance, but they do not support the issuance of stay in this action.

The defendants cite [Asher v. Abbott Labs.](#), 307 A.D.2d 211, 212, 763 N.Y.S.2d 555, 556 (N.Y. App. Div. 1998), in support of a stay pending a federal action. This court's reasoning in this case, however, had nothing to do with New York's statutory mandate that courts "take all necessary steps to avoid duplicate liability" in state antitrust cases. Rather, the appellate court merely held that interests of "comity, orderly procedure, and judicial economy" required a stay pending the conclusion of the federal action, particularly where "the federal action commenced first and discovery [had] been completed." [Id. at 211; 763 N.Y.S.2d at 556](#).

The court is similarly inclined to abide by the goals of comity, orderly procedure, and judicial economy, but the defendants have provided little argument that a stay in this case would serve these goals. Although the multidistrict action in federal court is off to a head start, its discovery may not encompass the same areas necessary in this case, especially because injury here, if any, will involve [\*18] costs passed down a distribution chain. Federal direct purchaser suits do not delve into such matters. The court therefore sees no need to halt this action only to have to engage in discovery anyway after the federal action concludes.

Moreover, issuing a stay and delaying a recovery for Investors Corporation and the putative class potentially for years would be contrary to the broad remedial purpose of the Vermont Consumer Fraud Act. As the court noted above, "the [Vermont Consumer Fraud Act] is 'remedial in nature' and therefore must be construed 'liberally so as to furnish all the remedy and all the purposes intended.'" [Elkins v. Microsoft Corp.](#), 174 Vt. 328, 331, 817 A.2d 9 (2002) (quoting [State v. Custom Pools](#), 150 Vt. 533, 536, 556 A.2d 72 (1988)). A stay would not conform with this statutory purpose.

## ORDER

For the foregoing reasons, the defendants motion to dismiss and alternative motion for a stay are DENIED.

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## **Nilavar v. Mercy Health System-Western Ohio**

United States District Court for the Southern District of Ohio, Western Division

June 2, 2005, Decided; June 2, 2005, Filed

Case No. 3:99cv612

### **Reporter**

2005 U.S. Dist. LEXIS 60941 \*

SUNDAR V. NILAVAR, Plaintiff, vs. MERCY HEALTH SYSTEM-WESTERN OHIO, et al., Defendants.

**Prior History:** [Nilavar v. Mercy Health Sys., 142 F. Supp. 2d 859, 2000 U.S. Dist. LEXIS 20384 \(S.D. Ohio, Dec. 18, 2000\)](#)

## **Core Terms**

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geographic, patients, radiology, Defendants', unreliable, antitrust, consumers, methodology, inpatient, residing, effects, provide a service, hospital setting, diagnostic, principles, anticompetitive, reliability, threshold, markets, expert testimony, codes, exclusive contract, motion to exclude, state law claim, expert opinion, calculation, Merger, medical services, geographic area, order to obtain

**Counsel:** [\*1] For Sundar V Nilavar, Plaintiff: Kenneth A Lazarus, Maggi Ann Lazarus, LEAD ATTORNEYS, Kenneth A Lazarus & Assoc, Washington, DC USA; Lee Charles Falke, LEAD ATTORNEY, Lee C Falke & Associates, Dayton, OH USA.

For Mercy Health System-Western Ohio, doing business as Mercy Medical Center, also known as Mercy Health Partners, doing business as Mercy Medical Hospital, Catholic Healthcare, Catholic Healthcare Partners, Michael J Peterson, Jerold A Maki, Defendants: Jeffrey R Teeters, LEAD ATTORNEY.

**Judges:** WALTER HERBERT RICE, UNITED STATES DISTRICT JUDGE.

**Opinion by:** WALTER HERBERT RICE

## **Opinion**

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DECISION AND ENTRY OVERRULING IN PART AND SUSTAINING IN PART DEFENDANTS' MOTION TO EXCLUDE EXPERT OPINIONS AND TESTIMONY OF JOHN PISARKIEWICZ, PH.D. (DOC. #141)

Plaintiff Sundar V. Nilavar, M.D. ("Plaintiff" or "Nilavar"), is a radiologist who for years was employed by Springfield Radiology, Inc. ("SRI"). Up until 1995, SRI physicians provided diagnostic radiology services to three hospitals in the Springfield and Urbana areas, in Ohio, two of which are owned by Defendant Mercy Health Systems-Western Ohio ("MHS-WO" or "Mercy"). As of 1991, SRI was comprised of eleven principals. In March of 1995, MHS-WO invited different radiologists [\*2] and radiology groups to tender proposals to be its exclusive provider of such services. In December of 1995, Diagnostic Imaging Associates of Ohio, Inc. ("DIA"), a firm led by Dr. Robin Osborn ("Osborn"), was awarded the contract by MHS-WO to be its exclusive provider of radiology services, effective

January 1, 1996. As a consequence, on December 20, 1995, MHS-WO notified Plaintiff that his clinical privileges would be terminated, effective January 1, 1996.<sup>1</sup>

On November 19, 1999, Plaintiff initiated the present litigation against MHS-WO; Catholic Healthcare Partners ("CHP"), MHS-WO's parent company; Michael J. Peterson ("Peterson"), the former Regional President and Chief Executive Officer of MHS-WO; and Jerrold A. Maki ("Maki"), Mr. Peterson's successor as Regional President and CEO of MHS-WO.<sup>2</sup> Plaintiff asserted eight causes of action, to wit: (1) contract in restraint of trade, in violation of § 1 of the Sherman Act, [15 U.S.C. § 1](#); (2) tying arrangement in restraint of trade, in violation of § 1 of the Sherman Act; (3) contract and tying arrangement in restraint of trade, in violation of Ohio's Valentine Act, Chapter 1331 of the Ohio Revised Code; (4) a state law claim of tortious interference with a business relationship; (5) a state law [\*3] claim of breach of implied covenant of good faith and fair dealing; (6) a state law claim of civil conspiracy; (7) a state law claim of denial of right to due process; and (8) a state law claim of breach of contract.

In a decision entered on December 19, 2000, the Court dismissed the following claims: 1) Plaintiff's federal and state antitrust claims of an illegal tying agreement (Count Two and a portion of Count Three); 2) state law claim for breach of implied covenant of good faith and fair dealing (Count Five); 3) state law conspiracy claims (Count Six) as brought against Maki and Peterson, in their entirety; and 4) state law conspiracy claim (Count Six) against MHS-WO and CHP, as based on the breach of implied covenant of good faith and fair dealing, federal and state antitrust claims, and violation of [26 U.S.C. § 501\(c\)\(3\)](#). [Nilavar v. Mercy Health System-Western Ohio, 142 F. Supp.2d 859 \(S.D.Ohio 2000\)](#).

Currently before the Court is Defendants' Motion to Exclude Expert Opinions and Testimony of John Pisarkiewicz, Ph.D. (Doc. #141). Dr. Pisarkiewicz proposes to testify as to Plaintiff's definition of the relevant product and geographic markets at issue herein, and the purported effects of the exclusive contract on those markets. For the reasons that follow, Dr. Pisarkiewicz's [\*4] proposed testimony as to the geographic market is unreliable and thus must be excluded. Furthermore, Dr. Pisarkiewicz is not qualified to offer an expert opinion as to alleged anticompetitive effects of Mercy's exclusive contract with DIA. As such, for the reasons described herein, his testimony on that issue will be excluded as well.

As the Court has noted previously, this matter is governed by the rule of reason. See [Nilavar, 142 F. Supp.2d at 873](#). As opposed to the per se analysis of alleged antitrust violations, which identifies certain practices that "are entirely void of redeeming competitive rationales," a rule of reason analysis requires a court to analyze the history of the restraint and the restraint's effect on competition. [National Hockey League Players' Ass'n v. Plymouth Whalers Hockey Club, 325 F.3d 712, 718 \(6th Cir. 2003\)](#), citing [Law v. Nat'l Collegiate Athletic Ass'n, 134 F.3d 1010, 1016 \(10th Cir. 1998\)](#). Under this analysis, an antitrust plaintiff must establish that the restraint, the conduct complained of, produces significant anticompetitive effects within relevant product and geographic markets. *Id.*, citing [Tanaka v. Univ. of Southern Cal., 252 F.3d 1059, 1063 \(9th Cir. 2001\)](#). In this case, Dr. Pisarkiewicz would testify that the product market is defined as "the physician component of diagnostic radiology services provided in a hospital setting," with a relevant product submarket of the provision of such services to hospital inpatients [\*5] (Report of John Pisarkiewicz, Ph.D. ("Pisarkiewicz Report"), Doc. #98 at ¶ 16). In his report, Dr. Pisarkiewicz defined the relevant geographic market as Clark and Champaign counties (*Id.*). The definition of the geographic market was subsequently amended by Dr. Pisarkiewicz as consisting of 19 ZIP codes "covering most of Clark and Champaign counties" (Doc. #144, Tab A (Second Affidavit of John Pisarkiewicz, Ph.D.), at 4-5).

#### I. Standards Governing Motions to Exclude Expert Testimony

The admissibility of expert testimony is governed by [Rule 702 of the Federal Rules of Evidence](#), which provides:

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<sup>1</sup> The Court previously set forth a more thorough iteration of the facts and circumstances giving rise to this litigation. [Nilavar v. Mercy Health System-Western Ohio, 142 F. Supp.2d 859 \(S.D.Ohio 2000\)](#).

<sup>2</sup> Plaintiff also set forth claims against Osborn and DIA, all of which have been dismissed. See Doc. #71.

If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case.

In *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 113 S. Ct. 2786, 125 L. Ed. 2d 469 (1993), the Supreme Court "established a general gatekeeping [or screening] obligation for trial courts" to exclude from trial expert [\*6] testimony that is unreliable and irrelevant. *Conwood Co., L.P. v. U.S. Tobacco Co.*, 290 F.3d 768, 792 (6th Cir. 2002) (citations omitted). This gatekeeping function applies "when considering all expert testimony, including testimony based on technical and other specialized knowledge." *Clay v. Ford Motor Co.*, 215 F.3d 663, 667 (6th Cir. 2000), citing *Kumho Tire Co., Ltd. v. Carmichael*, 526 U.S. 137, 141, 119 S. Ct. 1167, 143 L. Ed. 2d 238 (1999) (emphasis in original).

The district court must determine whether the evidence "both rests on a reliable foundation and is relevant to the task at hand." *Id.* (citation omitted). In assessing relevance and reliability, the district court must examine "whether the expert is proposing to testify to (1) scientific knowledge that (2) will assist the trier of fact to understand or determine a fact in issue." *Jahn v. Equine Servs., PSC*, 233 F.3d 382, 388 (6th Cir. 2000) (citations omitted). This involves a preliminary inquiry as to whether the reasoning or methodology underlying the testimony is scientifically valid and whether that reasoning or methodology properly can be applied to the facts in issue. *Id.* (citation and internal quotation marks omitted). Some of the factors that may be used in such an inquiry include: (1) whether the theory or technique has been tested and subjected to peer review and publication, (2) whether the potential rate of error is known, and (3) its general acceptance. *Hardyman v. Norfolk & W. Ry. Co.*, 243 F.3d 255, 260 (6th Cir. 2001). "This inquiry is a flexible one, [\*7] with an overarching goal of assessing the 'scientific validity and thus the evidentiary relevance and reliability' of the principles and methodology underlying the proposed expert testimony." *United States v. Langan*, 263 F.3d 613, 621 (6th Cir. 2001) (citation omitted). "[A] trial judge must have considerable leeway in deciding in a particular case how to go about determining whether particular expert testimony is reliable." *Kumho Tire Co., Ltd. v. Carmichael*, 526 U.S. 137, 152, 119 S. Ct. 1167, 143 L. Ed. 2d 238 (1999).

## II. Analysis

Defendants advance four arguments in support of their motion to exclude Dr. Pisarkiewicz's testimony, to wit: first, generally, that the proposed market definition is deficient as a matter of law; second, that Dr. Pisarkiewicz's definition of the product market is unreliable; third, that Dr. Pisarkiewicz's definition of the geographic market is unreliable; and fourth that he cannot provide expert testimony on the anticompetitive effects of the exclusive contract between Mercy and DAI. Following a brief discussion of Dr. Pisarkiewicz's qualifications as an expert, each argument will be addressed in turn.

### A. Dr. Pisarkiewicz's Qualifications as an Expert

Dr. Pisarkiewicz is an economist and Principal Consultant at Nathan Associates, an economic consulting firm in Arlington, VA, and is also an adjunct Professor [\*8] at George Washington University, where he teaches a graduate course in Health Economics. He served at the United States Federal Trade Commission ("FTC") as Acting Director of the Office of Policy Planning and Evaluation, and also as the FTC's chief economist in its antitrust suit against the American Medical Association (Pisarkiewicz Report at ¶ 1). His qualifications to opine as to issues of market definitions and competition are not in serious dispute.<sup>3</sup>

### B. Legal Propriety of Plaintiff's Proposed Market

The relevant product market is a product or service, or the smallest group of products or services, for which a hypothetical monopolist could profitably charge more than the competitive price for a significant period of time.

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<sup>3</sup> But see *infra*, describing his lack of qualifications to opine as to health management quality issues.

Repeating arguments advanced in their Motion for Summary Judgment (Doc. #117), Defendants insist that Plaintiff's market definition is legally foreclosed by decisions from courts examining similar instances of exclusive provider arrangements in the context of hospitals. Specifically, they rely heavily on the Supreme Court's decision in Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 104 S. Ct. 1551, 80 L. Ed. 2d 2 (1984), as well as upon this Court's decision in Reddy v. Good Samaritan Hosp., 137 F. Supp.2d 948 (S.D. Ohio 2001). According to Defendants, these decisions stand for the proposition that [\*9] "when a physician challenges a hospital's use of an exclusive contract, the relevant market is the area in which physicians compete for jobs" (Doc. #141 at 2-3). In other words, the Defendants contend that the product market is physicians' jobs, which, geographically, is a nationwide one. As such, Defendants urge the Court to reject Dr. Pisarkiewicz's opinions, in that they posit a market different from the markets defined in Jefferson Parish and Reddy.

The Court rejects this argument because it disagrees with Defendants' interpretation of Jefferson Parish and Reddy. As will be spelled out more thoroughly when the Court decides Defendants' motion for summary judgment, those decisions did not define, as a matter of law, the relevant product and geographic markets for instances in which a hospital enters into an exclusive contract with a medical services provider.

Refusing to exclude Dr. Pisarkiewicz's testimony due to alleged legal insufficiency, the Court turns to Defendants' arguments that his opinions regarding the product and geographic markets should be excluded, because he failed to employ reliable principles and methods to reach those opinions. As a means of analysis, the Court [\*10] initially discusses the opinion of Dr. Pisarkiewicz concerning the relevant product market, before turning to his opinion pertaining to the relevant geographic market.

### C. Relevant Product Market

As noted supra, Dr. Pisarkiewicz finds the existence of a relevant product market consisting of the physician component of diagnostic radiology services provided in a hospital setting. Defendants' chief complaint is that there is no basis for distinguishing radiology services that are performed in a hospital setting from those performed in non-hospital settings, such as stand-alone clinics or imaging centers. Defendants make this argument in a number of different ways. None is persuasive.

They first argue that this classification was derived solely in reliance on Dr. Nilavar's opinion. However, the distinction is also made by Ian Marshall Lande, M.D., Plaintiff's expert in the science and practice of radiology. Specifically, Dr. Lande, whose proposed opinion testimony has not been challenged by Defendants,<sup>4</sup> identifies three pertinent differences between radiology services provided in a hospital setting and those provided in other facilities:

Firstly, the patient populations served are very different. [\*11] Those served in hospitals typically are less stable medically, less agile, frequently the very old or young, often debilitated requiring the use of stretchers, traction devices, respirators, cardiac monitors, hyper alimentation, life support systems, infusion pumps, awkward medical equipment, orderly staff, paramedical personnel (therapists etc.) and nurses to name a few. Imaging these patients outside a hospital would be medically inappropriate if not impossible. Secondly, some patients have communicable diseases or suffer from disorders that require sterile environments. Imaging these patients outside a hospital would place the patient or general public at risk. Individuals referred from critical sections such as the ICU, emergency room, recovery room, or cardiac care unit clearly must have access to hospital based services. Finally, some studies require sedation, anesthesia, or intraoperative guidance, thereby limiting these types of procedures to a hospital setting.

Doc. #99, Tab E at 2. As such, the Court is unconvinced that the fact that Dr. Pisarkiewicz's opinion was informed by Dr. Nilavar necessarily renders unreliable the distinction between the locations where radiology services are [\*12] provided. Even ignoring Dr. Lande's opinion, Defendants are unclear as to why Dr. Pisarkiewicz's reliance

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<sup>4</sup> Defendants had filed a Motion to Exclude Expert Opinions and Testimony of Ian Marshall Lande, M.D. Designated by Plaintiff Sundar V. Nilavar (Doc. #124), but subsequently withdrew said motion. See Agreed Order Relating to Discovery Motions (Doc. #143)).

on the assessment of the practice of radiology by Dr. Nilavar, who is board-certified in that specialty, would render unreliable the principles and methods Dr. Pisarkiewicz relied upon when defining the relevant product market.

Next, Defendants argue that Dr. Pisarkiewicz's classification of radiology services is not recognized by any radiological licensure or credentialing system, that it is not referenced in any of the case law regarding exclusive radiology contracts, and that it is repudiated by Defendants' expert (Doc. #141 at 5-6). On their face, none of these claims addresses the methodology employed by Dr. Pisarkiewicz in formulating his decision. Instead, they each refer to a point of supposed authority that reaches a conclusion that is in conflict with the conclusion reached by him. However, it is well established that a court's analysis of the reliability of expert testimony is to focus on the methodology and principles used by the expert, and not on the expert's results or conclusions. [Clay, 215 F.3d at 667, citing Daubert, 509 U.S. at 595](#). For the same reason, reference to contrary conclusions of other authority [\*13] (even other expert witnesses), without a critique of a proffered expert's methodology or an account of some logical insufficiency of the expert's opinion, will not invalidate proposed expert testimony under [Rule 702](#).<sup>5</sup>

Defendants offer no other reasons for rejecting Dr. Pisarkiewicz's testimony with respect to his definition of the relevant product market. Accordingly, the methodology employed by Dr. Pisarkiewicz in defining the product market in this case is not a basis on which to exclude his expert opinion.

#### D. Relevant Geographic Market

In addition to defining a relevant product market, Plaintiff also has the burden of defining a relevant geographic market. The relevant geographic market is the locale in which consumers of a product or service can turn for alternate sources of supply. The central rubric in evaluating the relevant geographic market is as follows: "[T]he area of effective competition in the known line of commerce must be charted by careful selection of the market area in which the seller operates, and to which the purchaser can practicably turn for supplies." [White and White, Inc. v. American Hosp. Supply Corp., 723 F.2d 495, 501 \(6th Cir. 1983\)](#) (quoting [Tampa Electric Co. v. Nashville Coal Co., 365 U.S. 320, 81 S. Ct. 623, 5 L. Ed. 2d 580 \(1961\)](#)). A "properly defined geographic market includes potential suppliers [\*14] who can readily offer consumers a suitable alternative to the defendant's services." [Fed. Trade Comm'n v. Tenet Health Care Corp., 186 F.3d 1045, 1052 \(8th Cir. 1999\)](#).

As noted *supra*, Dr. Pisarkiewicz defines the geographic market as an area composed of 19 ZIP codes contained within Clark and Champaign Counties. His primary tools for opining that Defendants exercise market power in that geographic area are the Elzinga-Hogarty test and the critical loss test. Defendants counter that Dr. Pisarkiewicz's opinion as to Mercy's market power is unreliable, because he has manipulated those tests in order to arrive at a calculation favorable to Plaintiff's argument.

##### 1. Elzinga-Hogarty Test

The Elzinga-Hogarty test, devised by professors of economics Kenneth G. Elzinga and Thomas F. Hogarty, analyzes patterns of consumer origin and destination to identify relevant competitors of the contracting entities. See, e.g., [Fed. Trade Comm'n v. Freeman Hosp., 69 F.3d 260, 264 \(8th Cir. 1995\)](#); [United States v. Rockford Memorial Corp., 717 F. Supp. 1251, 1266 \(N.D.Ill. 1989\)](#), aff'd, [898 F.2d 1278 \(7th Cir.\)](#), cert. denied, [498 U.S. 920 \(1990\)](#). The test discerns market power by analyzing the movement of goods or services in or out of a proposed geographic market. It normally does so through the use of a two-pronged inquiry, to wit: the extent to which the product migrates out from inside the market and the extent to which the product migrates in from outside the market. For [\*15] antitrust purposes, a plaintiff would need to show that such in-flow and out-flow is low in order to prove that the actions of a firm with market power could have an adverse effect on competition. In the normal scenario involving the sale of a product, the two prongs of the Elzinga-Hogarty test are referred to, respectively, as LOFI (Little Out From Inside) and LIFO (Little In From Outside).

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<sup>5</sup> With respect to the purported case law rejecting Dr. Pisarkiewicz's definition of the product market, Defendants cite cases that are of the same ilk as [Jefferson Parish and Reddy](#). Similarly to Defendants' reliance on [Jefferson Parish and Reddy](#), the cases simply do not stand for the proposition that the relevant product market in this case has been defined as a matter of law, and, even if it had, such an argument would not, *per se*, be a reason to exclude Dr. Pisarkiewicz's testimony.

Of course, in a dispute arising out of the provision of health care, such as this one, the migration of products into or out from a particular geographic market is not implicated. Rather, the operative analysis in the health care setting is to determine what percentage of patients who reside within the geographic market leave that market to obtain medical services (out-migration of patients) and what percentage of patients who reside outside the geographic market travel to the market to obtain medical services (in-migration of patients). LOFI and LIFO scores are expressed in percentages — i.e., the sales of sellers located in the particular geographic area to customers in that same area divided by the total sales of these firms to all destinations, and the sales of firms in the producing area to [\*16] customers located in that area divided by the total purchases these customers make from all sellers wherever located. Kenneth G. Elzinga and Thomas F. Hogarty, The Problem of Geographic Market Delineation Revisited: The Case of Coal, 23 The Antitrust Bulletin 1, 2 (1978). Therefore, to show that Mercy has market power, Plaintiff herein would need to show that few residents of his proposed geographic market leave the area to obtain hospital-based radiological services (low in-migration of Mercy's competitor's services) and that few patients residing outside of his proposed geographic market come to the area to obtain hospital-based radiological services (low out-migration of Mercy's services). Low percentages of patients inside the proposed geographic market migrating outside that market or low percentages of those residing outside migrating inside it would demonstrate the existence of a cohesive geographic market, which would cause an antitrust defendant's alleged anticompetitive conduct to have a greater impact upon that market.

The use of the Elzinga-Hogarty test proves (or disproves) an antitrust litigant's formulation of a relevant geographic market by establishing a minimum threshold [\*17] percentage that must be met by the levels of in-migration and out-migration, as expressed in the ratios described above, in order to demonstrate the existence of a geographic market. Professors Elzinga and Hogarty wrote that the appropriate threshold for identifying a distinct geographic market is 90% of the consumers residing in a particular geographic area obtaining the relevant product within that area and 90% of those obtaining the product in that area residing therein. See id. (eschewing their initial formulation in a prior article of a 75% threshold as a "weak" result). In other words, a geographic market is properly defined when 10% or less of consumers in the area leave that area to obtain the relevant product and when 10% or less of consumers who obtain the relevant product within the geographic area come from outside the area. Courts which have employed the Elzinga-Hogarty test in antitrust cases agree that a 10% threshold is needed for a strong result. See, e.g., Gordon v. Lewiston Hosp., 272 F. Supp.2d 393, 426 (M.D.Pa. 2003); California v. Sutter Health System, 130 F. Supp.2d 1109, 1121 (N.D.Cal. 2001); Fed. Trade Comm'n v. Freeman Hosp., 911 F. Supp. 1213, 1218 (W.D.Mo.) (recognizing Professors Elzinga's and Hogarty's express abandonment of a 25% threshold in favor of a 10% threshold), aff'd, 69 F.3d 260 (8th Cir. 1995).

In Dr. Pisarkiewicz's Report, he proposed a relevant geographic market of Clark and [\*18] Champaign Counties, which includes Mercy Medical Center and Community Hospital in Springfield, Ohio (Clark County) and Mercy Memorial Hospital in Urbana, Ohio (Champaign County). The Elzinga-Hogarty percentages for that formulation of the geographic market were an in-migration ratio of 4.8% and an out-migration ratio of 25.0%. Even though Elzinga and Hogarty expressly characterized 25% as a weak result, Dr. Pisarkiewicz described it as "a good result" (Pisarkiewicz Report at ¶ 30). Nonetheless, in the Report, he suggested that the results could be strengthened by utilizing individual ZIP codes rather than county borders (Id. at ¶ 33).

Contemporaneous with his deposition in this matter on July 22, 2003, Dr. Pisarkiewicz supplemented the Report with further analysis. As he predicted in his Report, the use of ZIP codes yielded stronger results than county boundaries. According to the Report, the results were strengthened by removing from consideration ZIP codes in the southwest corner of Clark County and from the northeast corner of Champaign County. Presumably, this is so, because individuals in those areas, which are closer to Dayton and Columbus, respectively, are likely to travel to [\*19] hospitals in those larger markets instead of one of the three hospitals involved herein. This caused the outflow percentage to drop to 16%, while the inflow percentage increased to 11% (Pisarkiewicz Report at ¶ 33). As Defendants note, this was still shy, on both accounts, of the 10% cut-off for a strong result under the Elzinga-Hogarty test. Accordingly, toward the conclusion of Dr. Pisarkiewicz's deposition, he expressed an intention to refine further the analysis in order to improve the results with respect to that test.

On September 12, 2003, Plaintiff submitted the Affidavit of John Pisarkiewicz, Ph.D., dated August 5, 2003 (Doc. #125, Ex. Q ("Pisarkiewicz Affidavit")). Therein, Dr. Pisarkiewicz reports that after further refinement of his analysis, the average of the LOFI and LIFO scores is 91.3% - a level that, according to Dr. Pisarkiewicz, "clearly meets the [Elzinga-Hogarty] guidelines" (*Id.* at ¶ 3(m)).

Defendants' first critique of Dr. Pisarkiewicz's methodology is based not on any refinement made to his original calculations, but to his overall practice of "appl[ying] hospital-wide inpatient data even though his client complains of a restraint of trade in diagnostic radiology [\*201] procedures" (Doc. #141 at 7) (emphasis in original). In an affidavit of Dr. Pisarkiewicz filed subsequent to Defendants' motion to exclude his opinions (Doc. #144, Tab A ("Second Affidavit of John Pisarkiewicz")), he explains that this is a distinction without a difference, "because virtually every inpatient has some sort of radiology procedure" (*Id.* at ¶ 14). As Plaintiff notes, such hospital-wide inpatient data merely serves as a proxy for physician diagnostic radiology services (Doc. #144 at 9). Defendants quibble with this, yet the Court is unwilling to make a factual determination at this point as to whether Plaintiff's proxy argument is correct.

Regardless, the lion's share of Defendants' complaint with Dr. Pisarkiewicz's methodology relates to the refinements made subsequent to his original Report. In each instance, Defendants allege that Dr. Pisarkiewicz's refinement was actually a result-oriented manipulation intended to produce a LOFI/LIFO calculation that would be favorable to Plaintiff's claimed geographic market. Specifically, the adjustments at issue are the following: First, Dr. Pisarkiewicz excluded various specialty and out of state hospitals from his analysis.<sup>6</sup> Second [\*211], he excluded patients who required a procedure for which more than 90% of patients left the market. Third, he excluded patients whose records did not report a code indicating what sort of procedure they obtained. Fourth, he excluded patients who received obstetrics and newborn care.

The Court is most troubled by the second exclusion — i.e., the exclusion of patients who required a procedure for which more than 90% of patients left the market. Dr. Pisarkiewicz explains that this exclusion was necessary in order to ignore procedures that are "generally not available or not available in sufficient quantity or quality at the three hospitals in the relevant market" (Pisarkiewicz Second Affidavit at ¶ 16). According to him, "[t]he whole point of these adjustments is to focus on the type of patients who would seek the types of service available at the three hospitals [in the proposed geographic area]. And it is the market for the radiology services available to these types of patients that was adversely affected by the actions of the defendants" (*Id.* at ¶ 18). In his opposition memorandum, Plaintiff echoes this explanation: "[T]he idea was to ensure that the LIFO/LOFI figures were not unfairly [\*22] distorted through the inclusion of irrelevant data and to focus on the types of patients who seek the services available at the three hospitals within Clark and Champaign Counties. It is the [availability of] radiology services ... to these types of patients that was adversely affected by the actions of the Defendants" (Doc. #144 at 10).

First, this explanation is incorrect as a matter of law. The Sixth Circuit, in defining a geographic market, has indicated that, although there may be some cross-over of product at the edge of a market, "when the evidence indicates that a large proportion of consumers within the proposed area in fact turn to alternative sources of supply outside the proposed area, the market boundaries posited by the plaintiff must be rejected." *Re/Max Int'l, Inc. v. Realty One, Inc.*, 173 F.3d 995, 1017 (6th Cir. 1999), citing *Bathke v. Casey's Gen. Stores, Inc.*, 64 F.3d 340, 346 (8th Cir. 1995). This rationale was applied in the medical services context in *Sutter, supra*, to which Plaintiff claims fidelity in his application of the Elzinga-Hogarty test. In that case, which involved the merger of two hospitals, the court explained that

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<sup>6</sup>These hospitals include Cincinnati Children's Hospital Medical Center, Cleveland Clinic Foundation, James Cancer Hospital and Solove Research Institute, Children's Hospital Columbus, and The Children's Medical Center of Dayton, Dearborn County, Gateway Rehab, Hillside Rehabilitation, Margaret Mary, Reid, Rainbow Babies and Children's Hospital, St. Elizabeth, St. Lukes East and West, Todd Children's Hospital, "and other out of state hospitals" (Doc. #125 Ex. Q, Table 1).

[w]here a hospital outside of the proposed geographic market draws patients from the same region from which the merging hospitals draw their patients, the hospital located outside of the test [\*23] market is considered a practical alternative to which patients residing in the area of overlap can turn for acute inpatient services.

California v. Sutter Health System, 84 F. Supp.2d at 1073. See also, Freeman Hosp., 911 F. Supp. at 1220 ("If the service area residents currently use other hospitals, then those hospitals are considered alternatives to the [hospitals within the proposed geographic market];" therefore, the geographic market must include those hospitals.). By Dr. Pisarkiewicz's own admission, there are a number of procedures for which a highly substantial percentage of patients (90% or more) leave the proposed geographic market. Accordingly, by ignoring these statistics, Dr. Pisarkiewicz's opinion is unreliable, not merely in the methodological sense with which economists are concerned, but in a legal sense, as well.

Second, and possibly more important for present purposes, Dr. Pisarkiewicz's exclusion of services, the inclusion of which would cause Plaintiff's proposed geographic market to score worse on the Elzinga-Hogarty test, is a blatant contradiction of his proposed product market, and possibly an effort to manipulate that test. As noted *supra*, Plaintiff's proposed product market is the physician component of diagnostic radiology services provided in a [\*24] hospital setting (Plaintiff's Memorandum in Opposition to Defendants' Motion for Summary Judgment (Doc. #126 at 41); Pisarkiewicz Report at ¶ 16). This formulation did not limit the definition to certain types of diagnostic radiology services provided in a hospital setting, nor did it limit the definition to such services provided in certain circumstances. In fact, as noted *supra*, according to Dr. Pisarkiewicz, the provision of hospital-wide services can be used as a proxy for the provision of radiology services. Yet, in an effort to justify the exclusion of the above data, Dr. Pisarkiewicz claims that "[t]he relevant product market is limited to the products and services available at the 3 hospitals" (Pisarkiewicz Affidavit at ¶ 3(j)). If this statement is to be given weight, it constitutes a replacement of the originally-stated product market with an utterly self-serving product market, which Plaintiff seemingly would define as the market for services provided by the three hospitals located in Clark and Champaign Counties. First, this results-oriented mode of economic analysis is not acceptable. The history of Dr. Pisarkiewicz's analysis shows a concerted effort, spanning his expert [\*25] witness report, his deposition and his two supplemental affidavits to tinker with the data such that the LOFI/LIFO scores would meet the 10% threshold. Obviously, Dr. Pisarkiewicz was successful in meeting the threshold, but only by way of contorting the market definitions into something lacking any basis in economics or antitrust law. As a consequence, he employed unreliable principles and methods. See Fed. R. Evid. 702(2).

Moreover, Dr. Pisarkiewicz himself admits that at least some of the patients who left the area for services (who were excluded from his analysis) did so not because the service they required was not available at one of the three hospitals in the area, but because they chose a hospital with services that they perceived to be better: "It is certainly the case that I excluded from consideration inpatients from the market who ... sought certain [procedures] generally not available or not available in sufficient quantity or quality at the three hospitals in the relevant market" (Pisarkiewicz Second Affidavit at ¶ 16) (emphasis added).<sup>7</sup> A consumer's choice to purchase a product that he or she believes to be of superior quality is emblematic of the presence of competition. The only possible [\*26] basis for excluding transactions in which consumers freely exercised such choice would be to conceal the presence of actual competition. In asserting the inelasticity of patient demand for radiology services, Dr. Pisarkiewicz, in his original Report, explained that "the question of geographic boundaries is usually answered by examining where patients actually obtain hospital services" (Pisarkiewicz Report at ¶ 28). Yet, his final calculations intentionally exclude the reality of where many patients in Clark and Champaign Counties obtain their hospital radiology services.

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<sup>7</sup> With respect to the notion of "sufficient quantity," in his original Report, Dr. Pisarkiewicz explained that there are types of "specialized medical services ... for which patients are likely to search more widely and place greater trust in a hospital [that] performs these specialized procedures more frequently than [Mercy Medical Center, Mercy Memorial Hospital or Community Hospital]" (Pisarkiewicz Report at ¶ 34). Accordingly, to say that a service is not available in sufficient quantity is actually another way of saying that it is perceived to be not available in sufficient quality.

The first and fourth exclusions described, supra, trigger essentially the same concerns because they operate to exclude data in a manner inconsistent with Plaintiff's proffered product market definition. Specifically, they exclude from consideration patients who traveled out of the area to visit specialty and or out of state hospitals (the first exclusion) as well as patients requiring obstetrics and newborn care services (the fourth exclusion). Like the 90% exclusion, Dr. Pisarkiewicz excluded these services because of their supposed unavailability in the proposed geographic market. Specifically, Dr. Pisarkiewicz admitted [\*27] that obstetrics care is, in fact, available in the proposed geographic market (at Community Hospital) but possibly not in the quality or quantity preferred by consumers. As explained supra, the fact that consumers travel elsewhere for medical services that they perceive to be better suggests the presence of competition and does not suggest a reason for excluding such services from consideration. The same criticism applies to his exclusion of so-called specialty hospitals.<sup>8</sup> Again, as Defendants note, these facilities presumably perform the same sort of radiological services as the hospitals that are not excluded from Dr. Pisarkiewicz's data set, yet there is no explanation for their exclusion (Doc. #141 at 10).

Finally, with respect to the third exception — the elimination of cases that are missing procedure codes — Dr. Pisarkiewicz assumes that these cases would possess the same rates of in-migration and out-migration as those that are not missing the codes. Although the Court offers no opinion as to the efficacy of this assumption, it does agree with Defendants that, assuming Dr. Pisarkiewicz is correct, this exclusion would raise the exact same concerns as those that exist with regard [\*28] to the 90% exclusion described, supra.

In terms of Daubert and Rule 702(2), Dr. Pisarkiewicz's opinion is unreliable, given that it rests on unreliable principles and methods. Although the Court can assume, *arguendo*, that a standard application of the Elzinga-Hogarty test would be perfectly admissible under Daubert, the same cannot be said of Dr. Pisarkiewicz's application of that test to the facts of this case. To be sure, it appears that the Elzinga-Hogarty test has been tested and subjected to review, not only by other economists, but by the creators of the test themselves, who revisited its mechanics in order to address purported errors and to ensure what they believed to be more accurate results. See Kenneth G. Elzinga and Thomas F. Hogarty, The Problem of Geographic Market Delineation Revisited: The Case of Coal, 23 The Antitrust Bulletin 1 (1978) (responding to the test's critics and tweaking it accordingly). Further, based on the test's widespread use by courts which have adjudicated antitrust claims, see supra, it appears to be accepted generally in the economic and legal communities.

Yet, for the reasons described herein, Dr. Pisarkiewicz did not employ the Elzinga-Hogarty test in the [\*29] manner in which it was intended. As the Supreme Court noted in a decision examining Daubert, although it is true that Daubert directs district courts to evaluate a proffered expert's methodology and not his conclusion, "nothing in either Daubert or the Federal Rules of Evidence requires a district court to admit opinion evidence that is connected to existing data only by the *ipse dixit* of the expert." General Electric Co. v. Joiner, 522 U.S. 136, 146, 118 S. Ct. 512, 139 L. Ed. 2d 508 (1997). Here, Dr. Pisarkiewicz's conclusion that Plaintiff's proposed market satisfies the requirements of the Elzinga-Hogarty test is, at best, based on his *ipse dixit* that much data, deemed by this Court to be relevant, based upon the above discussions, should have been excluded from analysis. At worst, Dr. Pisarkiewicz's conclusion is based on a manipulation of the test employed in order to reach a preferred result. As the Court noted above, neither law nor logic compelled the adjustments that facilitated the conclusion reached by Dr. Pisarkiewicz with respect to the Elzinga-Hogarty test. At best, he employed unreliable methods and principles.

Based upon the foregoing, the Court concludes that the opinion of Dr. Pisarkiewicz with respect to Plaintiff's proposed geographic market definitions, [\*30] insofar as they are based on an unreliable application of the Elzinga-Hogarty test, must be excluded.

## 2. Critical Loss Test

Dr. Pisarkiewicz also attempts to justify his exclusions using the critical loss test. Critical loss analysis inquires as to whether the purported monopolist would be able to raise prices without causing the "critical loss" of enough consumers to make the increase in prices unprofitable. Tenet, 186 F.3d at 1053. This test is employed by the FTC

<sup>8</sup> Defendants suggest that some of the hospitals in Dr. Pisarkiewicz's list are not actually specialty facilities. For example, they suggest that the Cleveland Clinic "is not a specialty hospital at all but rather a tertiary acute care hospital" (Doc. #141 at 10).

in its Horizontal Merger Guidelines, which are used by the FTC to ascertain a relevant geographic market in exercising its prosecutorial discretion to challenge a merger. See Department of Justice, Federal Trade Commission, Antitrust Division, 1992 Horizontal Merger Guidelines, 57 Fed. Reg. 41552 § 1.21. The Merger Guidelines define a geographic market "to be a region such that a hypothetical monopolist ... could profitably impose at least a 'small but significant and nontransitory' increase in price ["SNIP"]..." Id. The standard SNIP size recommended by the Merger Guidelines is a 5% increase. Sutter, 84 F. Supp.2d at 1077. Accordingly, the critical loss test addresses the question of whether the geographic market has been properly defined by analyzing the number of consumers that [\*31] must leave the market, if faced with an anticompetitive price increase, before a hypothetical monopolist would abandon its attempts to impose a SNIP. Id. at 1076 (citations omitted). Herein, the critical loss test would ask how many patients would have to leave the market in order to defeat a price increase of 5%, and also whether those consumers actually would leave the market. Id. at 1077.

Defendants' main complaint regarding Dr. Pisarkiewicz's utilization of the critical loss test is that he relied upon "gross charges" for inpatient and outpatient radiological services in calculating the critical loss figure, instead of the actual, net revenue obtained by the hospitals from such services (Doc. #141 at 13). Defendants also point out the "gross charges" for such radiological services are 30 to 40% higher than the actual revenue received. Dr. Pisarkiewicz defends the use of the gross charges in that they "become bargaining positions for negotiations with managed care plans," presumably making them instructive as to actual revenues (Pisarkiewicz Second Affidavit at ¶ 26). In any case, Dr. Pisarkiewicz also indicates that "these [were] the only data the defendant saw fit to turn over..." (Id.). For this reason, [\*32] Plaintiff believes that Defendants' complaint "is grossly unfair" (Doc. #144 at 13).

Regardless of whether the data used by Dr. Pisarkiewicz to gauge supposed revenues was the correct set of data, and regardless of the fairness of Defendants' conduct, the Court believes that the same manipulations of the patient data that proved fatal to Dr. Pisarkiewicz's Elzinga-Hogarty analysis also prove fatal to his critical loss analysis. As suggested supra, an important factor of critical loss analysis is the determination of whether patients actually would leave the proposed market in the event of a SNIP. This is referred to as diversion analysis. See Sutter, 84 F. Supp.2d at 1078-81. As Defendants note, in Sutter, the court rejected the plaintiff's diversion analysis, pointing to, inter alia, the plaintiff's own Elzinga-Hogarty results, which indicated that one out of seven patients — approximately 14% - residing in the proposed market left in order to obtain inpatient services, even in the absence of a 5% price increase. Id. at 1080. Herein, before employing the dubious exclusions described supra, Dr. Pisarkiewicz found that 25% of residents within the proposed geographic market were leaving in order to obtain radiology services incident [\*33] to hospital care. Given that 25% of the users of the relevant product (the physician component of radiology services in a hospital setting) are already leaving the proposed geographic market to obtain such services, it is inescapable that patients would leave that market in the event of a SNIP. Consequently, regardless of whether these patients left the area in order to obtain services that were not available in Clark or Champaign County, or whether they left in order to obtain services that were or were deemed superior to those available in those counties, it defies logic to suggest that these same patients would not leave in the event of an anticompetitive price increase. Dr. Pisarkiewicz insists that the fact that patients travel to locations such as Dayton or Columbus in order to obtain inpatient radiology services provided in connection with hospital services available in those places, and not available in the proposed geographic market, does not detract from his application of the test (Pisarkiewicz Second Affidavit at ¶ 19). Yet, as explained supra, this contradicts Plaintiff's stated formulation of the product market, which is diagnostic radiology services provided in a hospital [\*34] setting. This definition does not distinguish radiology services based on the type of underlying care provided (other than whether it is being provided on an inpatient or outpatient basis). Implying that Plaintiff's market definition does make such a distinction is merely a results-oriented attempt to influence the geographic market analysis in Plaintiff's favor.

Defendants make other arguments incident to their critical loss analysis, regarding such issues as service area overlap and calculation of driving times between markets. The Court does not find it necessary to address those issues, since the flaws in Dr. Pisarkiewicz's diversion analysis are sufficient to defeat the reliability of his opinion regarding the critical loss test.

As it did with respect to the Elzinga-Hogarty test, the Court assumes, without deciding, that a standard application of the critical loss test would satisfy the requirements set forth in Daubert and Rule 702. Yet, because the Court can find no justifiable explanation for ignoring key data for the critical loss test, it concludes that Dr. Pisarkiewicz's principles and methods in applying that test are unreliable; therefore, the resultant, unreliable opinion must [\*35] be excluded pursuant to Daubert and Rule 702.

#### E. Anticompetitive Effects

Lastly, Defendants dispute Dr. Pisarkiewicz's qualifications to opine as to the alleged anticompetitive effects of Mercy's contract with DIA. Specifically, Dr. Pisarkiewicz opines that this contract will cause such effects, because it will result in problems with record keeping and transcription services for physicians' notes at Mercy Hospitals, the reduction of patients' choice of physicians, and the excessive use of locum tenens physicians.<sup>9</sup>

Both Dr. Pisarkiewicz and Plaintiff's counsel have admitted in a number of different instances that Dr. Pisarkiewicz is offered as an expert in the area of economics, and not health care management. See, e.g., Pisarkiewicz Second Affidavit at ¶ 39 (expressing that he is unclear as to what role Dr. Osborn or DIA played with respect to the transcription problems — either in creating them or in being responsible for them); Pisarkiewicz Depo. at 187-88 (Plaintiff's counsel objecting to questions posed by Defendants' counsel regarding quality of transcription services because "[that subject is] completely outside the realm of his expertise"); Id. at 335-36 (explaining that his background [\*36] does not include econometric analyses in health care using outcome quality variables); Id. at 314 (Plaintiff's counsel explaining that Dr. Pisarkiewicz "claims to be an expert in economics, not health management"). Dr. Pisarkiewicz's own description of his credentials describes his background in medical antitrust cases, with respect to market definitions and impact on competition, but is silent as to anything in his background that would qualify him as an expert in health care quality issues. See Pisarkiewicz Report at ¶ 1.

In view of the fact that neither Plaintiff nor Dr. Pisarkiewicz believes that his expertise extends to the health management quality concerns on which he purports to offer opinions, the Court concludes that Dr. Pisarkiewicz is not qualified to offer an expert opinion as to such.

#### III. Conclusion

Defendants' motion to exclude Dr. Pisarkiewicz's testimony is overruled insofar as it challenges his opinion regarding the definition of the relevant product market as the physician component of diagnostic radiology services provided in a hospital setting, with a relevant product submarket of the provision of such services to hospital inpatients. However, it is sustained, insofar as it [\*37] seeks to exclude Dr. Pisarkiewicz's opinion regarding the relevant geographic market and the alleged anticompetitive effects of Mercy's exclusive contract with DIA, which are identified above.

June 2, 2005

/s/ Walter Herbert Rice

WALTER HERBERT RICE, JUDGE

UNITED STATES DISTRICT COURT

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<sup>9</sup> Locum tenens physicians are essentially temporary physicians who, according to Dr. Pisarkiewicz, are "paid little and are unfamiliar with the staff, the equipment and the hospital procedures" and are paid less than regular physicians (Pisarkiewicz Report at ¶ 52).



## Ramallo Bros. Printing, Inc. v. El Dia, Inc.

United States District Court for the District of Puerto Rico

June 3, 2005, Decided

Civil No. 02-2400 (JAF)

### **Reporter**

392 F. Supp. 2d 118 \*; 2005 U.S. Dist. LEXIS 20367 \*\*; 2005-2 Trade Cas. (CCH) P75,051

RAMALLO BROS. PRINTING, INC., Plaintiffs, v. EL DIA, INC.; EDITORIAL PRIMERA HORA, INC., and ADVANCED GRAPHIC PRINTING, INC., Defendants.

**Subsequent History:** Related proceeding at [Ramallo Bros. Printing, Inc. v. El Dia, Inc., 2006 U.S. Dist. LEXIS 61972 \(D.P.R., Aug. 28, 2006\)](#)

## **Core Terms**

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printing, shoppers, advertising, newspaper, supplements, insertion, pricing, printers, percent, sales, Defendants', monopolization, discounts, predatory, customers, delivery, bundling, summary judgment, editorial, package, anti trust law, market share, competitor, contracts, products, alleges, monopoly power, probability, consumers, profits

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > General Overview

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

Civil Procedure > ... > Summary Judgment > Supporting Materials > Discovery Materials

### **HN1 [] Summary Judgment, Motions for Summary Judgment**

A district court should grant a motion for summary judgment if the pleadings, depositions, answers to the interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#).

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

392 F. Supp. 2d 118, \*118LÁ2005 U.S. Dist. LEXIS 20367, \*\*20367

## **HN2** Summary Judgment, Entitlement as Matter of Law

A factual dispute is "genuine" if it could be resolved in favor of either party, and "material" if it potentially affects the outcome of the case.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Evidence > Burdens of Proof > Allocation

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

Evidence > Burdens of Proof > Initial Burden of Persuasion

Evidence > Burdens of Proof > Ultimate Burden of Persuasion

## **HN3** Entitlement as Matter of Law, Genuine Disputes

On a motion for summary judgment, the moving party carries the burden of establishing that there is no genuine issue as to any material fact; however, the burden may be discharged by showing that there is an absence of evidence to support the nonmoving party's case. The burden has two components: (1) an initial burden of production, which shifts to the nonmoving party if satisfied by the moving party; and (2) an ultimate burden of persuasion, which always remains on the moving party.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

## **HN4** Summary Judgment, Burdens of Proof

On a motion for summary judgment, the non-moving party may not rest upon the mere allegations or denials of the adverse party's pleading but must set forth specific facts showing that there is a genuine issue for trial. Fed. R. Civ. P. 56(e).

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

## **HN5** Summary Judgment, Entitlement as Matter of Law

Summary judgment exists to pierce the boilerplate of the pleadings and assess the proof in order to determine the need for a trial.

Antitrust & Trade Law > Regulated Practices > Monopolies & Monopolization > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

## [\*\*HN6\*\*](#) [] Regulated Practices, Monopolies & Monopolization

Summary judgment may be especially appropriate in an antitrust case because of the chill antitrust litigation can have on legitimate price competition.

Antitrust & Trade Law > Sherman Act > General Overview

## [\*\*HN7\*\*](#) [] Antitrust & Trade Law, Sherman Act

Antitrust claims by competitors aggrieved by their rivals' low prices require critical examination because those low prices benefit consumers and consumer welfare is the primary concern of the antitrust laws. Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals. These injuries to rivals are byproducts of vigorous competition, and the antitrust laws are not balm for rivals' wounds. Thus, a plaintiff faces a stiff burden in any litigation under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > Sherman Act > General Overview

## [\*\*HN8\*\*](#) [] Antitrust & Trade Law, Sherman Act

Courts must be on guard against efforts of plaintiffs to use the antitrust laws to insulate themselves from the impact of competition.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

## [\*\*HN9\*\*](#) [] Summary Judgment, Entitlement as Matter of Law

Summary judgment is particularly appropriate where the non-moving party does not rely on disputed facts but on unreasonable inferences. Creditable inferences must rest on solid, fact-specific footings.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Regulated Industries > Communications > Sherman Act

Antitrust & Trade Law > Regulated Practices > Monopolies & Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > Scope > General Overview

## [\*\*HN10\*\*](#) [] Antitrust & Trade Law, Sherman Act

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To demonstrate attempted monopolization under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), a plaintiff must generally show: (1) the defendant has engaged in predatory or anticompetitive conduct with (2) a specific intent to monopolize and (3) a dangerous probability of achieving monopoly power.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### [\*\*HN11\*\*](#) [ ] **Monopolies & Monopolization, Attempts to Monopolize**

A dangerous probability of success in the relevant market requires evidence that the defendant had sufficient market power to have been reasonably able to create a monopoly. Thus, a colorable claim for attempted monopolization under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), must include evidence of the market power of the defendants and, therefore, must, like claims under [§ 1](#) of the Sherman Act, [15 U.S.C.S. § 1](#), include facts defining the relevant market.

Antitrust & Trade Law > Sherman Act > Scope > Monopolization Offenses

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > Scope > General Overview

#### [\*\*HN12\*\*](#) [ ] **Scope, Monopolization Offenses**

[Section 2](#) of the Sherman Act forbids any monopoly, attempt to monopolize, or combination or conspiracy to monopolize. [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

#### [\*\*HN13\*\*](#) [ ] **Monopolies & Monopolization, Attempts to Monopolize**

Any analysis of a dangerous probability of achieving monopoly power ordinarily includes an analysis of a defendant's share of a properly defined relevant market. Proof of a defendant's high market share not an inflexible requirement, but courts should give weight to the traditional requirement and require exceptional circumstances before straying from it.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### [\*\*HN14\*\*](#) [ ] **Monopolies & Monopolization, Attempts to Monopolize**

A market share of less than 50 percent does not support a finding of dangerous probability of achieving a monopoly.

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > ... > Market Definition > Relevant Market > Geographic Market Definition

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Evidence > Burdens of Proof > General Overview

### **HN15** [blue icon] Sherman Act, Claims

As part of the dangerous probability analysis, the plaintiff has the burden to demonstrate a properly-defined relevant product and geographic market. Failure to prove the relevant market dooms a claim under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Antitrust & Trade Law > ... > Market Definition > Relevant Market > Geographic Market Definition

### **HN16** [blue icon] Monopolies & Monopolization, Attempts to Monopolize

A plaintiff has the burden to prove each element of an attempted monopolization claim, or summary judgment is appropriate.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

### **HN17** [blue icon] Summary Judgment, Entitlement as Matter of Law

Summary judgment is warranted by any fatal factual deficiency in the non-movant's case.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Healthcare Law > Business Administration & Organization > Covenants not to Compete > General Overview

### **HN18** [blue icon] Price Fixing & Restraints of Trade, Tying Arrangements

"Package" sales are widespread and ordinarily lawful. Buyers often find package sales attractive, and a seller's decision to offer such packages can merely be an attempt to compete effectively--conduct that is entirely consistent with the Sherman Act.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [HN19](#) [] Price Fixing & Restraints of Trade, Tying Arrangements

It is undisputed that competition is enhanced when a firm is able to offer various marketing options, including bundling of support and maintenance service with the sale of equipment. Nor do such actions run afoul of the antitrust laws.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [HN20](#) [] Price Fixing & Restraints of Trade, Tying Arrangements

Tying is not automatically unlawful under the antitrust laws.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [HN21](#) [] Price Fixing & Restraints of Trade, Tying Arrangements

To prove a per-se tying violation, a plaintiff must prove: (1) the tying and tied goods are two separate products; (2) the defendant affords consumers no choice but to purchase the tied product from it as a condition of obtaining the tying product; (3) the defendant has sufficient market power in the tying product market to distort consumers' choices with respect to the tied product; and (4) the tying arrangement forecloses a substantial volume of commerce.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [HN22](#) [] Price Fixing & Restraints of Trade, Tying Arrangements

To establish coercion, a plaintiff must demonstrate that a defendant's pricing structure forces the buyer into the purchase of a tied product that the buyer either did not want at all or might have preferred to purchase elsewhere on different terms. The element of coercion, however, cannot be satisfied by mere discounts or other forms of package sales unless the combined purchase is the only economically-viable alternative.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [HN23](#) [] Price Fixing & Restraints of Trade, Tying Arrangements

Products are not tied unless a package is the only viable economic option and a separate purchase is prohibitively expensive.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

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## [HN24](#) Price Fixing & Restraints of Trade, Tying Arrangements

A tying claim must fail absent any proof of anti-competitive effects in the market for the tied product.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [HN25](#) Price Fixing & Restraints of Trade, Tying Arrangements

Two products exist for tying purposes only where there is substantial consumer demand for separate products. The answer to the question whether one or two products are involved turns not on the functional relation between them but rather on the character of the demand for the two items.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [HN26](#) Price Fixing & Restraints of Trade, Tying Arrangements

The absence of a coerced purchase defeats any possibility of an unlawful tying arrangement.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [HN27](#) Price Fixing & Restraints of Trade, Tying Arrangements

The essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all or might have preferred to purchase elsewhere on different terms.

Constitutional Law > ... > Freedom of Speech > Free Press > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

## [HN28](#) Freedom of Speech, Free Press

Would-be advertisers have no right to compel a newspaper to accept their advertisements, let alone editorial material. An advertiser's right to free speech does not give it the right to make use of a newspaper's printing presses and distribution systems without the newspaper's consent.

Constitutional Law > ... > Freedom of Speech > Free Press > General Overview

## [HN29](#) Freedom of Speech, Free Press

A newspaper's right to control editorial content extends to how editorial materials are prepared. The government is prohibited from imposing a penalty in terms of the cost in printing and composing time and material and in taking up space that could be devoted to other material the newspaper may have preferred to print.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [\*\*HN30\*\*](#) [L] **Price Fixing & Restraints of Trade, Tying Arrangements**

Although few cases have addressed bundled pricing as a potential antitrust violation, one requirement is clear: The challenged prices must have the effect of excluding a single-product competitor.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

### [\*\*HN31\*\*](#) [L] **Price Fixing & Restraints of Trade, Tying Arrangements**

In determining whether bundled pricing constitutes an antitrust violation, the fact that the plaintiff is profitable is highly significant. Only price cutting that threatens equally or more efficient firms is condemned under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#). The plaintiff must prove that the defendant's pricing makes it unprofitable for the plaintiff to continue to produce.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

### [\*\*HN32\*\*](#) [L] **Actual Monopolization, Anticompetitive & Predatory Practices**

An attempted monopolization plaintiff basing its claims on predatory pricing must establish two prerequisites to recovery. First, the prices complained of must be below an appropriate measure of the defendant's costs. Second, recoupment must be probable; the alleged predator must have the ability to eliminate its competition and then recover its losses through future high prices.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

### [\*\*HN33\*\*](#) [L] **Actual Monopolization, Anticompetitive & Predatory Practices**

Although the United States Supreme Court has not specified the appropriate measure of cost in a predatory pricing case, the generally accepted standard in the United States Court of Appeals for the First Circuit and most other circuits is whether a seller's prices exceed its incremental (or marginal) cost: Ordinarily the measure of a predatory price is price below incremental cost, that is to say, the addition to total cost (to the firm) of producing and selling additional output would exceed the return from selling that additional output.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

### [\*\*HN34\*\*](#) [L] **Actual Monopolization, Anticompetitive & Predatory Practices**

Incremental or marginal cost is difficult to measure. The United States Court of Appeals for the First Circuit and most other circuits, therefore, rely on average variable cost (those costs that change as output changes) as an approximation of incremental cost. In the First Circuit and most others, variable cost is the normal test of predation.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### **HN35** [+] **Actual Monopolization, Anticompetitive & Predatory Practices**

Because the antitrust laws seek to promote vigorous price competition resulting in low prices, courts must be mindful that low prices are a positive aspect of a competitive marketplace and are encouraged by the antitrust laws. Courts, therefore, carefully scrutinize attempted monopolization claims based on predatory pricing. The requisites for proving predatory pricing are demanding because the conditions under which it is plausible are not common and because it can easily be confused with merely low prices which benefit consumers.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

#### **HN36** [+] **Actual Monopolization, Anticompetitive & Predatory Practices**

Claims of below-cost pricing on a small percentage of a firm's sales are insufficient to raise a triable issue of predatory pricing.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

#### **HN37** [+] **Actual Monopolization, Anticompetitive & Predatory Practices**

Predation claims cannot be based on occasional instances of allegedly predatory pricing because they are not likely to drive rivals from the market and to permit the predator to raise prices and profits subsequently. A predatory pricing plaintiff can prevail only by adducing evidence suggesting that a defendant's overall price structure was predatory, not that a small minority of sales were below average variable cost.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

#### **HN38** [+] **Actual Monopolization, Anticompetitive & Predatory Practices**

Promotional discounts by new entrants are not regarded as predatory.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

#### **HN39** [+] **Actual Monopolization, Anticompetitive & Predatory Practices**

Unless continued over a long period of time, in which case it is no longer promotional, promotional pricing by new entrants is no threat to competition. Under these circumstances, courts find promotional prices lawful, no matter what that price-cost relationship.

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Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

Tax Law > ... > C Corporations > Insurance Companies > Deductions

Tax Law > ... > Losses > Net Operating Losses > General Overview

#### **HN40** [↓] **Actual Monopolization, Anticompetitive & Predatory Practices**

Sales below average total cost (in other words, whether a firm has a bottom-line net loss) are irrelevant to predatory pricing analysis in the United States Court of Appeals for the First Circuit and the majority of other circuits that have adopted the average variable cost standard.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### **HN41** [↓] **Monopolies & Monopolization, Attempts to Monopolize**

A final requirement of an attempted monopolization claim is evidence that the defendants had a specific intent to destroy competition or build monopoly. Evidence of a mere desire to increase market share or win customers from a competitor does not suffice.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### **HN42** [↓] **Monopolies & Monopolization, Attempts to Monopolize**

The necessary intent to monopolize is something more than an attempt to compete vigorously.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > Predatory Hiring & Price Squeezes

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

#### **HN43** [↓] **Anticompetitive & Predatory Practices, Predatory Hiring & Price Squeezes**

Predatory hiring cases must be proved by a showing that the hiring was made with such predatory intent, i.e., to harm the competition without helping the defendant, or by showing a clear nonuse in fact.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > Sherman Act > Scope > Monopolization Offenses

#### **HN44** [↓] **Monopolies & Monopolization, Actual Monopolization**

The offense of monopolization under § 2 of the Sherman Act, 15 U.S.C.S. § 2, requires proof that the defendants: (1) have acquired a monopoly in the relevant market; and (2) have willfully acquired or maintained that monopoly power.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

#### [HN45](#) [+] **Private Actions, Standing**

A private antitrust plaintiff must show antitrust injury or injury of the type the antitrust laws were intended to prevent.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

#### [HN46](#) [+] **Private Actions, Standing**

Competitors and consumers in the market where trade is allegedly restrained are presumptively the proper plaintiffs to allege antitrust injury.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

#### [HN47](#) [+] **Regulated Practices, Market Definition**

Courts are reluctant to confine markets for delivery of particular types of advertising to a single method, given the variety of alternatives ordinarily available.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

#### [HN48](#) [+] **Public Enforcement, State Civil Actions**

Puerto Rico's antitrust laws mirror the federal antitrust statutes.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### [HN49](#) [+] **Regulated Practices, Trade Practices & Unfair Competition**

The elements of a claim for unfair trade practices under *31 P.R. Laws Ann. § 5141* (1991 & Supp. 2001) are: (1) proof of the reality of the damage suffered; (2) a causal relationship between such damage and the action or omission of another person; and (3) said act or omission is negligent or wrongful.

Torts > ... > Business Relationships > Intentional Interference > Elements

Torts > Business Torts > Commercial Interference > General Overview

Torts > ... > Commercial Interference > Business Relationships > General Overview

Torts > ... > Commercial Interference > Contracts > General Overview

Torts > ... > Contracts > Intentional Interference > Elements

## **HN50**[ **Intentional Interference, Elements**

To establish a claim for tortious interference with a contractual relationship, a plaintiff must show: (1) the existence of a contract; (2) that the interfering party acted with intent and knowledge of the existence of the contract; (3) that the plaintiff suffered damages; and (4) that there exists a causal link between the injury and the interfering party's actions.

Torts > ... > Commercial Interference > Contracts > General Overview

## **HN51**[ **Commercial Interference, Contracts**

When a contract that is allegedly interfered with is terminable at will, the privilege of competition has been recognized. In such a case, there is no contract right to have the relation continued but only an expectancy, which is not actionable.

**Counsel:** **[\*\*1]** For Ramallo Brothers Printing, Inc., Plaintiff: Allan Kanner, PHV Conlee S. Whiteley, Allan Kanner and Associates, P.C., New Orleans, LA; Camilo K. Salas, Salas & Co. L.C., New Orleans, LA; John F. Nevares, John F. Nevares & Assoc. PSC, San Juan, PR; PHV Daniel E. Buras, Jr., Stewart E. Niles, Jr., New Orleans, LA; PHV Lawrence J. Centola, Niles, Salas Bourque & Fontana, L.C., New Orleans, LA.

For El Dia, Inc., Editorial Primera Hora, Inc., Advanced Graphic Printing, Inc., Defendants: PHV Bruce W. Sanford, PHV Lee H. Simowitz, PHV Mark A. Cymrot, PHV Robert D. Lystad, PHV Ronald F. Wick, PHV Andrew J. Durkovic, PHV Elizabeth A. Scully, Baker & Hostetler LLP, Washington, DC; Salvador Antonetti-Zequeira, Ricardo F. Casellas, Roberto A. Camara-Fuertes, Fiddler, Gonzalez & Rodriguez, San Juan, PR.

For Sessions, Fishman & Nathan, LLP, Interested Party: Jack M. Alltmont, Sessions, Fishman & Nathan, LLP, New Orleans, LA.

For All Distribution, Inc., Interested Party: Gerardo Pavia, Pavia & Diaz Garcia, San Juan, PR.

For El Dia, Inc., Editorial Primera Hora, Inc., Advanced Graphic Printing, Inc., Counter Claimants: PHV Bruce W. Sanford, PHV Lee H. Simowitz, PHV Mark A. Cymrot, PHV Robert D. Lystad, PHV Ronald F. Wick, PHV Andrew J. Durkovic, PHV Elizabeth A. Scully, Baker **[\*\*2]** & Hostetler LLP, Washington, DC; Salvador Antonetti-Zequeira, Ricardo F. Casellas, Roberto A. Camara-Fuertes, Fiddler, Gonzalez & Rodriguez, San Juan, PR.

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**Judges:** JOSE ANTONIO FUSTE, Chief U. S. District Judge.

**Opinion by:** JOSE ANTONIO FUSTE

## **Opinion**

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### **[\*123] OPINION AND ORDER**

Plaintiff Ramallo Bros. Printing, Inc. ("Plaintiff") brings the present action against Defendants El Dia, Inc. ("Defendant El Dia"); Editorial Primera Hora, Inc. ("Defendant Editorial Primera Hora"); and Advanced Graphic Printing, Inc. ("Defendant AGP"); alleging violations of Sections 4 and 16 of the Clayton Act, [15 U.S.C. §§ 15](#) and [26 \(1997 & Supp. I 2003\)](#); Sections 1 and 2 of the Sherman Act, [15 U.S.C. §§ 1](#) and [2, \(1997 & Supp. I 2003\)](#); and

various causes of action under state law, including the antitrust laws of the Commonwealth of Puerto Rico, *10 P.R. LAWS ANN.* §§ 258, 260 and 268 (1997 & Supp. 2001). Docket Document Nos. 1, 13, 40. Plaintiff seeks injunctive and monetary relief. *Id.*

Defendants **[\*\*3]** move for summary judgment. Docket Document Nos. 156, 189, 213. Plaintiff opposes the motion. Docket Document Nos. 176, 196.

## I.

### **Factual and Procedural Synopsis**

We derive the facts and allegations from our February 6, 2004, opinion and order, and from the parties' pleadings and statements of material fact. Docket Document Nos. 1, 12, 13, 38, 40, 59, 156, 176, 188, 196.

Plaintiff is a corporation organized and existing under the laws of Puerto Rico, with its principal place of business in Puerto Rico. It is a commercial printer whose business consists of, *inter alia*, the printing of inserts ("shoppers") advertising the sale of goods, which are distributed by inserting them in newspapers of general circulation in Puerto Rico, as well as by other means. Shoppers are used by major retailers, such as supermarkets, drug stores, toy stores, and furniture stores as advertising vehicles for products offered for sale. Shoppers usually range in size from four to twelve pages, and contain color pictures of individual products, together with prices and other product information.

Plaintiff is part of a group of businesses that also includes a commercial forms printer, **[\*\*4]** a software integration business, a paper company, and a boat distributor, as well as a three-building industrial complex that includes leased space for commercial tenants and houses Plaintiff's printing facilities, which are located in what Plaintiff describes on its website as a "world-class manufacturing environment."

Defendant *El Dia* is a corporation organized and existing under the laws of Puerto Rico with its principal place of business in Puerto Rico. Defendant *El Dia* is the owner and publisher of *El Nuevo Dia*, the largest newspaper in Puerto Rico based on paid circulation and revenues. The business **[\*124]** of the newspaper includes, *inter alia*, the distribution of shoppers printed by Defendant *El Dia*, Defendant AGP, and other commercial printers, including Plaintiff. Defendant *El Dia* is also part of a group of companies that includes Defendant Editorial Primera Hora and Defendant AGP, as well as other related businesses.

Defendant Editorial Primera Hora is a corporation organized and existing under the laws of Puerto Rico with its principal place of business in Puerto Rico. Defendant Editorial Primera Hora owns and publishes *Primera Hora*, a daily Puerto Rico newspaper, which **[\*\*5]** is a new entrant into the daily newspaper market. *Primera Hora* is printed by Defendant *El Dia*. Defendant Editorial Primera Hora's business also includes, *inter alia*, the distribution of a few shoppers.

Defendant AGP is a corporation organized and existing under the laws of Puerto Rico with its principal place of business in Puerto Rico. Defendant AGP is a commercial printing company that was formed by Defendant *El Dia* in 1997. Defendant AGP's business, like that of Plaintiff, includes, *inter alia*, the printing of shoppers.

#### **A. Newspaper Advertising in Puerto Rico**

*El Nuevo Dia* and *Primera Hora* are two of four daily newspapers in Puerto Rico, all of which depend primarily on advertising for their revenues. Most retail newspaper advertising takes one of two forms: (1) display advertising that appears within the body of the newspaper, commonly referred to as "run of press" or ROP advertising, and (2) shoppers and other pre-printed inserts containing various types of advertising.

One vehicle for ROP advertising in *El Nuevo Dia* and *El Vocero*, Puerto Rico's two largest newspapers, is commercial supplements, sections of the newspaper usually containing **[\*\*6]** both editorial content and display

advertising by multiple advertisers. *El Nuevo Dia* publishes approximately 190 commercial supplements annually, including supplements published to commemorate Mother's Day, Christmas, and Secretaries' Week, or based on themes such as autos, weddings, and babies. *El Nuevo Dia* produces and prints commercial supplements on newsprint using the newspapers' staffs and presses. According to its publisher, *El Vocero* follows the same practice for producing commercial supplements.

A small portion of commercial supplements, called "corporate supplements," focus on a featured business and usually celebrate that business' anniversary or some other special event. Corporate supplements constitute a negligible portion of the advertising and commercial printing business in Puerto Rico. From 1999 to 2003, *El Nuevo Dia* had about 5,000 commercial inserts, but only 134 corporate supplements. Corporate supplements typically contain stories about a featured company and serve as a vehicle for the newspaper to sell advertising to sponsors, usually the featured company's vendors. Like commercial supplements, corporate supplements are produced entirely in-house. **[\*\*7]** *El Nuevo Dia* has designated Creative Minds, a former *El Nuevo Dia* staff unit that is now a division of AGP, as its exclusive agent for producing corporate supplements, and it will only insert corporate supplements produced by Creative Minds. Creative Minds performs all the functions needed to produce the supplement, including preparation of editorial content and artwork, sales of advertising, coordination of the printing and insertion in the newspaper. Defendants' stated reasons for the policy of using only Creative Minds to produce corporate supplements are the need to maintain editorial **[\*125]** integrity, to ensure the content is accurate and comports with its style and content policies, and to take advantage of the cost savings.

Shoppers and corporate supplements are printed most frequently on glossy paper rather than newsprint, a process that requires the services of a commercial printer with a web press -- such as Plaintiff and Defendant AGP -- because glossy paper products cannot be printed on newspaper presses. Plaintiff complains that it printed *El Nuevo Dia*'s corporate supplements prior to Defendant AGP's formation, but *El Nuevo Dia* will now only use Defendant AGP **[\*\*8]** to print corporate supplements.

With four daily newspapers, three of which are separately owned, Puerto Rico has one of the most competitive newspaper markets in the United States. Only six other U.S. cities have more than two daily newspapers. Daily newspapers also compete with many other methods available for retailers to deliver their advertising messages to consumers. Plaintiff's vice-president for sales and many of the advertiser-deponents identified the media competing with daily newspapers as television, radio, magazines, direct mail, outdoor advertising, catalogues, coupons, the Internet, and the many regional newspapers in Puerto Rico. Shoppers are only one option for advertisers to deliver their message.

Those retailers that include shoppers in their advertising mix also use a variety of competing delivery channels to distribute their shoppers. While newspapers are the most common delivery means, some advertisers also use door-to-door delivery, direct mail, and free distribution in stores, malls, and other places.

## **B. Competition Between Plaintiff and Defendant AGP**

In 1995, Plaintiff acquired a commercial printer in Puerto Rico that competed directly with **[\*\*9]** Plaintiff in the printing of shoppers, effectively leaving Plaintiff as the only high-volume printer of shoppers located in Puerto Rico. According to Plaintiff's economics expert, Dr. Franklin M. Fisher, Plaintiff printed in excess of 80 percent of the shoppers produced in Puerto Rico before Defendant AGP entered the market.

In the early 1990s, *El Dia* was a significant purchaser of commercial printing services for the printing of glossy magazines and other sections of its newspaper. *El Dia* also printed some advertising material, including shoppers, on newsprint using the same presses it used to print the newspaper, but *El Dia* did not have the presses necessary to print glossy paper products. *El Dia* considered entering the printing business as early as 1992 because it witnessed an exodus of printing business to off-island printers. Believing that upward of 40 percent of commercial printing for the Puerto Rican market was being performed offshore, *El Dia* decided to create AGP in 1997 to capture the offshore business and provide more competition within Puerto Rico.

Since Defendant AGP's formation, customers seeking lower prices and better service have moved regularly among printers. [\*\*10] It has not been uncommon for advertisers to move their shopper business from Defendant AGP to Plaintiff, from Plaintiff to Defendant AGP, or back and forth on multiple occasions or to printers in other locations. A number of shoppers distributed in Puerto Rico are printed by printers located in the mainland United States and in the Dominican Republic. From 1999 to 2003, approximately 20 percent of [\*126] the shoppers inserted into *El Nuevo Dia* were printed by companies located outside Puerto Rico.

Within two years of its formation, Defendant AGP was printing 31 percent of the shoppers inserted in *El Nuevo Dia*. Its percentage rose to 36 percent in 2000 but has remained largely unchanged thereafter.<sup>1</sup> Plaintiff's share of inserts in *El Nuevo Dia* moved in a range between a low of 37 percent in 2000 and 2003 to a high of 46 percent in 2001. The number of shoppers Plaintiff printed for insertion in *El Nuevo Dia* increased by 63 percent between 1999 and 2003 and its revenues from all shoppers increased by 23 percent.

[\*\*11] Even with the new competition from Defendant AGP, Plaintiff continues to advertise itself on its website as "the number one commercial printer in Puerto Rico and the Caribbean." *Printing Impressions*, which Plaintiff's website describes as "America's most influential journal for the printing and allied industries," ranks Plaintiff as 85th in 2004 among the top 400 printing companies in the United States -- up from 166th in the 2001 rankings. Plaintiff's audited financial statements show, and its chief financial officer testified, that Plaintiff has been consistently profitable each year from 1998 through 2003, both company-wide and for printing shoppers. Plaintiff's profits from shoppers are substantially larger than industry averages, according to Plaintiff's printing expert, who testified that Ramallo's profits represented an average of 12 percent of shopper sales, compared to an industry-wide average for newspaper inserts of 5.4 percent. Plaintiff's chief financial officer testified that Plaintiff's net sales and stockholders' equity also were "considerably greater" in 2003 than they were in 1996, the year before Defendant AGP was formed.

Plaintiff remains the largest printer [\*\*12] of shoppers in Puerto Rico based on revenue. In 2003, Plaintiff reported approximately \$ 18 Million in revenue from printing shoppers, compared to approximately \$ 11.6 Million for Defendant AGP. Plaintiff today prints more shoppers than AGP and more than it did before Defendant AGP was formed.

Plaintiff's performance contrasts with Defendant AGP's struggles as a new entrant. While Defendant AGP was cash-flow positive prior to this lawsuit, it has only once shown a net profit. In February 2005, Defendant AGP laid off 20 percent of its work force and instituted other operational cost cuts in an attempt to improve its financial performance.

### **C. Defendants' Sales Practices**

Like other newspapers, both *El Nuevo Dia* and *Primera Hora* give discounts to advertisers based on the volume of advertising they commit to the newspapers. Although newspapers publish rate cards showing rates for ROP advertising and for insertion of shoppers, advertisers testified that the rate card frequently serves as a starting point for negotiations between the newspaper and the advertiser. Plaintiff complains that sometimes the discounts for insertion services exceed 50 percent off rate card, [\*\*13] but Plaintiff has not shown that these discounts are unusual, particularly for the large advertisers using shoppers in Puerto Rico, such as Wal-Mart, Pueblo, Walgreens, Pitusa, Sears, and J.C. Penney. Plaintiff admits that even with highly-discounted rates, Defendant El Dia makes a substantial profit from the insertion of shoppers.

*El Nuevo Dia* and *Primera Hora* insert shoppers without regard to the identity or location of the commercial printer that [\*127] prints them. There is no evidence that either newspaper has ever refused to insert a shopper because

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<sup>1</sup> Plaintiff has not offered market share information. Defendants have submitted figures showing the number of shoppers inserted in *El Nuevo Dia*. These figures do not include shoppers distributed in other newspapers or by other means and, therefore, do not constitute complete market shares.

it was printed by Plaintiff, or by any other commercial printer. Many of *El Nuevo Dia*'s largest shopper insertion clients print shoppers with Plaintiff. Most advertisers that print with Defendant AGP negotiate with Defendant AGP separately from the newspapers. Defendants, however, have two programs in which an advertiser can receive a discount or other benefit from *El Nuevo Dia* or *Primera Hora* based, in part, on the advertiser's use of AGP: Group contracts and other package discount arrangements, and a loyalty points program called "Alcance." Plaintiff's complaint focuses on these two programs. The programs are not mandatory; **[\*\*14]** they are provided as an option to customers.

Defendants have entered into five group contracts with some advertisers that include prices for printing with Defendant AGP, as well as prices for shopper insertion or ROP advertising in *El Nuevo Dia* or *Primera Hora*. These contracts contain incentives for the advertiser to print with Defendant AGP, such as a lower price for insertion or 'ROP advertising if the advertiser provides a minimum volume of printing business to Defendant AGP. Defendants have also offered package pricing for printing, insert and ROP advertising to some advertisers, but Plaintiff has not submitted evidence quantifying these arrangements. Printing and insertion services are, however, always separately available from Defendants.

Defendants' "Alcance" program allows customers to accumulate points by purchasing ROP advertising, insertion, commercial printing, and other services from Defendants and other affiliated companies. These points may be redeemed for services, such as advertisements in *El Nuevo Dia* or *Primera Hora*. "Alcance" points may not be used, however, to purchase printing services from AGP. Some large advertisers do not receive "Alcance" **[\*\*15]** points for their purchases because they negotiate for other price concessions.

#### **D. Plaintiff's Allegations**

Plaintiff filed the present complaint on September 16, 2002, alleging the following seven causes of **[\*128]** action: (1) conspiracy to unreasonably lessen and eliminate competition in the markets for the printing and delivery of shoppers and corporate supplements, in violation of [Section 1 of the Sherman Act](#); (2) unreasonable restraint of trade in the printing and delivery markets, in violation of [Section 1 of the Sherman Act](#); (3) attempt to monopolize the printing market, in violation of [Section 2 of the Sherman Act](#); (4) conspiracy to monopolize the printing market, in violation of [Section 2 of the Sherman Act](#); (5) monopolization and maintenance of monopoly power in the delivery market, in violation of [Section 2 of the Sherman Act](#); (6) conspiracy to eliminate or injure competitors by misappropriating trade secrets and inducing competitors' employees to breach their employment contracts; and (7) violations of the antitrust laws of Puerto Rico. [Docket Document No. 1](#). On November 5, 2002, Plaintiff filed an amended complaint alleging additional counts for violations of **[\*\*16]** Puerto Rico's unfair trade practices law (count 8) and intentional interference with prospective economic advantages and business and contractual relationships under Puerto Rico law (count 9). [Docket Document No. 13](#).

On November 13, 2002, Defendants moved to dismiss all counts 1 through 7, with the exception of count 3 as it pertained to corporate supplements, for failure to state a claim. [Docket Document No. 21](#). Defendants also filed a counterclaim, alleging the following five causes of action: (1) abuse of process under Puerto Rico law; (2) commercial disparagement under Puerto Rico law; (3) violation of Section 43(a) of the Lanham Act, [15 U.S.C. § 1125\(a\)](#); (4) tortious interference with contract under Puerto Rico law; and (5) violations of Article 1802 of the Civil Code of Puerto Rico, *31 P.R. LAWS ANN. § 5141*. [Docket Document No. 12](#). On November 21, 2002, Defendants filed a supplemental motion to dismiss counts 8 and 9 for failure to state a claim. [Docket Document No. 25](#). Plaintiffs filed a second amended complaint on December 31, 2002. [Docket Document No. 40](#).

On February 6, 2004, we granted Defendants' motion **[\*\*17]** to dismiss counts 1, 4, and 6, finding that count 6 was time-barred and that Plaintiff's conspiracy claims failed because Defendants were commonly owned and controlled and, therefore, were legally incapable of conspiring with each other. We also dismissed count 8 insofar as it asserted claims under *10 P.R. LAWS ANN. § 259 (1997 & Supp. 2001)*, and count 9 insofar as it asserted a claim for interference with prospective economic relationships. [Docket Document No. 59](#).

Plaintiff's surviving claims are counts 2,<sup>2</sup> 3, 5, 7, 8 (insofar as it asserts claims under Article 1802 of the Puerto Rico Civil Code, 31 P.R. LAWS ANN. § 5141 (1991 & Supp. 2001)), and 9 (insofar as it asserts a claim for tortious interference with business and contractual relationships). *Id.*

[\*\*18] After exhaustive discovery that lasted more than a year, on March 1, 2005, Defendants moved for summary judgment. Docket Document No. 156. Plaintiff opposed the motion on April 4, 2005. Docket Document No. 176.

On May 13, 2005, Defendants voluntarily withdrew counts 2, 3, and 4 of the counterclaim. Docket Document No. 204. Defendants continue to maintain counts 1 and 5 of the counterclaim based on allegations that Plaintiff has used the lawsuit improperly to advance a plan to secure and maintain exclusive control over the commercial printing business in Puerto Rico. Plaintiff did not timely move for summary judgment against the counterclaim.

## II.

### Summary Judgment Motion Standard

The standard for summary judgment is straightforward and well-established. [HN1](#) A district court should grant a motion for summary judgment "if the pleadings, depositions, and answers to the interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." [Fed. R. Civ. P. 56\(c\)](#). [HN2](#) A factual dispute is [\*\*19] "genuine" if it could be resolved in favor of either party, and "material" if it potentially affects the outcome of the case. [Calero-Cerezo v. United States DOJ](#), 355 F.3d 6, 19 (1st Cir. 2004).

[HN3](#) The moving party carries the burden of establishing that there is no genuine issue as to any material fact; however, the burden "may be discharged by 'showing' . . . that there is an absence of evidence to [\*129] support the nonmoving party's case." [Celotex Corp. v. Catrett](#), 477 U.S. 317, 325, 331, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986). The burden has two components: (1) an initial burden of production, which shifts to the nonmoving party if satisfied by the moving party; and (2) an ultimate burden of persuasion, which always remains on the moving party. See *id. at 331*.

[HN4](#) The non-moving party "may not rest upon the mere allegations or denials of the adverse party's pleading, but . . . must set forth specific facts showing that there is a genuine issue for trial." [Fed. R. Civ. P. 56\(e\)](#). [HN5](#) Summary judgment exists "to pierce the boilerplate of the pleadings and assess the proof in order to determine the need for a trial." [Euromodas, Inc. v. Zanella](#), 368 F.3d 11, 17 (1st Cir. 2004) [\*\*20] (citing [Wynne v. Tufts Univ. Sch. of Med.](#), 976 F.2d 791, 794 (1st Cir. 1992)).

"The Supreme Court has emphasized . . . that [HN6](#) summary judgment may be especially appropriate in an antitrust case because of the chill antitrust litigation can have on legitimate price competition." [Indiana Grocery, Inc. v. Super Valu Stores, Inc.](#), 864 F.2d 1409, 1412 (7th Cir. 1989) (citing [Matsushita Elec. Indus. Co. v. Zenith Radio Corp.](#), 475 U.S. 574, 594-95, 89 L. Ed. 2d 538, 106 S. Ct. 1348 (1986)). See also [PepsiCo, Inc. v. Coca-Cola Co.](#), 315 F.3d 101, 104 (2d Cir. 2002) (summary judgment often appropriate in antitrust cases "because of the concern that protracted litigation will chill pro-competitive market forces"). [HN7](#) Antitrust claims by competitors aggrieved by their rivals' low prices require critical examination, because those low prices benefit consumers, and consumer welfare is the primary concern of the antitrust laws. "Competition is a ruthless process. A firm that reduces cost and expands sales injures rivals. . . . These injuries to rivals are byproducts of vigorous competition, and the antitrust

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<sup>2</sup> Defendants contend that count 2 was necessarily dismissed as a result of our ruling on February 6, 2004, because our ruling dismissed all conspiracy claims and count 2 alleges concerted action under [Section 1 of the Sherman Act](#). Plaintiff contends that count 2 is a claim for an unlawful tying arrangement under [Section 1 of the Sherman Act](#) and, therefore, the reasoning behind the dismissal of Plaintiff's other conspiracy counts does not apply. Because our discussion herein of Plaintiff's tying claims under [Section 2 of the Sherman Act](#) applies equally to a tying claim asserted under [Section 1](#), we will treat count 2 as a surviving claim.

laws are not balm for rivals' wounds. . . Thus the plaintiff [\*\*21] faces a stiff burden in any [Sherman Act] § 2 litigation." *Ball Mem'l Hosp., Inc. v. Mutual Hosp. Ins., Inc.*, 784 F.2d 1325, 1338 (7th Cir. 1986). HN8[] "Courts must be on guard against efforts of plaintiffs to use the antitrust laws to insulate themselves from the impact of competition." *Buffalo Courier-Express, Inc. v. Buffalo Evening News, Inc.*, 601 F.2d 48, 55 (2d Cir. 1979). HN9[] Summary judgment is particularly appropriate where the non-moving party does not rely on disputed facts, but on unreasonable inferences. "Creditable inferences must rest on solid, fact-specific footings." *Quaker State Oil Refining Corp. v. Garrity Oil Co.*, 884 F.2d 1510, 1516 (1st Cir. 1989).

### III.

## Analysis

### A. Attempted Monopolization

Plaintiff alleges that Defendants have attempted to monopolize the market for printing shoppers and corporate supplements in Puerto Rico by (1) unlawfully tying the printing of shoppers and corporate supplements to ROP advertising and insertion in *El Nuevo Dia* and *Primera Hora*, (2) unlawfully "bundling" printing services with ROP advertising and insertion in Defendants' newspapers, and (3) [\*\*22] predatorily pricing Defendants' printing and insertion services. Docket Document No. 1. HN10[] To demonstrate attempted monopolization under Section 2 of the Sherman Act,<sup>3</sup> a plaintiff must generally show "(1) that the defendant has engaged in predatory or anticompetitive conduct with (2) a [\*130] specific intent to monopolize and (3) a dangerous probability of achieving monopoly power." *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456, 122 L. Ed. 2d 247, 113 S. Ct. 884 (1993). HN11[] "[A] dangerous probability of success in the relevant market . . . requires evidence that the defendant had sufficient market power to have been reasonably able to create a monopoly.' . . . A colorable claim, thus, must include evidence of the market power of the defendants and, therefore, must, like Section 1 claims, include facts defining the relevant market." *R.W. Int'l, Inc. v. Borden Interamerica, Inc.*, 673 F. Supp. 654, 657 (D.P.R. 1987) (Fuste, J.) (internal quotes omitted).

#### **[\*\*23] 1. Dangerous Probability of Achieving Monopoly Power**

Defendants contend that Plaintiff has failed to show that Defendants have a dangerous probability of achieving monopoly power in the market for printing shoppers and corporate supplements in Puerto Rico. Docket Document No. 156. Plaintiff contends that Defendants' practices nearly drove Plaintiff into bankruptcy, and that only a substantial new contract in another line of business enabled Plaintiff to survive. Docket Document No. 176. Plaintiff further contends that Defendants' policy regarding corporate supplements has already foreclosed all corporate supplement business to Plaintiff, and that if Defendants' practices continue, Defendant AGP will drive Plaintiff out of the business of printing shoppers. *Id.* Plaintiff's attempted monopolization theory depends on the allegation that Defendants will drive it out of the shopper printing market and absorb its market share, thereby acquiring monopoly power.

#### **a. Plaintiff's Financial Health**

In support of their motion, Defendants cite overwhelming and undisputed evidence that Plaintiff is healthy and viable and expects to remain so for the foreseeable [\*\*24] future. Docket Document No. 156. Plaintiff has made a net profit from printing shoppers in every year since Defendant AGP was formed. Plaintiff's revenues from printing shoppers grew by more than 20 percent from 1999 to 2003 despite competition from Defendant AGP. Plaintiff's insertions in *El Nuevo Dia*, the newspaper Plaintiff claims is attempting to drive it out of business, increased by 63 percent between 1999 and 2003. Plaintiff has recently gained significant new shopper clients, including Wal-Mart

<sup>3</sup> HN12[] Section 2 of the Sherman Act forbids any monopoly, or attempt to monopolize, or combination or conspiracy to monopolize. 15 U.S.C. § 2.

and J.C. Penney (from AGP) and Walgreens (from mainland U.S. printers). Plaintiff continues to derive more revenue from shoppers (approximately \$ 18 Million in 2003) than Defendant AGP (approximately \$ 11.6 Million).

Plaintiff's actions also reflect a financially and competitively healthy business, not a business on the brink of bankruptcy or exit from the printing market. Plaintiff has expanded and modernized its printing capacity with substantial investments in equipment since Defendant AGP entered the market, including the acquisition of three printing presses. Plaintiff submitted forecasted financial statements to its lender that predict steadily increasing sales and profits [\*\*25] from 2004 through 2008. Plaintiff's chief financial officer and its outside auditor both testified that Plaintiff is a viable, healthy company, and that Plaintiff has made no plans or preparations to file for bankruptcy or discontinue the printing of shoppers. Plaintiff's chief executive officer directly contradicted his own company's case when he testified that he "cannot imagine" a time when Defendant AGP would be the sole printer of shoppers in Puerto Rico.

Plaintiff cites the testimony of its chief financial officer that, but for the addition [\*131] of a new contract in a different line of business (telephone directory printing), Plaintiff *might* have undergone a reorganization that *might* have led to bankruptcy. Given Plaintiff's consistent profitability and position in the market, such speculative and self-serving testimony could not persuade a reasonable finder of fact that Plaintiff was ever on the verge of failure.

Plaintiff also cites an analysis of its publicly-available financial statements performed by Defendant AGP in which Defendant AGP observed that Plaintiff's high-debt level had resulted in a weak cash-flow position. The same document, however, notes a marked improvement [\*\*26] in Plaintiff's profitability, which is consistent with the testimony of Plaintiff's own executives. Moreover, Plaintiff's debt load resulted from its decision to develop a large industrial park project; any resulting negative effect Plaintiff's debt service obligations may have had on its cash flow cannot be attributed to Defendants' actions.

Finally, Plaintiff relies on the opinion of its economics expert, Dr. Franklin M. Fisher, whose report states incorrectly that Plaintiff is unprofitable. When presented with Plaintiff's audited financial statements, Dr. Fisher dismissed Plaintiff's history of consistent profitability, and testified instead that Plaintiff was not earning "economic profits" from shoppers, *i.e.*, that Plaintiff's profits do not represent a sufficient rate of return on its investment to provide Plaintiff's shareholders with an incentive to continue investing in the business. Dr. Fisher, however, did not calculate Plaintiff's "economic profits" for any year, testified that he lacked the information to do so, and has not provided any data to support his opinion. Plaintiff has not submitted any evidence that its profit margin on shoppers has decreased as a result [\*\*27] of competition from Defendant AGP, and Plaintiff's printing expert opined that Plaintiff's profits exceed the industry average. Dr. Fisher's report and testimony regarding Plaintiff's unprofitability is factually incorrect, and his testimony about economic profits is speculative and also inconsistent with the testimony of Plaintiff's printing expert. Dr. Fisher's opinion on this point is, therefore, rejected.

By every measure of financial performance, there is no risk that Plaintiff is about to be "eliminated" from the market, as it alleges. The evidence on which Plaintiff relies, even when construed in the light most favorable to Plaintiff, is unpersuasive and implausible and creates no genuine issue of material fact. Plaintiff's contention that Defendants have a dangerous probability of achieving a monopoly in the printing market fails in the face of abundant and undisputed evidence of Plaintiff's financial health.

#### **b. Plaintiff's Market Strength**

**HN13** [Any analysis of dangerous probability of achieving monopoly power ordinarily includes an analysis of defendant's share of a properly defined relevant market. See, e.g., Springfield Terminal Ry. v. Canadian Pac., Ltd., 133 F.3d 103, 107-08 (1st Cir. 1997)] [\*\*28] (proof of defendant's high market share not "an inflexible requirement," but court should give "weight to the traditional requirement, and require exceptional circumstances before straying from it"). Despite the importance of this factor to the courts, Plaintiff has not undertaken market share calculations and professes ignorance of its own market share. The undisputed evidence submitted by Defendants regarding the printers of shoppers inserted in *El Nuevo Dia* further supports the conclusion that there is no reasonable probability that Defendants will achieve a monopoly in printing shoppers.

[\*132] There is no doubt that the business of printing shoppers has become more competitive since Defendant AGP entered the market. Plaintiff complains that Defendant AGP quickly took about 30 percent of the market. Plaintiff's expert, Dr. Fisher, however, testified that Plaintiff was printing more than 80 percent of the shoppers printed in Puerto Rico before Defendant AGP began competing for the business. The evidence submitted by Defendants shows that Defendants' share of inserts that appeared in *El Nuevo Dia* remained roughly constant from 1999 through 2003, and more than 60 percent of the [\*29] shoppers inserted in *El Nuevo Dia* have been printed by printers other than Defendant AGP, which does not suggest any trend toward monopoly power on the part of Defendants.

Even if offshore printers are excluded from the market as Plaintiff argues, effectively leaving Plaintiff and Defendant AGP as the only participants in the relevant market, Defendants' market share would necessarily remain below 50 percent. Plaintiff's revenues from shoppers exceed Defendant AGP's revenues from shoppers and corporate supplements combined for each year from 1999 through 2003. [HN14](#) [↑] A market share of less than 50 percent does not support a finding of dangerous probability of achieving a monopoly. See, e.g., [\*U.S. Anchor Mfg. v. Rule Indus.\*, 7 F.3d 986, 1001 \(11th Cir. 1993](#)) (no dangerous probability of success as a matter of law because defendant's market share below 50 percent at all relevant times); [\*Indiana Grocery\*, 864 F.2d at 1414-15](#) (50 percent share insufficient where plaintiff conceded that defendant "could never control" market); [\*United States v. Empire Gas Corp.\*, 537 F.2d 296, 305 \(8th Cir. 1976\)](#) (market shares of 50 percent and [\*30] 47 percent insufficient for dangerous probability).

Plaintiff has not articulated any special circumstances that would lead us to forego the traditional reliance on market share analysis. On the contrary, the evidence of Plaintiff's continued financial strength and ability to compete vigorously confirms that Defendants do not have a dangerous probability of achieving monopoly power in the shopper printing market.

Plaintiff alleges that Defendant AGP will gain a market share in excess of 50 percent by eliminating Plaintiff and absorbing its market share. Plaintiff's financial strength refutes this suggestion. The First Circuit has also rejected this theory in [\*Springfield Terminal\*](#), where the plaintiff, a much smaller and more precariously-positioned competitor than Plaintiff here, asked the court to assume that the defendant would force it into bankruptcy and acquire it:

We would find attempt claims presumptively implausible if the challenged conduct has been in place for at least two years and the remaining market remains robustly competitive as evidenced by ongoing entry, profitability of rivals, and stability of their aggregate market share.

[133 F.3d at 110](#) [\*31] (quoting P. Areeda & H. Hovenkamp, **FEDERAL ANTITRUST LAW**, P 807f, pp. 360-61). Here, Plaintiff remains profitable, and there is no evidence that its market share is declining. Thus, Plaintiff's claim is inherently implausible, and Plaintiff has provided no evidence to support its allegation that it is about to be eliminated from the printing market.

### **c. Plaintiff's Failure To Establish A Relevant Market**

[HN15](#) [↑] As part of dangerous probability analysis, Plaintiff also has the burden to demonstrate a properly-defined relevant product and geographic market. [\*Fraser v. Major League Soccer, L.L.C.\*, 284 F.3d 47, 61-62](#) [\*133] (1st Cir.), cert. denied, 537 U.S. 885, 154 L. Ed. 2d 144, 123 S. Ct. 118 (2002) (failure to prove relevant market "dooms [plaintiffs'][section 2](#) claims"); [\*Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp.\*, 79 F.3d 182, 197](#) (1st Cir. 1996). Plaintiff's expert, Dr. Fisher, argues that the relevant geographic market is limited to printers physically located in Puerto Rico, because the time and expense required to transport shoppers into Puerto Rico from other locations, as well as other considerations, render printers outside Puerto Rico poor [\*32] substitutes for Puerto Rican printers.

We do not believe a finder of fact could rationally exclude from the relevant market printers located outside Puerto Rico that currently sell significant quantities of shoppers into Puerto Rico. Currently, approximately 20 percent of the shoppers inserted in *El Nuevo Dia* are printed outside Puerto Rico, suggesting that offshore printers already compete substantially with Plaintiff and Defendant AGP. During the pendency of this lawsuit, a printer from the Dominican Republic successfully entered the market to print shoppers for distribution in Puerto Rico. Moreover, Dr.

Fisher admits that if prices increased sufficiently, the presence of offshore printers could constrain prices charged by Puerto Rican printers. Finally, the record reveals substantial testimony from customers that have used or considered offshore printers, or would do so if prices increased in Puerto Rico.

Plaintiff's allegation that Defendants have a dangerous probability of achieving a monopoly in the printing of shoppers is devoid of evidentiary basis for three reasons: Plaintiff is a healthy, viable company that shows no signs of being eliminated as a competitor; Defendants' [\[\\*\\*33\]](#) market shares do not reflect a risk that Plaintiff will be driven from the market; and Plaintiff's definition of the relevant geographic market is too narrow. [HN16](#)<sup>↑</sup> Plaintiff has the burden to prove each element of its attempted monopolization claim, or summary judgment is appropriate. [Springfield Terminal, 133 F.3d at 107-10 HN17](#)<sup>↑</sup> (summary judgment warranted by "any fatal factual deficiency" in non-movant's case). Summary judgment is, thus, appropriate on the attempted monopolization claim.

## **2. Predatory or Anticompetitive Conduct**

Plaintiff also fails to meet its burden of creating a triable issue of material fact that Defendants engaged in any predatory or anticompetitive conduct. Plaintiff alleges three different types of anticompetitive conduct in support of its attempted monopolization claim: (1) unlawful tying, (2) unlawful bundling, and (3) predatory pricing. [Docket Document No. 1.](#)

In the tying and bundling claims, Plaintiff contends that Defendants' joint sales efforts - group contracts and other package discount offers and the "Alcance" program - are anticompetitive. [HN18](#)<sup>↑</sup> "Package" sales, however, are widespread and ordinarily lawful. "Buyers often find package [\[\\*\\*34\]](#) sales attractive; a seller's decision to offer such packages can merely be an attempt to compete effectively - conduct that is entirely consistent with the [Sherman Act](#)." [Jefferson Parish Hospital Dist. No. 2 v. Hyde, 466 U.S. 2, 12, 80 L. Ed. 2d 2, 104 S. Ct. 1551 \(1984\)](#). See also [Eastman Kodak Co. v. Image Tech. Servs., Inc., 504 U.S. 451, 478-79, 119 L. Ed. 2d 265, 112 S. Ct. 2072 \(1992\)](#) [HN19](#)<sup>↑</sup> ("It is undisputed that competition is enhanced when a firm is able to offer various marketing options, including bundling of support and maintenance service with the sale of equipment. Nor do such actions run afoul of the antitrust laws.") (footnote omitted); [SMS Sys. \[\\[\\\*134\\]\]\(#\) Maint. Servs., Inc. v. Digital Equip. Corp., 188 F.3d 11, 21 \(1st Cir. 1999\)](#). See Daniel A. Crane, [Multiproduct Discounting: A Myth of Nonprice Predation, 72 U. Chi. L. Rev. 27, 28-29 \(Winter 2005\)](#) ("Package discounting. . . is a pervasive phenomenon in the national economy, and one that produces substantial consumer benefits.") (footnote omitted).

Package sales are unlawful only in limited circumstances that Plaintiff has failed to show. The undisputed evidence demonstrates that Defendants have engaged only in a vigorous and lawful [\[\\*\\*35\]](#) effort to compete with a dominant competitor in the commercial printing business.

**Tying.** Plaintiff contends that Defendants' offers of insertion and ROP advertising discounts to advertisers who print with Defendant AGP amounts to an unlawful tying of shoppers to insertion and advertising. [Docket Document No. 1.](#) Plaintiff further contends that Defendant El Dia's policy of inserting only corporate supplements that are produced by a unit of Defendant AGP constitutes an unlawful tying arrangement. *Id.*

[HN20](#)<sup>↑</sup> "Tying is not automatically unlawful under the antitrust laws . . ." [Coady Corp. v. Toyota Motor Distrib., Inc., 361 F.3d 50, 60 \(1st Cir. 2004\)](#). [HN21](#)<sup>↑</sup> To prove a per-se tying violation, Plaintiff must prove that: (1) the tying and tied goods are two separate products; (2) the defendant affords consumers no choice but to purchase the tied product from it as a condition of obtaining the tying product; (3) the defendant has sufficient market power in the tying product market to distort consumers' choices with respect to the tied product; and (4) the tying arrangement forecloses a substantial volume of commerce. [United States v. Microsoft Corp., 346 U.S. App. D.C. 330, 253 F.3d 34, 85 \(D.C. Cir. 2001\)](#); [\[\\*\\*36\] Borschow Hosp. and Med. Supplies, Inc. v. Cesar Castillo Inc., 96 F.3d 10, 17 \(1st Cir. 1996\)](#) (quoting [Data Gen. Corp. v. Grumman Sys. Support Corp., 36 F.3d 1147, 1178 \(1st Cir. 1994\)](#)).

**Shoppers.** With respect to printing shoppers, the evidence is undisputed that the sale of advertising space or insertion of shoppers in *El Nuevo Dia* is not conditioned on the purchase of printing from Defendant AGP. Dr. Fisher agrees that there is no evidence of what he calls "classic" tying arrangements with respect to shoppers. Plaintiff, however, contends that the second element of its tying claim - the coercion of advertisers to print shoppers with

Defendant AGP - is met because Defendants allegedly coerce advertisers to use Defendant AGP by offering them discounts or lower prices on insertion and ROP advertising in the newspapers, as well as the accumulation of "Alcance" program points that can be redeemed at the newspapers. Docket Document No. 176. Plaintiff complains that it cannot offer the same types of discounts, but it has not quantified the discounts to which it objects; it has only submitted evidence of several examples of package offers [\[\\*\\*37\]](#) that it contends are coercive.

[HN22](#)<sup>↑</sup> To establish coercion the plaintiff must demonstrate that defendant's pricing structure "force[s] the buyer into the purchase of tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms." Wells Real Estate, Inc. v. Greater Lowell Bd. of Realtors, 850 F.2d 803, 814 (1st Cir. 1988) (quoting Jefferson Parish Hospital Dist. No. 2,466 U.S. at 12). See also Kell v. Am. Capital Strategies Ltd., 278 F.Supp.2d 156, 161 (D.P.R. 2003). The element of coercion, however, cannot be satisfied by mere discounts or other forms of package sales unless the combined purchase is the only economically-viable alternative. Marts v. Xerox, Inc., 77 F.3d 1109, 1113 (8th Cir. [\[\\*135\]](#) 1996) [HN23](#)<sup>↑</sup> (products not tied unless package is "only viable economic option" and separate purchase is "prohibitively expensive"); Ortho Diagnostic Sys. v. Abbott Lab., 920 F. Supp. 455, 471 (S.D.N.Y. 1996) (collecting cases).

Plaintiff ignores this prevailing legal standard in the First Circuit and relies on a criticized and outdated Fourth Circuit opinion, [\[\\*\\*38\]](#) Advance Business Systems & Supply Co. v. SCM Corp., 415 F.2d 55 (4th Cir. 1969), for the proposition that any conditional discount on one product renders the sale of two products together a tying arrangement. Plaintiff would have this court find that related companies cannot lawfully enter into joint sales efforts involving package discounts. The court rejects this standard.

While Plaintiff repeatedly characterizes Defendants' package discount programs as coercive, it supports its claims with examples of advertisers that rejected Defendants' offers. This evidence misses the point. Defendants cannot be offering the "only viable economic option" (Marts, 77 F.3d at 1113) when advertisers frequently reject their offers. Defendants have submitted undisputed testimony from advertisers confirming that advertisers regularly reject group contracts offered by Defendants, other packages offered by Defendant AGP, and opportunities to accumulate "Alcance" points by printing with Defendant AGP. Not a single customer testified to being coerced to print with Defendant AGP in order to receive benefits from Defendants' newspapers. Defendants also have submitted undisputed [\[\\*\\*39\]](#) evidence that 62 percent of all *El Nuevo Dia* advertisers that inserted shoppers had them printed by Plaintiff and by other printers in the mainland or the Dominican Republic, not by Defendant AGP. The record also shows that Plaintiff has maintained an approximately constant share of major shopper accounts since 1999, including customers that it has won from Defendant AGP and customers who have turned down Defendants' package offers.

These facts demonstrate that buying advertising from *El Nuevo Dia* without also buying printing services from AGP cannot have been "prohibitively expensive." Philip Areeda & Herbert Hovenkamp, ANTITRUST LAW P 1758b (2d ed. 2004) at p. 328 (no tying arrangement based on package discounts unless separate sales outside of package are below ten percent of total sales). See also Ortho Diagnostic Sys., 920 F.Supp. at 472 (17 percent of revenue resulted from non-package sales; "This empirical evidence alone shows that the purchase [of these products from the defendant] at the unbundled prices was not economically prohibitive.").

Plaintiff has failed to produce any evidence that Defendants have coerced advertisers to print shoppers with [\[\\*\\*40\]](#) Defendant AGP. What Plaintiff equates with coercion amounts to nothing more than normal competitive activity. Accordingly, we find that a reasonable finder of fact could not conclude that Defendants coerced advertisers with their discounts and, therefore, Plaintiff's tying claim with respect to shoppers fails.<sup>4</sup>

<sup>4</sup> Plaintiff contends that Defendants have engaged in unlawful tying in violation of Section 1, and then argues that those tying arrangements support its attempted monopolization claims under Section 2 of the Sherman Act. Docket Document No. 176. The existence of two separate products and the presence of coercion are essential elements of an unlawful tying arrangement under Section 1 of the Sherman Act. If Plaintiff's tying claims fail under Section 1, then they cannot provide evidence for its attempted monopolization claims under Section 2.

[\*136] **Corporate supplements.** With respect to corporate supplements, Defendant El Dia has a policy that it will insert in the newspaper only corporate supplements [\*\*41] produced by a unit of Defendant AGP. Plaintiff argues that this policy ties the distribution of corporate supplements, the tying product, with commercial printing by Defendant AGP, the tied product. Docket Document No. 176. Defendants assert that the policy does not satisfy the first and second elements necessary for a tying claim and is not anticompetitive. Docket Document No. 156. In addition, Defendants assert a First Amendment right to maintain the policy. Id. The court finds that Plaintiff has not established the elements of a tying claim and, therefore, will enter summary judgment against this claim.

Plaintiff makes a centerpiece of its case a de minimis part of the advertising and printing business in Puerto Rico. Plaintiff has not quantified the number of inserts it contends is printed within its alleged printing market, but Defendants have submitted undisputed evidence that of the 5,000 commercial inserts in *El Nuevo Día* in a five-year period only 134 were corporate supplements. Plaintiff has submitted evidence that one advertiser wanted to use Plaintiff to print its corporate supplement. Even Dr. Fisher concedes that *El Nuevo Día's* corporate supplement [\*\*42] policy, standing alone, does not have a significant anticompetitive effect. HN24[] "The tying claim must fail absent any proof of anti-competitive effects in the market for the tied product." Wells Real Estate, 850 F.2d at 815. Plaintiff has failed to satisfy this burden.

Plaintiff also has failed to show the other elements of tying. Defendants contend that corporate supplements are not separate products, but rather two components of a single product -- the preparation of a section of the newspaper. Docket Document No. 156. Corporate supplements are one of several vehicles Defendant El Dia creates to sell advertising space, in this case to the featured company's sponsors. Plaintiff cannot distinguish corporate supplements from the newspaper's sports section or Defendant El Dia's own glossy paper magazines that are printed by Defendant AGP and inserted into the newspaper. Each of these products contains editorial material, as well as advertising that generates most of the newspaper's income.<sup>5</sup> The newspaper pays the costs of producing corporate supplements, including creative work, insertion, advertising sales, and printing, from sponsors' advertising revenues, just [\*\*43] as the cost of other sections of the newspaper are paid for largely from advertising revenues.

HN25[] Two products exist for tying purposes only where there is substantial consumer demand for separate products. "The answer to the question whether one or two products are involved turns not on the functional relation between them, but rather on the character of the demand for the two items." Jefferson Parish Hosp. Dist. No. 2, 466 U.S. at 19; [\*\*44] Data Gen. Corp., 36 F.3d at 1179 (internal quotations omitted). The evidence does not support a finding of such separate demand. Since the newspaper is paying [\*137] the costs for the corporate supplements, the featured business is not purchasing printing or any of the other services needed to produce the corporate supplement and therefore is not providing a demand for printing. Even if the featured business were considered a printing customer, Plaintiff has not produced sufficient evidence for a reasonable fact finder to conclude that the printing of corporate supplements constitutes a separate product.

For the same reason, Plaintiff cannot prove that Defendants coerce featured businesses to purchase printing from Defendant AGP. Because *El Nuevo Día* corporate supplements are financed through advertising revenues from the supplement, the featured business does not purchase printing, and thus it is not coerced to purchase any product.

HN26[] The absence of a coerced purchase defeats any possibility of an unlawful tying arrangement. Jefferson Parish Hospital Dist. No. 2, 466 U.S. at 12. HN27[] ("The essential characteristic of an invalid tying arrangement lies in the seller's [\*\*45] exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the *buyer* either did not want at all, or might have preferred to purchase elsewhere on different terms.").

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<sup>5</sup> Corporate supplements, thus, resemble other advertising vehicles as to which courts have rejected tying claims that attempted to split integral components of those vehicles into tied and tying products. Hirsh v. Martindale-Hubbell, Inc., 674 F.2d 1343, 1347 (9th Cir. 1982) (advertising in legal directory and requirement to purchase copy of directory single product); RFD Publ'ns, Inc. v. Oregonian Publ'g. Co., 749 F.2d 1327, 1327 (9th Cir. 1984) (sale of newspaper advertising and advertising mailed to non-subscriber's single product).

Defendant El Dia's right to control the editorial content and preparation of corporate supplements is also protected by the First Amendment. [HN28](#)<sup>↑</sup> Would-be advertisers have no right to compel a newspaper to accept their advertisements, let alone editorial material. "The [advertiser's] right to free speech does not give it the right to make use of the defendants' printing presses and distribution systems without defendants' consent." [Chicago Joint Bd., Amalgamated Clothing Workers of Am. AFL-CIO v. Chicago Tribune Co.](#), 435 F.2d 470, 478 (7th Cir. 1970). See also [Person v. New York Post Corp.](#), 427 F.Supp. 1297, 1301 (E.D.N.Y. 1977) (claim that newspaper could be ordered to carry plaintiff's advertisements "runs squarely against the wall of freedom of the press"). *El Nuevo Dia* has chosen to maintain editorial and business control over corporate supplements by assigning their production to Creative Minds, formerly an *El Nuevo Dia* [\\*\\*46](#) staff unit that was transferred to Defendant AGP. This approach ensures the newspaper that the content of corporate supplements is accurate and comports with its style and content policies.

Plaintiff acknowledges that corporate supplements are an editorial product; it contends, however, that Defendant El Dia can maintain editorial control even while Plaintiff prints the corporate supplements, as it did prior to the creation of Defendant AGP. [HN29](#)<sup>↑</sup> The newspaper's right to control editorial content, however, extends to how editorial materials are prepared. In [Miami Herald Publ'g Co. v. Tornillo](#), the Supreme Court said that the government is prohibited from imposing a penalty "in terms of the cost in printing and composing time and material and in taking up space that could be devoted to other material the newspaper may have preferred to print." [418 U.S. 241, 256, 41 L. Ed. 2d 730, 94 S. Ct. 2831 \(1974\)](#). Requiring the newspaper to engage an outside printer, when it can use an affiliated company, would impose unnecessary costs on the newspaper that would violate its First Amendment rights.

Accordingly, summary judgment will be entered against Plaintiff's tying claim regarding corporate supplements.

[\[\\*\\*47\]](#) **Bundling.** Plaintiff claims that when Defendants offer financial incentives - such as group contracts and the "Alcance" program - to encourage advertisers to print shoppers with AGP, these incentives constitute unlawful bundling. Docket Document No. 176. Defendants contend that [\[\\*138\]](#) their joint selling practices are widely used, pro-competitive, and lawful. The court agrees with the Defendants.

[HN30](#)<sup>↑</sup> Although few cases have addressed bundled pricing as a potential antitrust violation, one requirement is clear: The challenged prices must have the effect of excluding a single-product competitor. See P. Areeda & H. Hovenkamp, ANTITRUST LAW P 749 (2d ed. 2004 Supp.) at p. 182-83 ("[A] requirement that the bundling practice be sufficiently severe to exclude an equally efficient single-product rival, and without an adequate business justification, seems to strike about the right balance between permitting aggressive pricing while prohibiting conduct that can only be characterized as anticompetitive."). In [Ortho Diagnostic Systems](#), summary judgment was granted against the plaintiff, a single-product competitor, because the plaintiff was indisputably able to compete profitably against [\[\\*\\*48\]](#) the multi-product defendant, despite the defendant's bundled pricing. [HN31](#)<sup>↑</sup> "The fact [that the plaintiff was profitable] is highly significant. . . . Only price cutting that threatens equally or more efficient firms is condemned under [Section 2](#)." [The plaintiff must prove] "that the defendant's pricing makes it unprofitable for the plaintiff to continue to produce." [920 F. Supp. at 469-70](#).

Here, far from being excluded, Plaintiff has indisputably experienced consistent and increasing profits and sales during the seven years of Defendant AGP's existence, and Plaintiff consistently makes the largest volume of shopper sales in the alleged market. Plaintiff has provided no evidence of the amount of printing sales subject to bundling, the amount of printing sales it claims to have lost as a result of specific bundled contracts, or how any discounts or benefits offered in any group contract actually caused Plaintiff's loss of sales. Without specific data on the specific sales allegedly lost by Plaintiff subject to group contracts by Defendants, and without evidence that those sales were lost because of bundled pricing, Plaintiff has not demonstrated antitrust injury. [Virgin Atl. Airways Ltd. v. British Airways PLC](#), 257 F.3d 256, 271 (2d Cir. 2001) [\[\\*\\*49\]](#) (requiring evidence showing "what percentage of bundled sales actually included one of the five routes at issue. . . . which of these flights were bundled with more competitive transatlantic routes, what prices were paid on the bundled flights, what costs were incurred, and whether [the defendant] realized sufficient profits to cover the alleged losses on the transatlantic flights").

Nor has Plaintiff shown that bundled discounts had a coercive effect on any customer. [Virgin Atl. Airways Ltd., 257 F.3d at 270](#) (noting absence of "exhibits showing that specific customers felt compelled to purchase products under the defendant's bundling program because the plaintiff could not match the discounts"). Rather, Plaintiff's continued ability to outsell Defendants, together with the substantial evidence of customers who have rejected Defendants' group contracts and "Alcance" program offers to print with Plaintiff, demonstrate that these practices have had no discernible exclusionary effect on Plaintiff. In the absence of such an effect, Plaintiff's bundling claim necessarily fails.<sup>6</sup>

**[\*\*50] [\*139] Predatory Pricing.** Plaintiff alleges that Defendants have engaged in predatory or below-cost pricing of shopper printing and insertion services. [Docket Document No. 1](#). The undisputed material facts fail to bear out this claim.

[HN32](#) [+] An attempted monopolization plaintiff basing its claims on predatory pricing must establish "two prerequisites to recovery" under [Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 125 L. Ed. 2d 168, 113 S. Ct. 2578 \(1993\)](#). First, the prices complained of must be "below an appropriate measure of [the defendant's] costs." [Id. at 223](#). Second, recoupment must be probable; the alleged predator must have the ability to eliminate its competition and then recover its losses through future high prices. [Id. at 224](#).

[HN33](#) [+] Although the Supreme Court has not specified the "appropriate measure" of cost in a predatory pricing case, the generally accepted standard in the First Circuit and most other circuits is whether a seller's prices exceed its incremental (or marginal) cost: "Ordinarily the measure of a 'predatory price' is price below 'incremental cost.' . . . that is to say, the addition to total cost (to the firm) of producing [\*\*51] and selling additional output would exceed the return from selling that additional output." [Clamp-All Corp. v. Cast Iron Soil Pipe Inst., 851 F.2d 478, 483 \(1st Cir. 1988\)](#) (Breyer, J.) (emphasis original; citation omitted). See also [Barry Wright Corp. v. ITT Grinnell Corp., 724 F.2d 227, 232 \(1st Cir. 1983\)](#) (Breyer, J.).

[HN34](#) [+] Incremental or marginal cost is difficult to measure. The First Circuit and most other circuits, therefore, rely on average variable cost (those costs that change as output changes) as an approximation of incremental cost. In the First Circuit and most others, variable cost is "the normal test of predation[.]" [Tri-State Rubbish, Inc. v. Waste Mgmt., Inc., 998 F.2d 1073, 1080 \(1st Cir. 1993\)](#). See also [Stearns Airport Equip. Co. v. FMC Corp., 170 F.3d 518, 532 \(5th Cir. 1999\); Morgan v. Ponder, 892 F.2d 1355, 1360 \(8th Cir. 1989\); Northeastern Tel. Co. v. American Tel. & Tel. Co., 651 F.2d 76, 88 \(2d Cir. 1981\)](#).

[HN35](#) [+] Because the antitrust laws seek to promote vigorous price competition resulting in low prices, "we must be mindful that low prices are a positive aspect [\*\*52] of a competitive marketplace and are encouraged by the antitrust laws." [Virgin Atl. Airways Ltd., 257 F.3d at 269](#). Courts, therefore, carefully scrutinize attempted monopolization claims based on predatory pricing. "The requisites for proving predatory pricing are demanding, because the conditions under which it is plausible are not common, and because it can easily be confused with merely low prices which benefit consumers." [Tri-State Rubbish, Inc., 998 F.2d at 1080](#). See also [Virgin Atl. Airways Ltd., 257 F.3d at 266](#) ("The Supreme Court has expressed deep skepticism regarding the viability of proving a predatory pricing scheme."); [Stearns Airport Equip. Co., 170 F.3d at 527](#) (same); [Bathke v. Casey's Gen. Stores, Inc., 64 F.3d 340, 343 \(8th Cir. 1995\)](#) (same).

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<sup>6</sup> [LePage's Inc. v. 3M, 324 F.3d 141 \(3d Cir. 2003\)](#), cert. denied, 542 U.S. 953, 124 S. Ct. 2932, 159 L. Ed. 2d 835 (2004), relied on by Plaintiff, is inapposite. The single-product plaintiff in [3M](#) was unable to compete with the defendant's multi-product discounts: The plaintiff's "healthy operating income" fell and became "large operating losses," its sales and its market share declined, and it closed one of its two plants. [324 F.3d at 161-62](#). Here, Plaintiff has been profitable, its shopper sales have increased, its market share has remained constant, and it has added new production capacity. Moreover, in [3M](#), the defendant was an admitted monopolist that used its multi-product discounts to prevent the plaintiff from successfully entering the market. [Id. at 159-60](#). Here, Defendant AGP was a new entrant and Plaintiff was the dominant incumbent, whose market share prior to AGP's entry was in excess of 80 percent.

Defendants have presented an analysis by an accounting expert that concludes that Defendant AGP did not price below average variable cost during the 1999-2003 period, i.e., that Defendant AGP maintained [\*140] a positive "contribution margin" - revenues less variable costs - for its shopper printing business throughout that period. Plaintiff responded [\*53] with an analysis by its economic expert, Dr. Fisher, that examined transactions with particular customers of Defendant AGP, and (among other things) treated discounts granted to those customers by Defendants El Dia and Primera Hora as deductions from Defendant AGP's revenues. Even with those recalculations, however, Dr. Fisher still concluded that Defendant AGP had a 21-percent positive contribution margin for the shopper customers he examined using one methodology, and a 26-percent positive contribution margin for the shopper customers he examined using an alternative methodology. It is, therefore, undisputed that Defendant AGP priced above its average variable costs in its overall shopper printing business.

Dr. Fisher also concluded that a limited number of printing jobs, representing 10 percent of Defendant AGP's sales by one methodology, and 8 percent of Defendant AGP's sales by an alternative methodology, were priced below its average variable costs. Even if Dr. Fisher is correct, [HN36](#) claims of below-cost pricing on a small percentage of a firm's sales are insufficient to raise a triable issue of predatory pricing. [HN37](#) Predation claims cannot be based on occasional instances of allegedly [\*54] predatory pricing, because they are not likely to drive rivals from the market and to permit the predator to raise prices and profits subsequently. A predatory pricing plaintiff can prevail only by adducing "evidence suggesting defendants' *overall* price structure was predatory," not that a small minority of sales were below average variable cost. [Morgan, 892 F.2d at 1361](#) (emphasis original). See also [Steams Airport Equip. Co., 170 F.3d at 529](#) ("[The plaintiff] has introduced no evidence that its survival is threatened by the sales lost to the rare, sporadic predation that it allege[s]."); [Taylor Publ'g Co. v. Jostens, Inc., 216 F.3d 465, 478 \(5th Cir. 2000\)](#) (alleged predatory pricing too limited to exclude competitor); [Springfield Terminal, 133 F.3d at 109](#) (one example of below-cost pricing insufficient).<sup>7</sup>

[\*\*55] Dr. Fisher also computed the portion of Defendant AGP's sales that he asserted was below average *total* cost, i.e., the extent to which Defendant AGP's revenues did not cover both its variable and fixed costs. [HN40](#) Sales below average total cost (in other words, whether a firm has a bottom-line net loss) are irrelevant to predatory pricing analysis in the First Circuit and the majority of other circuits that have adopted the average variable cost standard. [Adjusters Replace-A-Car, Inc. v. Agency Rent-A-Car, Inc., 735 F.2d 884, 891, 892 \(5th Cir. 1984\)](#) ("costly error" for plaintiff to interpret statement that defendant "had suffered 'a net loss from operations' [\*141] to be effectively an admission of predatory pricing;" plaintiff erroneously ignored "the difference between a net operating loss and a price below average variable cost"); [Berlyn, Inc. v. Gazette Newspapers, Inc., 223 F. Supp. 2d 718, 734-35 \(D. Md. 2002\)](#) (summary judgment on predation claim that newspaper's losses were funded by parent company; "Simply losing money is not a 'pricing policy.'"), aff'd, [73 Fed. Appx. 576 \(4th Cir. 2003\)](#).<sup>8</sup>

### **[\*\*56] 3. Specific Intent to Monopolize**

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<sup>7</sup> Plaintiff also argues that Defendant AGP charged prices below average variable cost to certain customers when it first entered the market in 1997, and shortly thereafter. [Docket Document No. 176](#). [HN38](#) Promotional discounts by new entrants, however, are not regarded as predatory. [HN39](#) "Unless continued over a long period of time, in which case it is no longer promotional, promotional pricing by new entrants . . . [is] no threat to competition. . . . Under these circumstances courts find promotional prices lawful, no matter what that price-cost relationship." III Phillip E. Areeda & Herbert Hovenkamp, [Antitrust Law](#) 492 (2002) (footnote omitted). See also [Am. Academic Suppliers, Inc. v. Beckley-Cardy, Inc., 922 F.2d 1317, 1322 \(7th Cir. 1991\)](#) ("It is commonplace for new entrants to use deep discounts to persuade customers to switch from established firms. These promotional discounts raise no antitrust problems. . . ., though often they are below incremental cost in a superficial sense."). Moreover, Defendant AGP's general manager in 1997-1998, in testimony offered by Plaintiff, said that the company never priced below cost.

<sup>8</sup> In its complaint, Plaintiff also alleges that Defendant El Dia engaged in below-cost pricing of insertion services in the newspaper. [Docket Document No. 1](#). Plaintiff subsequently contended that Defendant El Dia's above-normal profits on insertion proved that it possessed market power. [Docket Document No. 176](#). Those two positions are inconsistent. Defendants' accounting expert concluded that Defendants priced above average variable costs for insertion services, and there is no genuine dispute that Defendants' insertion pricing was not below any relevant measure of cost.

**HN41** [↑] A final requirement of an attempted monopolization claim is evidence that the defendants had a "specific intent to destroy competition or build monopoly[.]" [Times-Picayune Publ'g Co. v. United States, 345 U.S. 594, 626, 97 L. Ed. 1277, 73 S. Ct. 872 \(1953\)](#). Evidence of a mere desire to increase market share or win customers from a competitor does not suffice. E.g., [Spectrum Sports, Inc., 506 U.S. at 459 HN42](#) [↑] ("the necessary intent to monopolize . . . is something more than an attempt to compete vigorously").

Plaintiff has not shown that any of Defendants' conduct evidences an intent to monopolize the printing market. Plaintiff's principal evidence of intent consists of an affidavit from Defendant AGP's first general manager for the proposition that shortly before Defendant AGP was formed, Defendant AGP hired some of Plaintiff's employees with the knowledge that doing so would harm Plaintiff.

This testimony, however, does not establish an intent to monopolize the printing market. **HN43** [↑] Predatory hiring cases must be proved by a showing that the hiring "was made with such predatory intent, i.e., to harm the competition *without helping the* [\*\*57] [defendant], or by showing a clear nonuse in fact." [Universal Analytics, Inc. v. MacNeal-Schwendler Corp., 914 F.2d 1256, 1258 \(9th Cir. 1990\)](#) (emphasis added). Here, it is undisputed that Defendant AGP did use the employees who formerly worked for Plaintiff, and the affidavit acknowledges that hiring the employees benefited Defendant AGP by providing it with skilled employees who would not need to be trained.

Thus, Plaintiff has failed to demonstrate that Defendants had a specific intent to monopolize the printing market.

## B. Monopolization

Plaintiff also alleges that Defendant El Dia has monopolized the market for the delivery of shoppers in Puerto Rico. Docket Document No. 1. Plaintiff has failed to raise a triable issue with regard to this claim, and summary judgment is, therefore, appropriate.

**HN44** [↑] The offense of monopolization under [Section 2 of the Sherman Act](#) requires proof that the defendants (1) have acquired a monopoly in the relevant market and (2) have willfully acquired or maintained that monopoly power. [Eastman Kodak Co., 504 U.S. at 481](#) (citing [United States v. Grinnell Corp., 384 U.S. 563, 570-71, 16 L. Ed. 2d 778, 86 S. Ct. 1698 \(1966\)](#)). [\*\*58]

As a threshold matter, Plaintiff lacks standing to assert an antitrust claim for monopolization of the market for the [\*142] delivery of shoppers. **HN45** [↑] A private antitrust plaintiff must show "antitrust injury," or "injury of the type the antitrust laws were intended to prevent[.]" [Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328, 334, 109 L. Ed. 2d 333, 110 S. Ct. 1884 \(1990\)](#). Plaintiff is neither a consumer nor a competitor in the delivery market; Plaintiff neither advertises through the use of shoppers nor does it deliver shoppers to consumers in competition with Defendants. **HN46** [↑] "Competitors and consumers in the market where trade is allegedly restrained are presumptively the proper plaintiffs to allege antitrust injury." [Serpa Corp. v. McWane, Inc., 199 F.3d 6, 10 \(1st Cir. 1999\)](#).

Even if it had standing, Plaintiff has not presented a triable issue as to whether Defendants possess monopoly power in a relevant market. Plaintiff contends that the relevant market is limited to the delivery of shoppers through newspapers of general circulation in Puerto Rico. Plaintiff excludes all other forms of advertising and other methods of delivering shoppers from its market definition. There are [\*\*59] three competing newspaper companies in Puerto Rico that operate four daily newspapers: *El Nuevo Dia* and *Primera Hora* (which are under common ownership with Defendants), *El Vocero*, and the *San Juan Star*. Plaintiff's complaint alleges that each of these newspapers is in the shopper delivery market. Docket Document No. 1. It is unusual in the United States for cities with populations larger than Puerto Rico to have three independently-owned competitive daily newspapers. Plaintiff has not presented evidence to support the hypothesis that Defendants have monopoly power in shopper delivery despite the presence of two other competing newspapers also available to shopper advertisers.

It is also undisputed that shoppers are delivered to consumers in Puerto Rico by methods other than insertion in daily newspapers. Those other methods include house-to-house delivery, direct mail, and in-store distribution. While these methods may not be perfect substitutes for newspaper delivery, it is undisputed that numerous

advertisers use them to distribute significant numbers of shoppers in Puerto Rico. Wal-Mart, for instance, delivers only 15 percent of its shoppers through newspapers. [\*\*60] It is also undisputed that firms exist in Puerto Rico that specialize in such alternative delivery methods, including at one time a firm owned in part by Plaintiff itself. Barriers to entry for such firms appear to be low. *See Advo, Inc. v. Philadelphia Newspapers, Inc., 51 F.3d 1191, 1200 (3d Cir. 1995)*. Once again, Plaintiff has excluded from its market definition competitors that are already competing in the market. *HN47*[<sup>14</sup>] Courts are reluctant to confine markets for delivery of particular types of advertising to a single method, given the variety of alternatives ordinarily available. *Menasha Corp. v. News America Mktg. In-Store, Inc., 354 F.3d 661, 664 (7th Cir. 2004)* ("The number of ways to promote a product is large, and even a stranglehold over at-shelf coupon dispensers would affect only a tiny portion of these means."). Plaintiff's market definition is, thus, too narrow.

Finally, Plaintiff does not identify evidence of anticompetitive conduct by the Defendants that constituted the willful acquisition or maintenance of monopoly power in the alleged delivery market. There is no evidence that Defendants took any action that reduced competition either [\*\*61] among daily newspapers, or among alternative shopper delivery methods such as direct mail, house-to-house delivery, and in-store distribution.

### C. Violations of Puerto Rico Antitrust Laws

Plaintiff alleges that Defendants also have violated the antitrust laws of [\*143] Puerto Rico, 10 P.R. LAWS ANN. §§ 258, 260 and 268 (1997 & Supp. 2001). Docket Document No. 1. *HN48*[<sup>15</sup>] Puerto Rico's antitrust laws, however, mirror the federal antitrust statutes. *See Coastal Fuels of Puerto Rico, Inc. v. Caribbean Petroleum Corp., 79 F.3d 182 (1st Cir. 1996); Podiatrist Ass'n, Inc. v. La Cruz Azul De Puerto Rico, Inc., 332 F.3d 6, 16 (1st Cir. 2003); Leopoldo Fontanillas, Inc. v. Luis Ayala Colon Sucesores, Inc., 283 F. Supp. 2d 579, 592 (D.P.R. 2003)*. Plaintiff bases its Puerto Rico law antitrust claim on the same allegations that serve as the basis for its federal law antitrust claim. Accordingly, for the same reasons Plaintiff's federal antitrust claims fail as a matter of law, Plaintiff's Puerto Rico law antitrust claim also fails as a matter of law.

### D. Unfair Trade Practices

Plaintiff also asserts a claim for [\*\*62] unfair trade practices under Article 1802 of the Puerto Rico Civil Code, 31 P.R. LAWS ANN. § 5141 (1991 & Supp. 2001)). Docket Document No. 1. *HN49*[<sup>16</sup>] The elements of a claim under Article 1802 are (1) proof of the reality of the damage suffered; (2) a causal relationship between this damage and the action or omission of another person; and (3) said act or omission is negligent or wrongful. *Woods-Leber v. Hyatt Hotels of Puerto Rico, Inc., 951 F. Supp. 1028, 1035-36 (D.P.R. 1996)*.

Plaintiff has not established that Defendants committed any negligent or wrongful acts. On the contrary, we have found that Defendants have engaged in legitimate competition as a matter of law. Accordingly, Plaintiff cannot prove that any of Defendants' conduct constitutes an unfair trade practice under Article 1802.

### E. Tortious Interference

Plaintiff also asserts a claim for tortious interference with business and contractual relationships. Docket Document No. 1. *HN50*[<sup>17</sup>] To establish such a claim, Plaintiff must show: "(1) the existence of a contract; (2) that the interfering party acted with intent and knowledge of the existence of a contract; (3) that [\*\*63] plaintiff suffered damages; and (4) that there exists a causal link between the injury and the interfering party's actions." *Fontanillas, 283 F. Supp. 2d at 588* (citing *General Office Prods. Corp. v. A.M. Capen's Sons, Inc., 15 P.R. Offic. Trans. 727, 115 D.P.R. 553, 558-59 (1984)*). Moreover, *HN51*[<sup>18</sup>] when the contract allegedly interfered with is terminable at will, "the privilege of competition has been recognized. In such a case, there is no contract right to have the relation continued, but only an expectancy," which is not actionable. *Id.* (quoting *Dolphin Int'l of Puerto Rico v. Ryder Truck Lines, 127 D.P.R. 869, 883, 1991 Juris P.R. 13 (1991)*).

Here, Plaintiff has not identified any specific contract that Defendants are alleged to have interfered with, let alone evidence from which a finder of fact could determine whether any such contract was terminable at will. Instead,

Plaintiff relies on the general assertion that "shopper printing is handled mainly on a contract basis," Docket Document No. 176, and identifies specific accounts that it claims Defendants "targeted," in some cases unsuccessfully. Id. Because Plaintiff and Defendant AGP are competitors, that Defendant **[\*\*64]** AGP gained customers from Plaintiff is neither surprising nor unlawful. Even if the customers taken by Defendant AGP had contracts with Plaintiff - which Plaintiff has not established - the burden is on Plaintiff to show that the contracts were in effect when the customer switched printers, that the contracts were not terminable at will, and that Defendant AGP was aware of the existence and non-terminable nature of the contracts. Plaintiff has made no such showing.

**[\*144]** Finally, Plaintiff relies on evidence of Defendant AGP's hiring of Plaintiff's employees in 1997 in support of its tortious interference claim. We previously dismissed Plaintiff's predatory hiring claim as barred by the statute of limitations, Docket Document No. 59, and need not revisit the claim here.

#### IV.

#### Conclusion

This case falls into the category of antitrust actions against which the Supreme Court warned: It has been brought by a dominant competitor against a new entrant and has had potentially-serious anticompetitive effects. The record includes depositions from fifteen advertisers who have testified to the pro-competitive impact of having a new commercial printer in Puerto Rico. Plaintiff's **[\*\*65]** case, by contrast, has been marked by legal theories that conflict with controlling Supreme Court and First Circuit precedents, and factual allegations unsupported by any facts or based upon implausible inferences.

In accordance with the foregoing, we **GRANT** Defendants' summary judgment motion as to all remaining counts of the complaint. Judgment shall be entered accordingly.

#### **IT IS SO ORDERED.**

San Juan, Puerto Rico, this 3rd day of June, 2005.

S/Jose Antonio Fuste

JOSE ANTONIO FUSTE

Chief U. S. District Judge

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End of Document



## **Mothershed v. Justices of the Supreme Court**

United States Court of Appeals for the Ninth Circuit

April 15, 2005, Argued and Submitted, San Francisco, California ; June 6, 2005, Filed

No. 03-16878

**Reporter**

410 F.3d 602 \*; 2005 U.S. App. LEXIS 10407 \*\*; 2005-1 Trade Cas. (CCH) P74,826

GEORGE L. MOTHERSHED, Plaintiff-Appellant, v. JUSTICES OF THE SUPREME COURT; CLERK OF THE SUPREME COURT, STATE OF ARIZONA; SUPREME COURT OF ARIZONA DISCIPLINARY COMMISSION; HEARING OFFICER; BAR COUNSEL OF ARIZONA STATE BAR ASSOCIATION; STATE OF OKLAHOMA JUSTICES OF THE SUPREME COURT; OKLAHOMA PROFESSIONAL RESPONSIBILITY TRIBUNAL OF THE SUPREME COURT, Chief Master; OKLAHOMA PROFESSIONAL RESPONSIBILITY TRIBUNAL OF THE SUPREME COURT, Trial Panel of February 1, 2002; GENERAL COUNSEL OF OKLAHOMA BAR ASSOCIATION; TRIAL COUNSEL OF OKLAHOMA BAR ASSOCIATION; RUDOLPH HARGRAVE, Oklahoma Supreme Chief Justice; MADELINE HARGRAVE, Wife; ROBERT E. LAVENDER, Justice, Oklahoma Supreme Court; MAXINE LAVENDER, Wife; JOSEPH M. WATT, Vice-Chief Justice, Oklahoma Supreme Court; CATHY WATT, Wife; RALPH B. HODGES, Justice, Oklahoma Supreme Court; JANELLE HODGES, Wife; MARIAN P. OPALA, Justice, Oklahoma Supreme Court; JANE DOE OPALA, Wife; DANIEL J. BOUDREAU, Justice, Oklahoma Supreme Court; JANE DOE BOUDREAU, Wife; YVONNE KAUGER, Justice, Oklahoma Supreme Court; NED BASTOW, Husband; HARDY SUMMERS, Justice, Oklahoma Supreme Court; MARILYN SUMMERS, Wife; JAMES WINCHESTER, Justice, Oklahoma Supreme Court; SUSAN WINCHESTER, Wife; J. DANIEL MORGAN, Chief Master, Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE MORGAN, Wife; J. PATRICK KENT, Presiding Master, Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE KENT, Wife; ROBERT L. HERT, JR., Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE HERT, Wife; DANA WILLIAMS, Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; DALE CABINESS, Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE CABINESS, Wife; DAN MURDOCK, General Counsel, Supreme Court of Oklahoma; JANE DOE MURDOCK, Wife; ALLEN J. WELCH, Bar Counsel, Oklahoma Supreme Court; JANE DOE WELCH, Wife; CHARLES E. JONES, Chief Justice, Arizona Supreme Court; JANE DOE JONES, Wife; RUTH V. MCGREGOR, Vice Chief Justice, Arizona Supreme Court; JOHN DOE MCGREGOR, Husband; STANLEY FELDMAN, Justice, Arizona Supreme Court; JANE DOE FELDMAN, Wife; REBECCA WHITE BERCH, Justice, Arizona Supreme Court; JOHN DOE BERCH, Husband; MICHAEL D. RYAN, Justice, Arizona Supreme Court; JANE DOE RYAN, Wife; PETER CAHILL, Member of the Disciplinary Commission of the Supreme Court of Arizona; JESSICA GIFFORD FUNKHOUSER, Member of the Disciplinary Commission of the Supreme Court of Arizona; CYNTHIA L. CHOATE, Member of the Disciplinary Commission of the Supreme Court of Arizona; BARBARA ATWOOD, Member of the Disciplinary Commission of the Supreme Court of Arizona; C. ALAN BOWMAN, Member of the Disciplinary Commission of the Supreme Court of Arizona; CRAIG MEHRENS, Member of the Disciplinary Commission of the Supreme Court of Arizona; STEVEN G. NELSON, Member of the Disciplinary Commission of the Supreme Court of Arizona; LOREN J. BRAUD, Bar Counsel, Arizona Supreme Court aka Loren J. Broad; JANE DOE BRAUD, Wife aka Jane Doe Broad; JOHN PRESSLEY TODD, Hearing Office 7X, Arizona Supreme Court; JANE DOE TODD, Wife; NOEL K. DESSAINT, Clerk, Arizona Supreme Court; WILLIAM M. SPENCE, Attorney; JANE DOE SPENCE, Wife, Defendants-Appellees.

**Subsequent History:** Amended by, Rehearing denied by [Mothershed v. Justices of the Supreme Court, 2005 U.S. App. LEXIS 14804 \(9th Cir. Ariz., July 21, 2005\)](#)

410 F.3d 602, \*602L 2005 U.S. App. LEXIS 10407, \*\*10407

Reprinted as amended at [\*Mothershed v. Justices of the Supreme Court, 2005 U.S. App. LEXIS 14812 \(9th Cir. Ariz., July 21, 2005\)\*](#)

**Prior History:** [\[\\*\\*1\]](#) Appeal from the United States District Court for the District of Arizona. D.C. No. CV-02-02375-RCB. Robert C. Broomfield, District Judge, Presiding.

[\*State ex rel. Okla. Bar Ass'n v. Mothershed, 2003 OK 34, 66 P.3d 420, 2003 Okla. LEXIS 37 \(Okla., 2003\)\*](#)

**Disposition:** AFFIRMED.

## Core Terms

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Antitrust, district court, disciplinary proceeding, regulation, practice of law, challenges, state court, disciplinary, state bar, Sherman Act, out-of-state, quotation, marks, subject matter jurisdiction, lower federal court, federal court, restrictions, lack subject matter jurisdiction, anti trust law, overbreadth, proceedings, state-court, decisions, licensed

## LexisNexis® Headnotes

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Legal Ethics > Sanctions > Disciplinary Proceedings > Hearings

[\*\*HN1\*\*](#)  **Disciplinary Proceedings, Hearings**

See Okla. R. Disc. Proc. 6.7, Okla. Stat. tit. 5, ch. 1, app. 1-A.

Legal Ethics > Practice Qualifications

[\*\*HN2\*\*](#)  **Legal Ethics, Practice Qualifications**

Ariz. Sup. Ct. R. 33(d) provides that a member in good standing of the bar of another State may be admitted to appear pro hac vice in Arizona upon approval by the court hearing the matter.

Legal Ethics > Practice Qualifications

[\*\*HN3\*\*](#)  **Legal Ethics, Practice Qualifications**

Ariz. Sup. Ct. R. 34 lists the requirements for admission to the State Bar of Arizona, which include passing the bar examination and being certified by the Committee on Character and Fitness as possessing good moral character.

Civil Procedure > ... > Jurisdiction on Certiorari > Considerations Governing Review > State Court Decisions

[\*\*HN4\*\*](#)  **Considerations Governing Review, State Court Decisions**

The Rooker-Feldman doctrine's applicability is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > State Court Review

Civil Procedure > ... > Jurisdiction on Certiorari > Considerations Governing Review > State Court Decisions

#### **HN5** **Subject Matter Jurisdiction, Jurisdiction Over Actions**

Under Rooker-Feldman, lower federal courts are without subject matter jurisdiction to review state court decisions, and state court litigants may therefore only obtain federal review by filing a petition for a writ of certiorari in the Supreme Court of the United States. The doctrine does not, however, prohibit a plaintiff from presenting a generally applicable legal challenge to a state statute in federal court, even if that statute has previously been applied against him in state court litigation.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Legal Ethics > Sanctions > Disbarments

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

Civil Procedure > ... > Jurisdiction on Certiorari > Considerations Governing Review > State Court Decisions

#### **HN6** **Subject Matter Jurisdiction, Jurisdiction Over Actions**

United States district courts have subject-matter jurisdiction over general challenges to state bar rules, promulgated by state courts in nonjudicial proceedings, which do not require review of a final state-court judgment in a particular case. They do not have jurisdiction, however, over challenges to state-court decisions in particular cases arising out of judicial proceedings even if those challenges allege that the state court's action was unconstitutional. Review of those decisions may be had only in the United States Supreme Court.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

#### **HN7** **Subject Matter Jurisdiction, Jurisdiction Over Actions**

Where subject-matter jurisdiction will involve no arduous inquiry, both expedition and sensitivity to state courts' coequal stature should impel a federal court to dispose of that issue first.

Civil Procedure > Appeals > Standards of Review > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrers & Objections > Motions to Dismiss

**HN8** [down] Appeals, Standards of Review

A circuit court of appeals may affirm a district court's dismissal on any ground supported by the record.

Antitrust & Trade Law > Sherman Act > General Overview

Legal Ethics > Practice Qualifications

Legal Ethics > Sanctions > General Overview

Legal Ethics > Unauthorized Practice of Law

**HN9** [down] Antitrust & Trade Law, Sherman Act

The United States Supreme Court has held that the Sherman Act does not apply to certain categories of state action. One of these categories is the regulation of attorneys by a state supreme court.

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Legal Ethics > Practice Qualifications

Antitrust & Trade Law > Sherman Act > General Overview

Legal Ethics > Unauthorized Practice of Law

**HN10** [down] Scope, Exemptions

Ariz. Sup. Ct. R. 33(d) and 34 are compelled by direction of the State acting as a sovereign and are exempt from Sherman Act challenges.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN11** [down] Public Enforcement, State Civil Actions

The Arizona Uniform State Antitrust Act is interpreted in conformity with the federal antitrust laws.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN12** [down] Public Enforcement, State Civil Actions

See [Ariz. Rev. Stat. § 44-1412](#).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Legal Ethics > Practice Qualifications

Legal Ethics > Sanctions > General Overview

Legal Ethics > Unauthorized Practice of Law

### **HN13** [blue icon] **Public Enforcement, State Civil Actions**

In light of the Arizona legislature's avowed desire to achieve uniformity between the Uniform State Antitrust Act and the federal antitrust laws, the United States Court of Appeals for the Ninth Circuit concludes that the Arizona Supreme Court would most likely hold that its rules governing attorney conduct are not amenable to state law antitrust challenges.

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > Erie Doctrine

Governments > Courts > Judicial Precedent

### **HN14** [blue icon] **Federal & State Interrelationships, Erie Doctrine**

When interpreting state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Civil Procedure > ... > Justiciability > Standing > General Overview

Civil Procedure > ... > Justiciability > Standing > Third Party Standing

Constitutional Law > ... > Case or Controversy > Standing > Third Party Standing

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Standing

Governments > Legislation > Overbreadth

### **HN15** [blue icon] **Judicial & Legislative Restraints, Overbreadth & Vagueness of Legislation**

A plaintiff generally must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties. This limitation is relaxed in the [First Amendment](#) context, however, because when there is a danger of chilling free speech, society's interest in having the statute challenged may outweigh the prudential considerations that normally counsel against third-party standing. A plaintiff's ability to invoke so-called "overbreadth standing" has nothing to do with whether or not his own [First Amendment](#) rights are at stake but instead depends upon whether the plaintiff satisfies the requirement of injury-in-fact, and whether he can be expected satisfactorily to frame the issues in the case.

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

410 F.3d 602, \*602L<sup>A</sup>2005 U.S. App. LEXIS 10407, \*\*1

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom to Petition

## **HN16** [blue speech bubble icon] **Fundamental Freedoms, Freedom of Association**

The right to hire and consult an attorney is protected by the [\*First Amendment's\*](#) guarantee of freedom of speech, association and petition.

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Legal Ethics > Sanctions > General Overview

Legal Ethics > Practice Qualifications

Legal Ethics > Unauthorized Practice of Law

## **HN17** [blue speech bubble icon] **Counsel, Right to Counsel**

While the United States Supreme Court has acknowledged that the right to consult with an attorney falls within the [\*First Amendment's\*](#) purview, the Court has also repeatedly emphasized that the States have broad power to regulate the practice of law. The Court has explained that the interest of the States in regulating lawyers is especially great since lawyers are essential to the primary governmental function of administering justice, and have historically been officers of the courts.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

## **HN18** [blue speech bubble icon] **Judicial & Legislative Restraints, Time, Place & Manner Restrictions**

In order to further its substantial interest in regulating the legal profession, the State of Arizona may institute reasonable time, place, and manner restrictions on Arizonans' [\*First Amendment\*](#) right to consult with an attorney. Time, place, and manner regulations are reasonable provided that the restrictions are justified without reference to the content of the regulated speech, that they are narrowly tailored to serve a significant governmental interest, and that they leave open ample alternative channels for communication of the information.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

## [HN19](#) [blue download icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

The principal inquiry in determining content neutrality is whether the government has adopted a regulation of speech because of disagreement with the message it conveys. Speech restrictions are content-neutral when they can be justified without reference to the content of the regulated speech.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

Legal Ethics > Practice Qualifications

Legal Ethics > Unauthorized Practice of Law

## [HN20](#) [blue download icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

Ariz. Sup. Ct. R. 33(d) and 34 are content-neutral because they impose a generally applicable prohibition on the retention of out-of-state counsel without regard to the subject matter of the representation. (The rules do not, for example, prohibit out-of-state counsel from undertaking only certain categories of representation, such as suits against the State or against tobacco companies).

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

## [HN21](#) [blue download icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

A time, place, and manner regulation is narrowly tailored as long as the substantial governmental interest it serves would be achieved less effectively absent the regulation and the regulation achieves its ends without significantly restricting a substantial quantity of speech that does not create the same evils.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

Governments > Courts > Rule Application & Interpretation

Legal Ethics > Unauthorized Practice of Law

Legal Ethics > Practice Qualifications

## [HN22](#) [blue download icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

The State of Arizona has a significant interest in regulating the practice of law within its boundaries and Ariz. Sup. Ct. R. 33(d) and 34 further that interest by ensuring that attorneys practicing in the State are qualified and possess a familiarity with Arizona law.

**Counsel:** George L. Mothershed, Phoenix, Arizona, argued the cause for the appellant and filed a brief.

LeslieAnn Haacke, Renaud Cook Drury Mesaros, P.A., Phoenix, Arizona, argued the cause for the appellees; Terry Goddard, Attorney General, Phoenix, Arizona, Rosa Mroz, Assistant Attorney General, Phoenix, Arizona, N. Todd McKay, Renaud Cook Drury Mesaros, P.A., Phoenix, Arizona, Charles K. Babb, Assistant Attorney General,

Oklahoma City, Oklahoma, and Allen J. Welch, Oklahoma Bar Association, Oklahoma City, Oklahoma, were on the brief.

**Judges:** Before: Alfred T. Goodwin, Robert R. Beezer, and Diarmuid F. O'Scannlain, Circuit Judges. Opinion by Judge O'Scannlain.

**Opinion by:** Diarmuid F. O'Scannlain

## Opinion

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[\*604] O'SCANNLAIN, Circuit Judge:

We must decide whether a disbarred attorney may collaterally attack his state bar disciplinary proceedings in federal court.

[\*605] I

In 1999, the State Bar of Arizona initiated disciplinary proceedings against George L. Mothershed, an attorney who was licensed by the Oklahoma Bar Association but who lived and [\*2] practiced in Arizona. In response to the disciplinary board's allegation that he had unlawfully practiced law in the State, Mothershed entered a special appearance and moved to dismiss the complaint on the ground that he had not received a summons. The hearing officer denied this motion, and Mothershed subsequently refused to participate further in the disciplinary proceedings. A default judgment was entered against him, and the Supreme Court of Arizona issued an order censuring Mothershed for engaging in the unauthorized practice of law. See *In re Mothershed, No. SB-01-0076-D, 2001 Ariz. LEXIS 63 (2001)*.

The Oklahoma Bar Association thereafter initiated its own disciplinary proceedings against Mothershed. A three-member trial panel found that he had unlawfully practiced law in Arizona, and the Supreme Court of Oklahoma entered an order disbarring him. See *State ex rel. Okla. Bar Ass'n v. Mothershed, 2003 OK 34, 66 P.3d 420, 428 (Okla. 2003)*.

Mothershed responded by filing suit in the United States District Court for the District of Arizona against the Justices of the Oklahoma Supreme Court, the three members of the Oklahoma disciplinary trial panel, [\*3] and several officials of the Oklahoma Bar Association (the "Oklahoma Defendants"). He also sued the Justices of the Arizona Supreme Court, the Clerk of the Arizona Supreme Court, the members of the Arizona Supreme Court Disciplinary Commission, the hearing officer in the Arizona disciplinary proceedings, and a state bar staff counsel (the "Arizona Defendants"). Mothershed alleged that the Arizona disciplinary proceedings were invalid because he had not been served with a summons. He contended that the Oklahoma proceedings were likewise defective because his hearing did not occur between thirty and sixty days after appointment of the trial panel, as required by Rule 6.7 of the Oklahoma Rules Governing Disciplinary Proceedings.<sup>1</sup> Based upon these alleged procedural shortcomings, Mothershed asserted a claim under 42 U.S.C. § 1983 for due process and other constitutional violations, as well as state law tort claims for interference with contractual relationships, defamation, abuse of process, malicious prosecution, false light, and intentional infliction of emotional distress.

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<sup>1</sup> The rule provides:

**HN1** [The Chief Master or Vice-Chief Master of the Professional Responsibility Tribunal shall notify the respondent and the General Counsel of the appointment and membership of the Trial Panel and of the time and place for hearing, which shall not be less than thirty (30) nor more than sixty (60) days from the date of appointment of the Trial Panel. Extensions of this period may be granted by the Chief Master (or the Vice-Chief Master, in case of the unavailability of the Chief Master) for good cause shown.]

[\*\*4] Mothershed also contended that Arizona Supreme Court *Rules 33(d)* and *34*,<sup>2</sup> which set forth the *pro hac vice* admission requirements for out-of-state attorneys and the standards for admission to the State Bar of Arizona, violate Arizonans' *First Amendment* right to consult with an attorney and contravene both the Sherman Antitrust Act, *15 U.S.C. § 1*, and the Arizona Uniform State Antitrust Act, *ARIZ. REV. STAT. § 44-1402*. Mothershed requested damages totaling more than \$ 330 million [\*606] and an injunction reinstating his membership in the Oklahoma Bar Association and prohibiting the defendants from interfering with his Arizona law practice.

[\*\*5] After the defendants moved to dismiss the complaint on various grounds, the district court dismissed the Oklahoma defendants due to the absence of personal jurisdiction. The court later dismissed the claims against the Arizona defendants on the ground that Mothershed was improperly seeking review of the Arizona bar disciplinary proceedings in a lower federal court and that subject matter jurisdiction was therefore absent under the *Rooker-Feldman* doctrine. Mothershed timely appealed.

## II

In the face of growing judicial uncertainty about [HN4](#)<sup>↑</sup> the *Rooker-Feldman* doctrine's parameters, the Supreme Court recently reiterated that its applicability "is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments." *Exxon Mobil Corp. v. Saudi Basic Indus. Corp.*, 544 U.S. 280, 161 L. Ed. 2d 454, 125 S. Ct. 1517, 1521-22 (2005); see also *Rooker v. Fid. Trust Co.*, 263 U.S. 413, 416, 68 L. Ed. 362, 44 S. Ct. 149 (1923); *D.C. Court of Appeals v. Feldman*, 460 U.S. 462, 486-87, 75 L. Ed. 2d 206, 103 S. Ct. 1303 (1983). [\*6]

We must therefore decide whether Mothershed's claims fall within the *Rooker-Feldman* doctrine's narrowed scope.

### A

[HN5](#)<sup>↑</sup> Under *Rooker-Feldman*, lower federal courts are without subject matter jurisdiction to review state court decisions, and state court litigants may therefore only obtain federal review by filing a petition for a writ of certiorari in the Supreme Court of the United States. See *Rooker*, 263 U.S. at 416 (holding that a federal district court lacked subject matter jurisdiction over a suit that effectively sought review of an Indiana state court's decision); *Feldman*, 460 U.S. at 486-87 (holding that a federal district court was without subject matter jurisdiction to entertain a challenge to a decision of the District of Columbia Court of Appeals); see also 28 U.S.C. § 1257 ("Final judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court by writ of certiorari . . . ."). The doctrine does not, however, prohibit a plaintiff from presenting a generally applicable legal challenge to a state statute in federal court, even if that statute [\*7] has previously been applied against him in state court litigation.

This distinction is well illustrated by the *Feldman* decision itself. There, two aspiring attorneys had petitioned the District of Columbia Court of Appeals for a waiver of a D.C. bar rule requiring applicants to have graduated from an accredited law school. *Feldman*, 460 U.S. at 466. After the Court of Appeals denied their petitions, the plaintiffs filed suit in federal district court challenging both the D.C. bar rule's general constitutionality and the District of Columbia court's decision in their particular cases. *Id.* at 468, 472. The Supreme Court held that the district court possessed subject matter jurisdiction over the former claim but not the latter. *Id.* at 486-87. The Court explained:

[HN6](#)<sup>↑</sup> United States district courts . . . have subject-matter jurisdiction over general challenges to state bar rules, promulgated [\*607] by state courts in nonjudicial proceedings, which do not require review of a final state-court judgment in a particular case. They do not have jurisdiction, however, over challenges to state-court

<sup>2</sup> [HN2](#)<sup>↑</sup> *Rule 33(d)* provides that a member in good standing of the bar of another State may be admitted to appear *pro hac vice* in Arizona upon approval by the court hearing the matter. [HN3](#)<sup>↑</sup> *Rule 34* lists the requirements for admission to the State Bar of Arizona, which include passing the bar examination and being certified by the Committee on Character and Fitness as possessing good moral character.

decisions in particular cases arising out of [\*\*8] judicial proceedings even if those challenges allege that the state court's action was unconstitutional. Review of those decisions may be had only in this Court.

*Id. at 486*; see also *id. at 482 n.16* ("Orders of a state court relating to the admission, discipline, and disbarment of members of its bar may be reviewed only by the Supreme Court of the United States on certiorari to the state court, and not by means of an original action in a lower federal court." (quoting *MacKay v. Nesbett*, 412 F.2d 846, 846 (9th Cir. 1969)) (alteration in original)).

Similarly, in *Craig v. State Bar of California*, 141 F.3d 1353, 1354 (9th Cir. 1998) (per curiam), the plaintiff filed a § 1983 claim in federal court against the California bar after the state supreme court denied review of the California Committee of Bar Examiners' refusal to modify the new-attorney oath to comport with his religious beliefs. We held that subject matter jurisdiction was absent because the plaintiff was seeking review of his individual claim and did not present a general challenge to the California bar's policy. *Id.* We reasoned that a

plaintiff [\*\*9] can challenge the state supreme court's denial of bar admission to a particular applicant, the validity of the state's rules governing admission, or both. Lower federal courts lack subject matter jurisdiction over the first type of challenge . . . . In contrast, a general attack on a state's admissions rules may be heard by lower federal courts because a state supreme court acts in a nonjudicial capacity when it promulgates such rules.

*Id.* (citation omitted).

## B

Mothershed alleges that the Oklahoma defendants denied him due process and committed various state law torts because the Oklahoma bar disciplinary panel did not hold its hearing within the thirty-to-sixty-day time frame required by Rule 6.7 of the Rules Governing Disciplinary Proceedings. Because Mothershed does not contend that Rule 6.7 is systematically disregarded in all attorney disciplinary proceedings or that the rule is itself facially invalid, he is not asserting a "general challenge[] to [a] state bar rule[]." *Feldman*, 460 U.S. at 486. Rather, Mothershed is alleging that the Oklahoma defendants failed to apply Rule 6.7 during his own state bar disciplinary hearing, which constitutes [\*\*10] a "challenge[] to [a] state-court decision[] in [a] particular case[]." *Id.* Under the *Rooker-Feldman* doctrine, the district court lacked subject matter jurisdiction to review Mothershed's Oklahoma disciplinary proceedings, and we therefore affirm the dismissal of the Oklahoma defendants.<sup>3</sup>

## [\*\*11] C

Mothershed's claims premised upon the alleged absence of a summons directing him to appear at the Arizona disciplinary [\*608] hearing are likewise barred by the *Rooker-Feldman* doctrine because these claims constitute a particularized challenge to the Arizona disciplinary proceedings' results. The district court therefore correctly concluded that it lacked subject matter jurisdiction over Mothershed's § 1983 and state law tort claims against the Arizona defendants, all of which are premised upon his failure to receive a summons.

## D

Mothershed also alleges, however, that the admission requirements set forth in Arizona Supreme Court *Rules 33(d)* and *34* violate Arizonans' *First Amendment* right to consult an attorney of their choosing and contravene both the Sherman Antitrust Act and the Arizona Uniform State Antitrust Act. These claims pertain to the rules' validity as

<sup>3</sup>The district court's dismissal of the Oklahoma defendants was premised upon the absence of personal jurisdiction, not subject matter jurisdiction. *HN7* Where "subject-matter jurisdiction will involve no arduous inquiry," however, "both expedition and sensitivity to state courts' coequal stature should impel the federal court to dispose of that issue first." *Ruhrgas AG v. Marathon Oil Co.*, 526 U.S. 574, 587-88, 143 L. Ed. 2d 760, 119 S. Ct. 1563 (1999). Here, the subject matter jurisdiction inquiry involves a straightforward application of the *Rooker-Feldman* doctrine, and we accordingly adhere to the Supreme Court's admonition by relying upon the lack of subject matter jurisdiction to dismiss the Oklahoma defendants.

applied to all attorneys within Arizona (and, indeed, all Arizona residents) and thus do not present an individualized challenge to Mothershed's bar disciplinary proceedings. Rather--like the *Feldman* plaintiffs' general constitutional attack on the D.C. bar's accreditation requirement--these claims constitute [\*\*12] a general challenge to the rules governing admission to the Arizona bar. See *Hoover v. Ronwin*, 466 U.S. 558, 564-65, 80 L. Ed. 2d 590, 104 S. Ct. 1989 (1984) (entertaining a Sherman Act challenge to the Arizona bar exam's grading methodology brought by an attorney who had earlier contested his own exam results in separate Arizona state court proceedings).

Because "a general attack on a state's admissions rules may be heard by lower federal courts," *Craig*, 141 F.3d at 1354, the district court erred by concluding that it lacked subject matter jurisdiction over Mothershed's *First Amendment* and antitrust claims against the Arizona defendants.

### III

Although the district court did indeed possess subject matter jurisdiction over Mothershed's general challenges to the Arizona Supreme Court rules, [HN8](#)[<sup>1</sup>] we "may affirm the district court's dismissal on any ground supported by the record." *Wolfe v. Strankman*, 392 F.3d 358, 362 (9th Cir. 2004). We first consider Mothershed's antitrust claims and then turn to his *First Amendment* challenge.

#### A

In *Parker v. Brown*, 317 U.S. 341, 352, 87 L. Ed. 315, 63 S. Ct. 307 (1943), [HN9](#)[<sup>1</sup>] the Supreme Court held that the Sherman Act does [\*\*13] not apply to certain categories of state action. Later decisions have held that one of these categories is the regulation of attorneys by a state supreme court. In *Bates v. State Bar of Arizona*, 433 U.S. 350, 359, 53 L. Ed. 2d 810, 97 S. Ct. 2691 (1977), for example, the plaintiffs alleged that an Arizona bar disciplinary rule prohibiting advertising by attorneys violated the Sherman Act. The Court determined that the Arizona Supreme Court--not the state bar--was the "real party in interest." *Id. at 361*. That court had "adopted the rules," *id.*, and was "the ultimate body wielding the State's power over the practice of law," *id. at 360*. Because the advertising restrictions were "compelled by direction of the State acting as a sovereign," *id.* (internal quotation marks omitted), they were not amenable to a Sherman Act challenge.

Likewise, in *Hoover v. Ronwin*, 466 U.S. at 565, a plaintiff who had failed the Arizona bar exam filed suit against the members of the Committee on Examinations and Admissions alleging that the manner in which they graded the exam violated the Sherman Act. Although the individual members of the Committee [\*\*14] were [\*609] the named defendants, the Court concluded that the suit was barred by *Parker*'s state-action exception because the "Arizona Supreme Court necessarily delegated the administration of the admissions process to the Committee . . . and retained the sole authority to determine who should be admitted to the practice of law in Arizona." *Id. at 573*. Accordingly, the conduct being "challenge[d] was in reality that of the Arizona Supreme Court." *Id.*; cf. *Goldfarb v. Va. State Bar*, 421 U.S. 773, 790, 44 L. Ed. 2d 572, 95 S. Ct. 2004 (1975) (holding that a minimum fee schedule enforced by the Virginia state bar did not fall within the *Parker* exception because the fee schedule was not mandated by the Virginia Supreme Court and thus it could not "fairly be said that the State of Virginia through its Supreme Court Rules required the anticompetitive activities").

Here, Mothershed alleges that Arizona Supreme Court *Rules 33(d)* and 34 violate the Sherman Act. These claims are squarely foreclosed by *Bates* and *Hoover*. Although Mothershed's claim is nominally against certain state bar officials and the Supreme Court Justices in their individual capacities, it [\*\*15] is the Supreme Court of Arizona that is the "real party in interest" because the state bar rules that Mothershed is challenging are promulgated by the court in its supervisory role over the practice of law in Arizona. See *In re Shannon*, 179 Ariz. 52, 876 P.2d 548, 571 (Ariz. 1994) ("the determination of who shall practice law in Arizona and under what condition is a function placed by the state constitution in this court" (internal quotation marks omitted)). [HN10](#)[<sup>1</sup>] *Rules 33(d)* and 34 are therefore "compelled by direction of the State acting as a sovereign," *Bates*, 433 U.S. at 360 (internal quotation marks omitted), and are exempt from Sherman Act challenges.

#### B

Mothershed also asserts a state antitrust claim under Arizona law. [HN11](#) [↑] The Arizona Uniform State Antitrust Act "is interpreted in conformity with the federal [antitrust laws]." [Arizona v. Maricopa County Med. Soc'y, 643 F.2d 553, 554 n.1 \(9th Cir. 1980\)](#), *rev'd on other grounds*, [457 U.S. 332, 73 L. Ed. 2d 48, 102 S. Ct. 2466 \(1982\)](#); see also [Wedgewood Inv. Corp. v. Int'l Harvester Co.](#), 126 Ariz. 157, 613 P.2d 620, 623 (Ariz. Ct. App. 1979) ("The Arizona legislature clearly [\*\*16] intended to strive for uniformity between federal and state antitrust laws."). Indeed, [ARIZ. REV. STAT. § 44-1412](#) explicitly provides, [HN12](#) [↑] "It is the intent of the legislature that in construing [the Uniform State Antitrust Act], the courts may use as a guide interpretations given by the federal courts to comparable federal antitrust statutes." Cf. [Bunkers Glass Co. v. Pilkington PLC, 206 Ariz. 9, 75 P.3d 99, 102, 106 \(Ariz. 2003\)](#) (acknowledging the federal antitrust laws' general "importance" to the interpretation of the Uniform State Antitrust Act, while also observing that Arizona courts need not "rigidly follow federal precedent on every issue of antitrust law regardless of whether differing concerns and interests exist in the state and federal systems").

No court has previously had occasion to consider whether there exists a state-action exception to the Arizona antitrust laws. Nevertheless, [HN13](#) [↑] in light of the Arizona legislature's avowed desire to achieve uniformity between the Uniform State Antitrust Act and the federal antitrust laws, the Arizona Supreme Court would most likely follow *Bates* and *Hoover* and hold that its rules [\*\*17] governing attorney conduct are not amenable to state law antitrust challenges. See [Assurance Co. of Am. v. Wall & Assocs. LLC of Olympia, 379 F.3d 557, 560 \(9th Cir. 2004\)](#) [HN14](#) [↑] ("When interpreting [\*610] state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue . . ." (internal quotation marks and citation omitted)). Mothershed's state law antitrust claim therefore fails for the same reason as its federal counterpart.

C

Mothershed contends that Arizona Supreme Court *Rules 33(d)* and *34* violate the [First Amendment](#) right of Arizonans to consult with a lawyer of their choosing. Because Mothershed does not allege that he has himself suffered a [First Amendment](#) injury, we must first determine whether he has standing to pursue this claim on behalf of other Arizonans.

1

[HN15](#) [↑] A "plaintiff generally must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties." [Warth v. Seldin, 422 U.S. 490, 499, 45 L. Ed. 2d 343, 95 S. Ct. 2197 \(1975\)](#). This limitation is relaxed in the [First Amendment](#) [\*\*18] context, however, because "when there is a danger of chilling free speech, . . . society's interest in having the statute challenged" may outweigh the prudential considerations that normally counsel against third-party standing. [Sec'y of State v. Joseph H. Munson Co., 467 U.S. 947, 956, 81 L. Ed. 2d 786, 104 S. Ct. 2839 \(1984\)](#). A plaintiff's ability to invoke so-called "overbreadth standing" "has nothing to do with whether or not [his] own [First Amendment](#) rights are at stake" but instead depends upon whether the plaintiff "satisfies the requirement of 'injury-in-fact,' and whether [he] can be expected satisfactorily to frame the issues in the case." *Id. at 958*; see also [Gospel Missions of Am. v. City of Los Angeles, 328 F.3d 548, 554 \(9th Cir. 2003\)](#) ("the requirements of 'overbreadth standing' [are] injury-in-fact and the ability to frame the issues in the case satisfactorily").

In [Secretary of State v. Joseph H. Munson Co., 467 U.S. at 950](#), for example, a for-profit company that charged charities a fee for raising funds on their behalf brought a [First Amendment](#) challenge to a Maryland statute that prevented charities from paying [\*\*19] more than 25% of their funds as expenses. Although the plaintiff was not itself a charity and did not allege that its own [First Amendment](#) rights were infringed, *id. at 955*, the Court concluded that the company had overbreadth standing to pursue the claim. The Court reasoned that, as a result of the statute, charities were reluctant to contract with the plaintiff because it charged fees in excess of 25% and that the plaintiff's impetus to challenge the statute was therefore consonant with the charities' [First Amendment](#) interests. *Id. at 958* ("The activity sought to be protected is at the heart of the business relationship between Munson and its clients, and Munson's interests in challenging the statute are completely consistent with the [First Amendment](#) interests of the charities it represents."); see also [Clark v. City of Lakewood, 259 F.3d 996, 1010-11 \(9th Cir. 2001\)](#) (holding that the

owner of an adult entertainment establishment had overbreadth standing to pursue a [First Amendment](#) challenge against provisions of an ordinance that required the employees of such establishments to obtain a license because the licensing scheme--although [\[\\*\\*20\]](#) not directly applicable to the owner--threatened his business's viability).

Here, Mothershed alleges that the prohibitions embodied in *Rules 33(d)* and *34* have a chilling effect upon Arizonans' [\[\\*611\]](#) purported [First Amendment](#) right to consult with out-of-state counsel. Like the plaintiff in *Munson*, Mothershed--though not alleging any [First Amendment](#) harm to himself--has incurred a financial injury because these rules prevent him from practicing law in the State. Mothershed's violation of these provisions has also resulted in his being censured by the Arizona Supreme Court. Moreover, Mothershed has a strong interest in obtaining the invalidation of *Rules 33(d)* and *34* because he desires to practice law in Arizona without being admitted to the state bar. Mothershed therefore satisfies our requirements for overbreadth standing because he has suffered an injury-in-fact and can be expected to pursue the [First Amendment](#) claim vigorously. See *id. at 1011* (concluding that the owner of the adult entertainment establishment could "satisfactorily frame the issues in the case" because he "ha[d] a vested interest in having the [licensing] Ordinance over-turned").

2

Although [\[\\*\\*21\]](#) the [First Amendment's](#) applicability in the area of lawyer-client relations is not well-defined, we recognize that--at least as a general matter--[HN16](#)<sup>↑</sup> the "right to hire and consult an attorney is protected by the [First Amendment's](#) guarantee of freedom of speech, association and petition." *Denius v. Dunlap*, 209 F.3d 944, 953 (7th Cir. 2000); see also *United Mine Workers of Am. v. Ill. State Bar Ass'n*, 389 U.S. 217, 221-22, 19 L. Ed. 2d 426, 88 S. Ct. 353 (1967) (holding that a union had a [First Amendment](#) right to employ a salaried attorney to represent members pursuing workers' compensation claims); *DeLoach v. Bevers*, 922 F.2d 618, 620 (10th Cir. 1990) ("The right to retain and consult an attorney . . . implicates . . . clearly established [First Amendment](#) rights of association and free speech.").

[HN17](#)<sup>↑</sup> While the Supreme Court has acknowledged that the right to consult with an attorney falls within the [First Amendment's](#) purview, the Court has also repeatedly emphasized that "the States have broad power to regulate the practice of law." *Ill. State Bar Ass'n*, 389 U.S. at 222. The Court has explained that the "interest of the States in regulating [\[\\*\\*22\]](#) lawyers is especially great since lawyers are essential to the primary governmental function of administering justice, and have historically been 'officers of the courts.'" *Goldfarb*, 421 U.S. at 792.

[HN18](#)<sup>↑</sup> In order to further its substantial interest in regulating the legal profession, the State of Arizona may institute reasonable time, place, and manner restrictions on Arizonans' [First Amendment](#) right to consult with an attorney. Time, place, and manner regulations are reasonable provided that "the restrictions 'are justified without reference to the content of the regulated speech, that they are narrowly tailored to serve a significant governmental interest, and that they leave open ample alternative channels for communication of the information.'" *Kuba v. 1-A Agric. Ass'n*, 387 F.3d 850, 858 (9th Cir. 2004) (quoting *Ward v. Rock Against Racism*, 491 U.S. 781, 791, 105 L. Ed. 2d 661, 109 S. Ct. 2746 (1989) (internal quotation marks omitted)).

[HN19](#)<sup>↑</sup> "The principal inquiry in determining content neutrality . . . is whether the government has adopted a regulation of speech because of disagreement with the message it conveys. Speech restrictions are content-neutral [\[\\*\\*23\]](#) when they can be justified without reference to the content of the regulated speech." *Honolulu Weekly, Inc. v. Harris*, 298 F.3d 1037, 1043 (9th Cir. 2002) (internal quotation marks and citation omitted). [HN20](#)<sup>↑</sup> Arizona Supreme Court *Rules 33(d)* and *34* are content-neutral because they impose a generally applicable [\[\\*612\]](#) prohibition on the retention of out-of-state counsel without regard to the subject matter of the representation. (The rules do not, for example, prohibit out-of-state counsel from undertaking only certain categories of representation, such as suits against the State or against tobacco companies).

[HN21](#)<sup>↑</sup> A time, place, and manner regulation is narrowly tailored as long as the substantial governmental interest it serves "would be achieved less effectively absent the regulation and the regulation achieves its ends without . . . significantly restricting a substantial quantity of speech that does not create the same evils." *Galvin v. Hay*, 374 F.3d 739, 753 (9th Cir. 2004) (internal quotation marks omitted; alteration in original). As already noted, [HN22](#)<sup>↑</sup> the State of Arizona has a significant interest in regulating the practice of law within its boundaries, see [\[\\*\\*24\]](#)

Bates, 433 U.S. at 361 ("the regulation of the activities of the bar is at the core of the State's power to protect the public"), and Supreme Court *Rules 33(d)* and *34* further that interest by ensuring that attorneys practicing in the State are qualified and possess a familiarity with Arizona law. The rules' narrow tailoring is further evidenced by the fact that they do not impose a blanket prohibition on the appearance of out-of-state attorneys in Arizona courts. Rather, they provide that a qualified out-of-state attorney may be admitted *pro hac vice* by an Arizona court.

Lastly, *Rules 33(d)* and *34* leave open ample alternative channels through which Arizonans can obtain legal representation. Notwithstanding the restrictions on out-of-state attorneys, Arizonans have access to legal representation from the thousands of attorneys licensed by the Arizona bar.

Because Arizona Supreme Court *Rules 33(d)* and *34* are reasonable time, place, and manner regulations of Arizonans' First Amendment right to retain and consult with a lawyer, Mothershed's First Amendment claim fails as a matter of law.

#### IV

For the foregoing reasons, the judgment of the district court is

**AFFIRMED. [\*\*25]**

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End of Document



## **Miller's Pond Co., LLC v. City of New London**

Supreme Court of Connecticut

January 7, 2005, Argued ; June 7, 2005, Officially Released

SC 17166

**Reporter**

273 Conn. 786 \*; 873 A.2d 965 \*\*; 2005 Conn. LEXIS 210 \*\*\*; 2005-1 Trade Cas. (CCH) P74,823

MILLER'S POND COMPANY, LLC, ET AL. v. CITY OF NEW LONDON ET AL.

**Prior History:** [\*\*\*1] Action to recover damages for, inter alia, the defendants' alleged violation of the state antitrust act, and for other relief, brought to the Superior Court in the judicial district of New London, where the case was transferred to the Complex Litigation Docket at Norwich; thereafter, the court, McLachlan, J., granted the defendants' motion for summary judgment and rendered judgment thereon in their favor, from which the plaintiffs appealed.

*[Miller's Pond Co., L.L.C. v. City of New London, 2003 Conn. Super. LEXIS 57 \(Conn. Super. Ct., Jan. 10, 2003\)](#)*

**Disposition:** Reversed; further proceedings.

### **Core Terms**

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pond, immunity, antitrust, municipal, state action, water supply, regulations, water company, antitrust statute, trial court, defendants', department of public health, service area, plans, coordinating, facilities, environmental protection, antitrust liability, wholesale, relevant market, authorization, regional, public water supply, ambulance service, water system, quotation, marks, public utilities commission, water supply system, water authority

### **LexisNexis® Headnotes**

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Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **HN1[] Exemptions & Immunities, Parker State Action Doctrine**

See [Conn. Gen. Stat. § 35-31\(b\).](#)

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Courts > Judicial Precedent

273 Conn. 786, \*786A 873 A.2d 965, \*\*965A 2005 Conn. LEXIS 210, \*\*\*1

## **HN2** [down] **Public Enforcement, State Civil Actions**

See [Conn. Gen. Stat. § 35-44b.](#)

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

Civil Procedure > Judgments > Pretrial Judgments > General Overview

## **HN3** [down] **Pretrial Judgments, Judgment on Pleadings**

A motion for judgment on the pleadings requires a situation where the parties are willing to admit the facts and place their entire case on the legal issues raised, waiving the right to replead if the legal issue is decided against them.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN4** [down] **Public Enforcement, State Civil Actions**

See [Conn. Gen. Stat. § 35-26.](#)

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN5** [down] **Monopolies & Monopolization, Actual Monopolization**

See [Conn. Gen. Stat. § 35-27.](#)

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > Horizontal Market Allocation

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN6** [down] **Price Fixing & Restraints of Trade, Horizontal Refusals to Deal**

See [Conn. Gen. Stat. § 35-28.](#)

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

273 Conn. 786, \*786A 873 A.2d 965, \*\*965A 2005 Conn. LEXIS 210, \*\*\*1

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **[HN7](#)[] Price Fixing & Restraints of Trade, Tying Arrangements**

See [Conn. Gen. Stat. § 35-29.](#)

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **[HN8](#)[] Price Fixing & Restraints of Trade, Tying Arrangements**

Under [Conn. Gen. Stat. § 35-29](#), a "tying arrangement" is an agreement by a party to sell one product but only on the condition that the buyer also purchase a different (tied) product, or at least agree that he will not purchase that product from any other supplier.

Governments > Public Improvements > Sanitation & Water

## **[HN9](#)[] Public Improvements, Sanitation & Water**

See [Conn. Gen. Stat. § 25-33c.](#)

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > Appeals > Standards of Review > Questions of Fact & Law

Civil Procedure > ... > Standards of Review > Plain Error > General Overview

## **[HN10](#)[] Exemptions & Immunities, Parker State Action Doctrine**

The extent to which anticompetitive conduct is specifically directed or required by the government is a mixed question of fact and law. Mixed questions of fact and law are subject to plenary review on appeal.

Civil Procedure > Appeals > Standards of Review > General Overview

Civil Procedure > Appeals > Reviewability of Lower Court Decisions > Preservation for Review

## **[HN11](#)[] Appeals, Standards of Review**

A reviewing court may consider an alternate ground for affirmance that was raised before the trial court.

Governments > Legislation > Interpretation

## **[HN12](#)[] Legislation, Interpretation**

273 Conn. 786, \*786L<sup>873</sup> A.2d 965, \*\*965L<sup>2005</sup> Conn. LEXIS 210, \*\*\*1

In construing statutes, the fundamental objective of the Supreme Court of Connecticut is to ascertain and give effect to the apparent intent of the legislature. That court seeks to determine, in a reasoned manner, the meaning of the statutory language as applied to the facts of the case, including the question of whether the language actually does apply. In seeking to determine that meaning, the court looks to the words of the statute itself, to the legislative history and circumstances surrounding its enactment, to the legislative policy it was designed to implement, and to its relationship to existing legislation and common law principles governing the same general subject matter.

Governments > Legislation > Interpretation

**HN13** [  ] **Legislation, Interpretation**

See [Conn. Gen. Stat. § 1-2z.](#)

Antitrust & Trade Law > Sherman Act > General Overview

**HN14** [  ] **Antitrust & Trade Law, Sherman Act**

See [15 U.S.C.S. § 1.](#)

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

Governments > Local Governments > Claims By & Against

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Governments > Local Governments > Duties & Powers

Governments > Local Governments > Ordinances & Regulations

**HN15** [  ] **Exemptions & Immunities, Parker State Action Doctrine**

Federal case law holds that Parker immunity does not apply directly to local governments. A municipality's restriction of competition may sometimes be an authorized implementation of state policy, and have Parker immunity where that is the case. A municipality that desires Parker immunity must show that, under the state statutory scheme, it has both authority to regulate and authority to suppress competition. A court's inquiry into a municipality's statutory authority to regulate the field in question has been described as not exacting, because whether an ordinance is actually authorized by state statute suggests that as long as the local enactment is within a broad view of the authority granted by the state, whether it is actually violative of that statute is a question for state authorities, not one of federal antitrust law. Moreover, with respect to the municipality's authority to suppress competition despite the requirement of a clear articulation of a state policy to authorize anticompetitive conduct, the statutory authorization need not be explicit; the requirement is met if suppression of competition is the foreseeable result of what the statute authorizes.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN16** [  ] **Exemptions & Immunities, Parker State Action Doctrine**

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Connecticut has its own statutory version of state action immunity in the form of [Conn. Gen. Stat. § 35-31\(b\)](#).

Antitrust & Trade Law > Procedural Matters > Jurisdiction > Primary Jurisdiction

Communications Law > ... > Regulated Entities > Telephone Services > General Overview

Energy & Utilities Law > Antitrust Issues > General Overview

Antitrust & Trade Law > Regulated Industries > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > Utility Companies

Antitrust & Trade Law > Procedural Matters > Jurisdiction > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Courts > Judicial Precedent

## [HN17](#) Jurisdiction, Primary Jurisdiction

The Connecticut Antitrust Act, [Conn. Gen. Stat. § 35-24 et seq.](#), incorporates, in modified form, and with notable exceptions, various provisions of such federal antitrust laws as, for example, the Sherman Act, the Clayton Act, the Antitrust Civil Process Act, and of such state antitrust laws as the provisions embodied in the proposed Uniform State Antitrust Act. Under these circumstances, reference to opinions of courts in other jurisdictions, federal and state, on pertinent **antitrust law** issues, where appropriate, are an aid to interpretation of certain questions arising under the Connecticut statute.

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Energy & Utilities Law > Antitrust Issues > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

Antitrust & Trade Law > Regulated Industries > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > Utility Companies

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Antitrust & Trade Law > Public Enforcement > State Civil Actions

273 Conn. 786, \*786L<sup>873</sup> A.2d 965, \*\*965L<sup>2005</sup> Conn. LEXIS 210, \*\*\*1

Energy & Utilities Law > Utility Companies > Liability

### **HN18** [blue icon] Energy & Utilities, State Regulation

The antitrust exception authorized by [Conn. Gen. Stat. § 35-31\(b\)](#) represents a narrowly drawn version of the doctrine of state action immunity from antitrust liability articulated by the United States Supreme Court in Parker v. Brown. The Court in that case carved out an exemption from Sherman Act liability for activities commanded or directed by a state legislature. [Section 35-31\(b\)](#) limits that holding by purporting to immunize only activities that are specifically required or directed by state or federal statutes.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Criminal Law & Procedure > Trials > Burdens of Proof > Prosecution

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### **HN19** [blue icon] Exemptions & Immunities, Parker State Action Doctrine

Under [Conn. Gen. Stat. § 35-31\(b\)](#), in order to be shielded by qualified state action immunity, a defendant must show that its anticompetitive conduct was specifically directed or required by the government.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Legislation > Interpretation

Governments > Courts > Judicial Precedent

### **HN20** [blue icon] Public Enforcement, State Civil Actions

The legislative history of the Connecticut Antitrust Act, [Conn. Gen. Stat. § 35-24 et seq.](#), clearly establishes that it was intentionally patterned after the [antitrust law](#) of the federal government. Construction of the Act is aided by reference to judicial opinions interpreting the federal antitrust statutes. Accordingly, the Supreme Court of Connecticut follows federal precedent when it interprets the Act unless the text of Connecticut's antitrust statutes, or other pertinent state law, requires the court to interpret it differently.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Governments > Legislation > Statutory Remedies & Rights

Antitrust & Trade Law > ... > Private Actions > Costs & Attorney Fees > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### **HN21** [blue icon] Private Actions, Standing

See [Conn. Gen. Stat. § 35-35](#).

273 Conn. 786, \*786L<sup>873</sup> A.2d 965, \*\*965L<sup>2005</sup> Conn. LEXIS 210, \*\*\*1

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > ... > Private Actions > Costs & Attorney Fees > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

## [HN22](#) [down] **Private Actions, Standing**

See [15 U.S.C.S. § 15](#).

Governments > Legislation > Interpretation

## [HN23](#) [down] **Legislation, Interpretation**

Where statutes contain specific and general references covering the same subject matter, the specific references prevail over the general.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Legislation > Interpretation

Governments > Courts > Judicial Precedent

Governments > Legislation > General Overview

## [HN24](#) [down] **Public Enforcement, State Civil Actions**

Neither the legislative history of [Conn. Gen. Stat. § 35-44b](#) nor the language of the statute as enacted requires: (1) the repeal of antitrust statutes unique to Connecticut, without a parallel provision in the federal scheme; or (2) the overruling of state case law interpreting those statutes that are specific to Connecticut.

Governments > Legislation > Interpretation

## [HN25](#) [down] **Legislation, Interpretation**

The canon--that where statutes contain specific and general references covering the same subject matter, the specific references prevail over the general--is itself a form of extratextual evidence of the meaning of the statute.

Governments > Legislation > Interpretation

## [HN26](#) [down] **Legislation, Interpretation**

While canons certainly do have their place in the construction of statutes, it is unwise to elevate them over all other forms of extratextual evidence because, for almost every maxim found in the "grab bag" of canons, an equal and opposite proposition may be found. Although the so-called canons of statutory construction may at times serve as useful tools in deciphering legislative meaning, to rely on any one of them as a compelling factor in the interpretive process is problematic, because there are two opposing canons on almost every point. The so-called canons are not that, at least in the sense that any one of them reliably can be determined to apply or not to apply in any given

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case. They are, instead, merely guides drawn from experience, to be employed or not to be employed carefully and judiciously, depending on the circumstances. To permit them to displace the conclusions that careful interpretation yields would be a disservice to the legislative process, as well as to the judicial exercise of interpreting legislative language based upon the premise that the legislature intends to enact reasonable public policies.

Governments > Legislation > Interpretation

Governments > State & Territorial Governments > Legislatures

#### **HN27** Legislation, Interpretation

The Connecticut General Assembly is always presumed to know all the existing statutes and the effect that its action or non-action will have upon any one of them, as well as the interpretation that the courts have placed upon one of its legislative enactments and of the effect that its own nonaction, thereafter, may have.

Governments > Legislation > Interpretation

Governments > Courts > Judicial Precedent

#### **HN28** Legislation, Interpretation

The doctrine of stare decisis counsels that a court should not overrule its earlier decisions unless the most cogent reasons and inescapable logic require it. In assessing the force of stare decisis, Connecticut case law has emphasized that courts should be especially cautious about overturning a case that concerns statutory construction.

Governments > Legislation > Expiration, Repeal & Suspension

Governments > Legislation > General Overview

Governments > Legislation > Interpretation

#### **HN29** Legislation, Expiration, Repeal & Suspension

Implied repeal of a statute is not favored and will not be presumed where the old and new statutes can coexist peaceably.

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### **HN30** Market Definition, Relevant Market

Proper analysis in an antitrust case first requires determination of the relevant market. The relevant market for purposes of antitrust litigation is the area of effective competition within which the defendant operates. Market definition generally is a deeply fact-intensive inquiry.

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Governments > Public Improvements > Sanitation & Water

### **HN31** [blue download icon] **Public Improvements, Sanitation & Water**

Conn. Gen. Stat. § 25-33d(c) defines "exclusive service area" as an area where public water is supplied by one system.

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

Civil Procedure > Appeals > Record on Appeal

### **HN32** [blue download icon] **Pretrial Judgments, Judgment on Pleadings**

An appellant bears responsibility for providing an adequate record for review.

Administrative Law > Agency Adjudication > Decisions > Collateral Estoppel

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

Administrative Law > Agency Adjudication > Decisions > Res Judicata

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > Res Judicata

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > Appeals > Standards of Review > Questions of Fact & Law

Real Property Law > Zoning > Judicial Review

### **HN33** [blue download icon] **Decisions, Collateral Estoppel**

Whether a trial court properly granted a motion for summary judgment is a question of law subject to de novo review.

Governments > Public Improvements > Sanitation & Water

### **HN34** [blue download icon] **Public Improvements, Sanitation & Water**

The administrative definition of "available water" includes water supplied by contract, as well as that obtained through active sources. Conn. Agencies Regs. § 25-32d-1a(4). To be "available," however, the contract must not be subject to cancellation or suspension.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

### **HN35** [ ] **Exemptions & Immunities, Parker State Action Doctrine**

The mere pervasiveness of a regulatory scheme does not immunize an industry from antitrust liability for conduct that is voluntarily initiated.

Energy & Utilities Law > Utility Companies > Buying & Selling of Power

Governments > Local Governments > Finance

Energy & Utilities Law > Utility Companies > General Overview

Governments > Legislation > General Overview

Governments > Legislation > Types of Statutes > Special Legislative Acts

Governments > Local Governments > Duties & Powers

Governments > Public Improvements > Sanitation & Water

### **HN36** [ ] **Utility Companies, Buying & Selling of Power**

In Connecticut, regulation of water companies begins at their inception. Water companies may not be formed without a special act of the General Assembly after investigation and a report by the department of environmental protection, the department of public health and the department of public utility control into, inter alia, the proposed company's financial solvency, its water supply system adequacy and potability, and the effect on water supplies of other systems. Conn. Gen. Stat. [§ 2-20a. Conn. Gen. Stat.](#) § 7-234 provides that municipalities may acquire, construct and operate a municipal water supply system where (1) there is no existing private waterworks system, (2) the owner or owners of a private waterworks system are willing to sell or transfer all or part of such system to the municipality, or (3) a public regional waterworks system within said town, city or borough or district is willing to sell or transfer all or part of the system to the municipality. The extensive regulatory scheme is in furtherance of the legislative finding and general statement of policy articulated in [§ 25-33c](#).

Governments > Public Improvements > Sanitation & Water

### **HN37** [ ] **Public Improvements, Sanitation & Water**

See [Conn. Gen. Stat. § 25-33c](#).

Energy & Utilities Law > Utility Companies > General Overview

Environmental Law > Natural Resources & Public Lands > General Overview

Environmental Law > Water Quality > General Overview

Governments > Public Improvements > Sanitation & Water

#### **HN38**[] Energy & Utilities Law, Utility Companies

Connecticut's statutes and regulations envision a significant degree of cooperation, and indeed, regional coordination of water companies. The statutes also envision extensive planning in conjunction with that coordination.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview

#### **HN39**[] Exemptions & Immunities, Parker State Action Doctrine

Generalized statements of policy or implications from the sheer pervasiveness of a regulatory scheme as a whole simply do not have the requisite specificity under [Conn. Gen. Stat. § 35-31\(b\)](#). This is consistent with the ordinary meaning of the word "specific" used in the statute, defined as meaning explicitly set forth, definite, or intended for, applying to, or acting on a particular thing. [Section 35-31\(b\)](#) immunity requires a statute that addresses the challenged conduct directly and explicitly and accordingly is not triggered by implication alone.

Governments > Courts > Judicial Precedent

#### **HN40**[] Courts, Judicial Precedent

Trial court opinions are, although entitled to serious consideration, not binding authority in the Supreme Court of Connecticut.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

#### **HN41**[] Exemptions & Immunities, Parker State Action Doctrine

For purposes of application of the antitrust exemption of [Conn. Gen. Stat. § 35-31\(b\)](#), use of the term "may" does not support the notion that a defendant's action is specifically directed or required by statute.

**Counsel:** Ben A. Solnit, for the appellants (plaintiffs).

Michael P. Carey, with whom was John J. Radshaw III, for the appellees (defendants).

**Judges:** Sullivan, C. J., and Borden, Norcott, Palmer and Vertefeuille, Js. In this opinion BORDEN, PALMER and VERTEFEUILLE, Js., concurred. SULLIVAN, C. J., concurring.

**Opinion by:** NORCOTT

## **Opinion**

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[\*788] [\*\*967] NORCOTT, J. The principal issue in this appeal is whether the trial court properly determined that the defendants, the city of New London (city), the New London water and water pollution control authority (New London water authority), the town of Waterford, and the Waterford water pollution control authority (Waterford water authority), [\*\*968] are immune from antitrust liability under General Statutes § 35-31 (b) [\*\*\*2] <sup>1</sup> because their alleged anticompetitive activities were "specifically directed or required" by statute with respect to the wholesale water market in the New London area. The plaintiffs, Miller's Pond Company, LLC (Miller's Pond Company), Gary Saunders and Thomas Schacht,<sup>2</sup> appeal<sup>3</sup> from the judgment of the trial court following its grant of the defendants' motion for summary judgment. They contend that the trial court improperly: (1) applied § 35-31 (b), which exempts certain activities from the Connecticut Antitrust Act, General Statutes § 35-24 et seq., when those activities are "specifically directed or required by a statute of this state, or of the United States," to the facts of the present case; and (2) granted the defendants' motion for summary judgment because there are unresolved factual issues about the definition of the relevant market. As an alternate ground for affirming the trial court's decision, the defendants contend [\*789] that General Statutes § 35-44b<sup>4</sup> requires us to apply the broader federal case law principles governing state action antitrust immunity that have evolved from the United States Supreme Court decision [\*\*\*3] in Parker v. Brown, 317 U.S. 341, 350-51, 63 S. Ct. 307, 87 L. Ed. 315 (1943). We reverse the judgment of the trial court and remand the case for further proceedings.

[\*\*\*4] The record reveals the following facts and procedural history.<sup>5</sup> The defendants own water sources and water treatment, transmission and distribution facilities that serve the city, Waterford and other parts of southeastern Connecticut; the New London water authority and the Waterford water authority are the "two dominant water utilities" in southeastern Connecticut. The defendants own every source of freshwater and all related supply facilities that are located within their municipal borders and "capable of serving the region," except for Miller's Pond (pond), an approximately seventy-seven acre manmade lake located in the northeastern corner of Waterford. Miller's Pond Company owns and has exclusive riparian rights to the pond, which is served by several tributaries and receives water from a 9.83 square mile [\*969] watershed, making it "the only significant [\*790] untapped surface fresh water reservoir capable of supplying the relevant geographic market served by the defendants." That relevant market consists of the city, Waterford and portions of Montville and East Lyme, and may be expanded to include Groton, Ledyard, Preston and Norwich upon completion of a planned water interconnection loop. [\*\*\*5]

Since 1988, the plaintiffs have been seeking to sell or develop the pond as a water source for utilities in the region or as a private water supply for industrial or [\*\*\*6] recreational facilities. Indeed, in 1998, Miller's Pond Company entered into an agreement with the Connecticut Water Company to develop the sale and distribution of either raw or treated water from the pond in the New London region. The potential market in the region is controlled, however, by the defendants.

<sup>1</sup> General Statutes § 35-31 (b) provides: HN1 [↑] "Nothing contained in this chapter shall apply to those activities of any person when said activity is specifically directed or required by a statute of this state, or of the United States."

<sup>2</sup> Saunders is a founding member of Miller's Pond Company, LLC, and Schacht is a managing member of that company.

<sup>3</sup> The plaintiffs appealed from the judgment of the trial court to the Appellate Court, and upon the unopposed motion of the defendants, we transferred the appeal to this court pursuant to General Statutes § 51-199 (c) and Practice Book § 65-2.

<sup>4</sup> General Statutes § 35-44b provides: HN2 [↑] "It is the intent of the General Assembly that in construing sections 35-24 to 35-46, inclusive, the courts of this state shall be guided by interpretations given by the federal courts to federal antitrust statutes."

<sup>5</sup> For purposes of their motion for summary judgment, the defendants admitted all of the factual allegations in the plaintiffs' complaint. The trial court, therefore, treated the defendants' motion for summary judgment as the equivalent of a common-law motion for judgment on the pleadings. See, e.g., Sewer Commission v. Norton, 164 Conn. 2, 5, 316 A.2d 775 (1972) (stating that HN3 [↑] motion for judgment on pleadings "requires a situation where the parties are willing to admit the facts and place their entire case on the legal issues raised, waiving the right to replead if the legal issue is decided against them" [internal quotation marks omitted]). Accordingly, for purposes of this appeal, we accept as undisputed the facts pleaded in the complaint, and unless otherwise noted, quotations from the record originate from that pleading.

The city previously had supplied water to Waterford from sources owned and controlled by the city until December, 1986, when the long-term supply contract expired. During renegotiations of that agreement, Waterford informed the city that it intended to develop its own water supply system using the pond as the primary water source. The city opposed this plan, and in April, 1988, it imposed a moratorium on new water connections in Waterford, which was to remain in place until Waterford signed a new water service agreement with the city. Thereafter, Waterford abandoned its efforts to supply its water independently and, in October, 1988, it signed a new agreement for a term of forty-eight years (1988 agreement).

The 1988 agreement defined the water supply relationship between the city and Waterford. Its stated purpose is "to provide the terms and conditions pursuant to which (1) [\*\*\*7] the city will supply water to water consumers in [Waterford]; (2) other municipalities in New London County may have the opportunity to receive [\*791] water from the city through the supply facilities, transmission facilities and distribution facilities in [Waterford] and the city; and (3) the city and [Waterford] will negotiate in good faith toward the goal of a regional water and/or sewer system. This agreement provides for the use of the distribution facilities in [Waterford] and for the use of the supply facilities and transmission facilities owned or controlled by the city to provide water to water consumers in [Waterford]." The agreement also states that "the city and [Waterford] will use their best efforts to deter the construction and operation of new independent water systems in the city and [Waterford] respectively."<sup>6</sup> The 1988 agreement defines an "independent water system" as "any private water company or system, private community water system, or private community well serving more than one water consumer."

[\*\*\*8] The city also has an agreement to supply water to portions of the town of Montville. By its terms, the agreement required Montville to enter into a separate agreement with Waterford for the use of Waterford supply facilities needed for the city to deliver water to Montville.<sup>7</sup> Waterford [\*\*970] and Montville entered into this agreement in April, 1990 (1990 agreement). The 1990 agreement has several conditions that, *inter alia*, permit Montville to develop its own water sources only if that "development or purchase does not result in material depletion of any water resources of Waterford [or the [\*792] city] which are presently planned or existing; and . . . does not result in material depletion of any water resources of Waterford or [the city] which come into existence in the future and are located outside of Montville." The pond is the only property not already owned by the defendants that is subject to the restriction in the 1990 agreement, and the plaintiffs claim that the conditions in the 1990 agreement restrict their ability to market the pond to Montville as a regular or emergency water supply.

[\*\*\*9] In regulatory submissions to the department of public health addressing planning matters, both Waterford and the city have recognized the pond as an existing or future component of their water supply systems. The city included the pond in its plan in 1988 as a direct response to a notice from a realtor that the pond might be offered for sale on the open market.

As previously noted, the plaintiffs have been attempting to develop the pond either as a water source for the region or as a private supply for industrial or recreational facilities since 1988. They allege, however, that the defendants have, in accordance with the "best efforts to deter the construction and operation of new independent water systems" clause in the 1988 agreement, interfered with their development efforts in a variety of ways. For example, in December, 1998, the plaintiffs and representatives from the Connecticut Water Company met with the New London water authority and offered to enter into an agreement to sell water to the city. The city rejected this offer and refused to deal; in February, 1999, the chief administrator of the New London water authority threatened to use eminent domain proceedings if the [\*\*\*10] plaintiffs did not sell the pond to the city.<sup>8</sup> In April, 2000, Waterford, in

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<sup>6</sup> The 1988 agreement also provides that, in the event that the city determines that a water shortage exists, Waterford "shall" make available "a suitable additional source of water supply," if possible. If there is no additional source available, the city may refuse to accept new applications for water service in both the city and Waterford until the supply reserves are replenished.

<sup>7</sup> The plaintiffs note that during the negotiation of the 1990 agreement, Waterford refused to allow the Faria Corporation, a major industry in Montville, to have access to water for fire protection purposes.

accordance with [\*793] its officials' understanding of the "best efforts" clause in the agreement, similarly refused to deal with the plaintiffs.

In February, 1998, the city filed an application with the department of environmental protection to divert waters from Hunts Brook, which is located upstream from the pond. Had that department granted this application, it would have reduced the flow of water into the pond by approximately 8 million gallons per day, and reduced the safe yield of the pond by one third. In May, 1998, the plaintiffs announced their intention to develop the pond similarly, and subsequently, in November, 1998, they filed their own [\*\*\*11] application with the department of environmental protection to develop the pond as a regional water supply source and to dredge the valuable sand and gravel deposits from the basin. The department of environmental protection rejected this application without prejudice in October, 1999, because neither the city nor Waterford, as potential users of the water, had agreed to endorse the plaintiffs' application or join it.

In December, 1998, the department of environmental protection informed the city that its diversion application was incomplete, and instructed it to report on alternatives to the diversion of Hunts Brook, including obtaining water from the pond as [\*\*971] well as from other nearby towns such as Groton and Norwich.<sup>9</sup> Consistent with the 1988 agreement, the city has continued to refuse to discuss obtaining water from the pond, the plaintiffs or the Connecticut Water Company.

[\*\*\*12] In January, 1999, the plaintiffs attended a public information meeting at Waterford town hall that was held in conjunction with the department of environmental protection permitting process. The day after that meeting, [\*794] the plaintiffs met with Waterford's first selectman, Thomas Sheridan, who informed them of Waterford's desire to purchase the pond. Sheridan told the plaintiffs of Waterford's continued opposition to the development of the pond as an independent water supply. He likewise informed them that they would never be allowed to develop a water business and that "he had the power to put [the] plaintiffs' project 'on hold for two years' with a telephone call to Hartford." Shortly thereafter, in February, 1999, a meeting was held at the department of environmental protection offices in Hartford, attended by department personnel, New London water authority administrator Thomas Bowen, and counsel. Notes from that meeting indicate that Bowen told the department of environmental protection that the city was considering taking the pond by eminent domain.

On February 9, 1999, Bowen wrote on the city's behalf to the Southeast Water Utility Coordinating Committee. He advised the committee [\*\*\*13] of the city's immediate need for water from the pond, as well as the city's and Waterford's interests in purchasing the pond. Bowen mentioned assurances of future supply that the city had made to Montville, as well the defendants' opposition to the existence of another water company, like the plaintiffs' business, in the area.

Several days later, the city and Waterford executed a memorandum of understanding to develop new water sources (memorandum). The memorandum was negotiated through several secret meetings that were held at locations other than regular public facilities, including the dry-cleaning business of the chairman of the New London water authority. This memorandum, drafted in furtherance of the 1988 agreement, states that Waterford "and the city desire to act in a joint and coordinated manner to pursue the acquisition, development, and management of additional new water supply resources," through either direct purchase or the use [\*795] of eminent domain. Early drafts of the memorandum referred specifically to the pond. Subsequent submissions by the city and Waterford to the department of public health continued to refer to the pond as a component of their water systems, but [\*\*\*14] without the plaintiffs' consent. The inclusion of the pond in these supply plans triggers the anticompetitive provision of the Montville agreement, which prevents Montville from doing business with the plaintiffs.

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<sup>8</sup> The New London water authority reiterated its refusal to deal with the plaintiffs at a meeting in May, 2000. The chairman of the water authority told the plaintiffs that "we're the only game in [Waterford]. Forget going into the water business and forget the Connecticut Water Company."

<sup>9</sup> These other sources are located outside the city and Waterford, and are not subject to the 1988 agreement and its deterrence clause.

Thereafter, in May, 2000, the plaintiffs met again with the New London water authority to discuss the city's expressed intention to acquire the pond. The city again declined the plaintiffs' offer to conduct business respecting the pond's water, and Bowen again reiterated the city's plan to use the power of eminent domain to take the pond if the plaintiffs did not abandon their water business and sell the pond to the city.

[\*\*972] The plaintiffs also state that the city has manipulated market conditions by inflating the available safe yield of water. This market manipulation was done in accordance with the terms of the 1988 agreement that restricted Waterford's ability to seek water source supplies beyond those provided by the city, particularly by conditioning that ability on the city's unilateral declaration of a supply shortage. See footnote 6 of this opinion. Shortly after the execution of the 1988 agreement, the city increased its declared figure for safely available water [\*\*\*15] by 30 percent, from 5.4 million gallons per day to 7 million gallons per day. Both the department of environmental protection and the department of public health have challenged the accuracy of this figure, and an independent department of environmental protection study conducted in April, 1991, calculated that only 5.1 million gallons per day were available as a safe yield. Engineering standards at that time would have justified the declaration of a supply emergency, thus opening up a supply market into which the plaintiffs could have [\*796] competed. The department of public health ordered the city to conduct additional studies, which it did not commence until 1999 under the terms of a consent order. In October, 1999, the city reported that 5.7 million gallons of water per day were available, which was "perilously close" to the actual usage of 5.6 million gallons per day. The city did not, however, report this figure to the state because it could have resulted in a moratorium on new water connections and created a market for additional supply. Rather, the city reported another inflated figure of 6.4 million gallons to the department of public health, which remains under continued study.

[\*\*\*16] In August, 2000, the plaintiffs brought this action for damages and injunctive relief, claiming that the defendants' conduct constituted: (1) restraint of trade in violation of General Statutes § 35-26; <sup>10</sup> (2) monopolization in violation of General Statutes § 35-27; <sup>11</sup> (3) "per se" unlawful acts in violation of General Statutes § 35-28; <sup>12</sup> [\*\*\*17] and (4) illegal tying arrangements in violation of General Statutes § 35-29 <sup>13</sup> with [\*\*973] respect to the 1988 and 1990 [\*797] agreements. The defendants subsequently moved for summary judgment.

The trial court, taking [\*\*\*18] as undisputed the facts alleged in the pleadings; see footnote 5 of this opinion; concluded that the defendants were immune from antitrust liability because their activities constituted state action

<sup>10</sup> General Statutes § 35-26 provides: HN4 [↑] "Every contract, combination, or conspiracy in restraint of any part of trade or commerce is unlawful."

<sup>11</sup> General Statutes § 35-27 provides: HN5 [↑] "Every contract, combination, or conspiracy to monopolize, or attempt to monopolize, or monopolization of any part of trade or commerce is unlawful."

<sup>12</sup> General Statutes § 35-28 provides: HN6 [↑] "Without limiting section 35-26, every contract, combination, or conspiracy is unlawful when the same are for the purpose, or have the effect, of: (a) Fixing, controlling, or maintaining prices, rates, quotations, or fees in any part of trade or commerce; (b) fixing, controlling, maintaining, limiting, or discontinuing the production, manufacture, mining, sale, or supply of any part of trade or commerce; (c) allocating or dividing customers or markets, either functional or geographical, in any part of trade or commerce; or (d) refusing to deal, or coercing, persuading, or inducing third parties to refuse to deal with another person."

<sup>13</sup> General Statutes § 35-29 provides: HN7 [↑] "Every lease, sale or contract for the furnishing of services or for the sale of commodities, or for the fixing of prices charged therefor, or for the giving or selling of a discount or rebate therefrom, on the condition or understanding that the lessee or purchaser shall not deal in the services or the commodities of a competitor or competitors of the lessor or seller, shall be unlawful where the effect of such lease or sale or contract for sale or such condition or understanding may be to substantially lessen competition or tend to create a monopoly in any part of trade or commerce and where such goods or services are for the use, consumption or resale in this state."

HN8 [↑] Under § 35-29, a "tying arrangement is an agreement by a party to sell one product but only on the condition that the buyer also purchase a different (tied) product, or at least agree that he will not purchase that product from any other supplier." State v. Hossan-Maxwell, Inc., 181 Conn. 655, 659, 436 A.2d 284 (1980).

under § 35-31 (b). The trial court relied on this court's decision in *Mazzola v. Southern New England Telephone Co.*, 169 Conn. 344, 359, 363 A.2d 170 (1975),<sup>14</sup> [\*\*\*19] which explained § 35-31 (b) as a narrower version of the similar doctrine providing immunity from federal antitrust liability first articulated in *Parker v. Brown, supra*, 317 U.S. 350-51. The trial court found the requisite state action in the statutory scheme that required the municipalities to provide a safe water supply, particularly *General Statutes* § 25-33c.<sup>15</sup> The court concluded that the city opted to be directed by the state statutes [\*798] and regulations when it satisfied the statutory mandate by creating a municipal water system rather than contracting privately for water service. Accordingly, the trial court granted the defendants' motion for summary judgment, and this appeal followed.

On appeal, the plaintiffs claim that the trial court improperly granted the defendants' motion for summary judgment because: (1) a genuine issue of material fact exists as the trial court failed to consider the existence of the relevant wholesale water market and conducted its analysis in the context of the irrelevant, heavily regulated, retail market; and (2) under *Mazzola v. Southern New England Telephone Co., supra*, 169 Conn. 344, the defendants [\*\*\*20] are not entitled to state action immunity under § 35-31 (b) because their conduct was merely approved or acquiesced in by state regulatory agencies, and not "specifically directed or required" by state or federal statutes. The defendants contend otherwise, and they also claim that § 35-44b, as construed in *Vacco v. Microsoft Corp.*, 260 Conn. 59, 793 A.2d 1048 (2002), now requires this court to apply the federal case law principles governing state action immunity that have emerged following *Parker*, which provide for immunity if the municipalities' alleged anticompetitive conduct is a "foreseeable result" of state legislation.

Before we turn to the parties' specific claims, we set forth the proper standard of review. We will engage in plenary review of all issues raised in this appeal, particularly because HN10[↑] the extent to which anticompetitive conduct is "specifically directed or required" by the government is a mixed question of fact and law . . . ." (Citations omitted.) *Westport Taxi Service, Inc. v. Westport Transit District*, 235 Conn. 1, 26, [\*\*974] 664 A.2d 719 (1995); *id.*, 25-26 (declining to review transit district's § 35-31 [b] [\*\*\*21] state action defense to antitrust action because it was not raised in trial court and record was [\*799] insufficient for plain error review); see *Bortner v. Woodbridge*, 250 Conn. 241, 258, 736 A.2d 104 (1999) ("mixed questions of fact and law [are] subject to plenary review on appeal"); see also, e.g., *Craig v. Stafford Construction, Inc.*, 271 Conn. 78, 83, 856 A.2d 372 (2004) (trial court's grant of summary judgment motion); *Barrett v. Montesano*, 269 Conn. 787, 792, 849 A.2d 839 (2004) (statutory interpretation).

I

## WHETHER § 35-44b INCORPORATES THE FEDERAL STATE ACTION DOCTRINE OF PARKER INTO THE ANTITRUST IMMUNITY PROVIDED BY § 35-31 (b)

We first must determine the correct legal standards to apply to the facts pleaded in the complaint, which entails an examination of the interplay, if any, between federal case law, beginning with *Parker v. Brown, supra*, 317 U.S. 341, governing state action immunity, and the statutory state action immunity standard set forth by § 35-31 (b). Indeed, the defendants argue in support of the application of the federal standards that have evolved from the Supreme [\*\*\*22] Court's seminal decision in *Parker*, as an alternate ground for affirming the trial court's judgment.<sup>16</sup> They contend that § 35-44b requires us to construe and apply § 35-31 (b) in accordance with the federal case

<sup>14</sup> The trial court also relied on a pair of state and federal trial court decisions applying § 35-31 (b), both of which were authored by Judge Covello. See generally *Wheelabrator Environmental Systems, Inc. v. Galante*, 136 F. Supp. 2d 21, 2000 WL 863029 (D. Conn. 2001); *Professional Ambulance Service, Inc. v. Blackstone*, 35 Conn. Sup. 136, 400 A.2d 1031 (1978).

<sup>15</sup> *General Statutes* § 25-33c provides: HN9[↑] "The General Assembly finds that an adequate supply of potable water for domestic, commercial and industrial use is vital to the health and well-being of the people of the state. Readily available water for use in public water systems is limited and should be developed with a minimum of loss and waste. In order to maximize efficient and effective development of the state's public water supply systems and to promote public health, safety and welfare, the Department of Public Health shall administer a procedure to coordinate the planning of public water supply systems."

law following *Parker*, rather than under the more restrictive interpretations given it by Connecticut case law and applied by the trial court.

[\*800] The defendants' arguments with respect to [§ 35-44b](#) present an issue of statutory [\*\*\*23] construction. "It is well settled that [HN12](#)<sup>16</sup> in construing statutes, our fundamental objective is to ascertain and give effect to the apparent intent of the legislature." (Internal quotation marks omitted.) [Manifold v. Ragaglia](#), 272 Conn. 410, 419, 862 A.2d 292 (2004). "We seek to determine, in a reasoned manner, the meaning of the statutory language as applied to the facts of [the] case, including the question of whether the language actually does apply. In seeking to determine that meaning, we look to the words of the statute itself, to the legislative history and circumstances surrounding its enactment, to the legislative policy it was designed to implement, and to its relationship to existing legislation and common law principles governing the same general subject matter." (Internal quotation marks omitted.) [Jagger v. Mohawk Mountain Ski Area, Inc.](#), 269 Conn. 672, 679, 849 A.2d 813 (2004). [HN13](#)<sup>17</sup> "The meaning of a statute shall, in the first instance, be ascertained from the text of the statute itself and its relationship to other statutes. If, after examining such text and considering such relationship, the meaning of such text is plain and unambiguous [\*\*\*24] and does not yield absurd or unworkable results, extratextual evidence of the meaning of the statute shall not be considered." [General Statutes § 1-2z](#).

[\*\*975] [Section 35-44b](#), the statute at issue, provides: "It is the intent of the General Assembly that in construing [sections 35-24 to 35-46](#), inclusive, the courts of this state shall be guided by interpretations given by the federal courts to federal antitrust statutes." We now turn to a review of the two potentially conflicting state and federal legal landscapes.

A

#### Federal Antitrust Immunity under *Parker*

In 1943, the United States Supreme Court decided [Parker v. Brown, supra, 317 U.S. 341](#). In *Parker*, a producer [\*801] and packer of raisins had brought an action to enjoin enforcement by the state of California's department of agriculture of a uniform state marketing program that had been promulgated pursuant to state statute. [Id., 344-46](#). The raisin producer claimed that this program violated the [federal constitution's Commerce Clause](#) and the [Sherman Act](#), the federal antitrust statute.<sup>17</sup> [Id., 348-49](#). Addressing the Sherman Act claims, the Supreme Court assumed without [\*\*\*25] deciding that the marketing act would violate the antitrust statutes. [Id., 350](#). Noting federalism concerns, however, the court concluded that the marketing program "derived its authority and its efficacy from the legislative command of the state and was not intended to operate or become effective without that command," and that the Sherman Act "gives no hint that it was intended to restrain state action or official action directed by a state." [Id., 350-51](#). The court then limited its holding, stating that a state could not give individuals Sherman Act immunity "by authorizing them to violate it, or by declaring that their action is lawful . . ." [Id., 351-52](#). ([Citations omitted](#).) Ultimately, the court concluded that "the state in adopting and enforcing the [marketing] program made no contract or agreement and entered into no conspiracy in restraint of trade or to establish monopoly but, as sovereign, imposed the restraint as an act of government which the Sherman Act did not undertake to prohibit." [Id., 352](#).

<sup>16</sup> The trial court, in discussing [Parker v. Brown, supra, 317 U.S. 341](#), stated that it "is interesting to note that this doctrine has evolved through the years; under federal antitrust laws, the defendants' activities would clearly be exempt from liability." Accordingly, it is appropriate for us to consider the defendants' proposed alternate ground for affirmance. See, e.g., [New Haven v. Bonner](#), 272 Conn. 489, 497, 863 A.2d 680 (2005) [HN11](#)<sup>18</sup> (declining to consider alternate ground for affirmance that was not raised before trial court).

<sup>17</sup> The Sherman Act provides in relevant part: [HN14](#)<sup>19</sup> "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. . ." [15 U.S.C. § 1](#).

[\*\*\*26] With respect to the application of state action immunity to municipalities, subsequent decisions of the Supreme Court [HN15](#) have held that "Parker immunity does not apply directly to local governments . . . a municipality's restriction of competition may sometimes be [\*\*802] an authorized implementation of state policy, and have accorded Parker immunity where that is the case." (Citations omitted.) [\*Columbia v. Omni Outdoor Advertising, Inc.\*, 499 U.S. 365, 370, 111 S. Ct. 1344, 113 L. Ed. 2d 382 \(1991\)](#). A municipality that desires Parker immunity must show that, under the state statutory scheme, it has both "authority to regulate" and "authority to suppress competition." [\*Electrical Inspectors, Inc. v. East Hills\*, 320 F.3d 110, 118 \(2d Cir. 2002\)](#), cert. denied sub nom. [\*Islandia v. Electrical Inspectors, Inc.\*](#), 540 U.S. 982, 124 S. Ct. 467, 157 L. Ed. 2d 373 (2003), quoting [\*Columbia v. Omni Outdoor Advertising, Inc.\*, supra, 372](#). The court's inquiry into the municipality's statutory authority to regulate the field in question has been described as "not . . . exacting" because whether an ordinance [\*\*\*27] is "actually authorized by state statute suggests that as long as the local enactment is within a broad view of the authority granted [\*\*976] by the state, whether it is actually violative of that statute is a question for state authorities, not one of federal antitrust law." [\*Electrical Inspectors, Inc. v. East Hills\*, supra, 118-19](#). Moreover, with respect to the municipality's "authority to suppress competition," despite the requirement of a "clear articulation of a state policy to authorize anticompetitive conduct," the statutory authorization need not be "explicit"; the requirement is met "if suppression of competition is the "foreseeable result" of what the statute authorizes." *Id.*, 119, quoting [\*Columbia v. Omni Outdoor Advertising, Inc.\*, supra, 372-73](#), and [\*Hallie v. Eau Claire\*, 471 U.S. 34, 42, 105 S. Ct. 1713, 85 L. Ed. 2d 24 \(1985\)](#).<sup>18</sup>

[\*\*\*28] [\*803] B

#### State Action Immunity under [§ 35-31 \(b\)](#)

[HN16](#) Connecticut has, however, its own statutory version of state action immunity in the form of [§ 35-31 \(b\)](#). [Section 35-31 \(b\)](#) provides: "Nothing contained in this chapter shall apply to those activities of any person when said activity is specifically directed or required by a statute of this state, or of the United States." This statute was first explained by this court in [\*Mazzola v. Southern New England Telephone Co.\*, supra, 169 Conn. 353-54](#), wherein the plaintiff brought an action against the telephone company, claiming antitrust violations resulting from the telephone company's practices with respect to answering machines and message-taking devices. Specifically, the plaintiff challenged the requirement that individuals obtaining such services from sources other than the telephone company were required to purchase or lease "protective link apparatus from the [telephone company] at a monthly charge fixed by the [telephone company]." *Id.*, 353. In *Mazzola*, this court addressed the telephone company's argument that [§ 35-31 \(b\)](#) rendered it immune from antitrust liability because its activities had [\*\*\*29] been approved by the public utilities commission in accordance with the rate-setting procedure prescribed by [General Statutes § 16-19](#). *Id.*, 357-58.

The court began the decision in *Mazzola* by reviewing the origins of the Connecticut antitrust act, noting that [\*804] "enacted in 1971, [HN17](#) the act incorporates, in modified form, and with notable exceptions, various provisions of such federal antitrust laws as, for example, the [Sherman Act](#), the [Clayton Act](#), the [Antitrust Civil Process Act](#), and of such state antitrust laws as the provisions embodied in the proposed [Uniform State Antitrust Act](#). . . . Under these circumstances, reference to opinions of courts in other jurisdictions, federal and state, on [\*\*977] pertinent antitrust law issues, where appropriate, are an aid to our interpretation of certain questions

<sup>18</sup> Indeed, we note that the defendants cite multiple cases wherein municipal water and sewer companies have been held immune from federal antitrust liability under the *Parker* doctrine. See, e.g., [\*Hallie v. Eau Claire\*, supra, 471 U.S. 42](#) (Stating that "it is sufficient that the statutes authorized the city to provide sewage services and also to determine the areas to be served. We think it is clear that anticompetitive effects logically would result from this broad authority to regulate."); [\*McCallum v. Athens\*, 976 F.2d 649, 655 \(11th Cir. 1992\)](#) (concluding that municipal waterworks is immune from antitrust liability in action brought by retail customers because statutes "unequivocally revealed that [state legislature] contemplated that its municipalities might engage in anticompetitive conduct"); [\*Kern-Tulare Water District v. Bakersfield\*, 828 F.2d 514, 519-20 \(9th Cir. 1987\)](#) (concluding that city's refusal to consent to water district's transfer of surplus water to other utilities was "foreseeable within the [statutory] authority of the city to contract for, acquire and hold water rights, to furnish itself and its inhabitants with water, and to sell, lease, exchange, or transfer surplus water"), cert. denied, [\*486 U.S. 1015, 108 S. Ct. 1752, 100 L. Ed. 2d 214 \(1988\)\*](#).

arising under the present Connecticut statute." (Citations omitted.) [\*Id.\*](#), [347-48](#). After first concluding that the Superior Court, rather than the public utilities commission that regulated the telephone company, had primary jurisdiction over the antitrust claims in the case; [\*id.\*](#), [349-52](#); the court turned to the telephone company's [\\*\\*\\*30](#) state action arguments premised on [§ 35-31 \(b\)](#). Contrasting [§ 35-31 \(b\)](#) with other statutory antitrust exceptions, the court noted that [§ 35-31 \(b\)](#) "has no parallel in the federal antitrust statutes," and that "in enacting this provision the Connecticut legislature also did not choose to follow the example set by several other states of specifically and unqualifiedly exempting from antitrust liability the activities of industries and other organizations subject to the supervision of the state regulatory agency equivalent to our public utilities commission." [\*Id.\*](#), [359](#). This court stated that [HN18](#)<sup>↑</sup> "the exception authorized by [§ 35-31 \(b\)](#) represents a narrowly drawn version of the doctrine of 'state action' immunity from antitrust liability articulated by the United States Supreme Court in *Parker v. Brown*, [supra, [317 U.S. 341 at 350 at 350-51, 87 L. Ed. 315](#). The court in that case carved out an exemption from Sherman Act liability for activities 'commanded' or 'directed' by a state legislature. . . . [Section 35-31 \(b\)](#) limits that holding by purporting to immunize only activities which are 'specifically' required or directed by state or federal statutes. [\\*\\*\\*31](#)" (Citation omitted.) [\*Mazzola v. Southern New England Telephone Co., supra, 169 Conn. 359\*](#). After reviewing the facts of *Parker*, this court stated that the "*Parker* doctrine draws a firm line, in short, between activities actually commanded by the state, which are immune from antitrust liability and action merely approved or tolerated." [\*Id.\*](#), [361](#).

The court then reviewed the public utility rate-setting process of [§ 16-19](#), and concluded that "under these circumstances, the role that is statutorily assigned to the [public utilities commission] in rendering effective tariffs proposed by companies such as the defendant amounts to little more than acquiescence in a program originated by the defendant. In no sense, then, can activities of the defendant such as the kind of activities challenged by the plaintiff, purportedly authorized by a tariff filed with and approved by the [public utilities commission], be characterized as 'compelled by direction of the state acting as a sovereign' under the *Parker* doctrine as it has been judicially interpreted. . . . *Nor can such activities consequently be comprehended within the more stringent standards* [\\*\\*\\*32](#) *applicable to exemptions from antitrust liability established by* [\[§ 35-31 \(b\)\]](#)." (Citation omitted; emphasis added.) [\*Id.\*](#), [365-66](#).

This court next mentioned [§ 35-31 \(b\)](#) immunity in the 1995 decision in [\*Westport Taxi Service, Inc. v. Westport Transit District, supra, 235 Conn. 23-27\*](#). Although this court concluded that the issue was not reviewable because it had not been properly raised as a special defense at trial, and the record was not plain error, the court nevertheless briefly discussed in dicta the proper standards for that inquiry. [\*Id.\*](#), [23-25](#). The court cited *Mazzola*, acknowledging that it had interpreted [§ 35-31 \(b\)](#) as more stringent than the federal law, and stated that [HN19](#)<sup>↑</sup> under the statute, "in order to be shielded by qualified state action immunity, the defendant must show that its anti-competitive conduct was 'specifically' [\[\\*806\]](#) directed or required' by the government [\\*\\*978](#) . . . ." (Citation omitted.) [\*Id.\*](#), [25](#).

C

#### Whether [§ 35-44b](#) Requires Incorporation of the Federal Immunity Standards into a [§ 35-31 \(b\)](#) Analysis

This court decided *Westport Tax Service, Inc.*, in 1995, three years after the enactment of [\\*\\*\\*33](#) [§ 35-44b](#), which was cited therein in further support of the proposition that, because [HN20](#)<sup>↑</sup> "the legislative history of the act clearly establishes that it was intentionally patterned after the [antitrust law](#) of the federal government. . . . Our construction of the Connecticut Anti-Trust Act is aided by reference to judicial opinions interpreting the federal antitrust statutes. . . . Accordingly, we follow federal precedent when we interpret the act unless the text of our antitrust statutes, or other pertinent state law, requires us to interpret it differently." (Citations omitted; emphasis added; internal quotation marks omitted.) [\*Id.\*](#), [15-16](#); see also [\*id.\*](#), [15 n.17](#) ("we note that in 1992, the legislature explicitly incorporated into law its intent that the judiciary be guided by interpretations of federal antitrust statutes when it enacted . . . [§ 35-44b](#)"). The text of [§ 35-44b](#) provides: "It is the intent of the General Assembly that in construing [sections 35-24 to 35-46](#), inclusive, the courts of this state shall be guided by interpretations given by the federal courts to federal antitrust statutes."

This court explained [§ 35-44b](#) in detail in [Vacco v. Microsoft Corp., supra, 260 Conn. 60-61](#), [\*\*\*34] wherein the plaintiff brought an action under the [Connecticut Antitrust Act](#) against the defendant, Microsoft Corporation. We concluded that the plaintiff, as an end user licensee of the operating system software manufactured by the defendant, could not maintain a state antitrust action [\*807] under [General Statutes § 35-35](#)<sup>19</sup> because he was not the direct purchaser of the software. [Id., 62-64](#). In so concluding, we noted that [§ 35-35](#) was modeled after the relevant section of the federal Clayton Act, [15 U.S.C. § 15](#),<sup>20</sup> and that the federal courts have interpreted that statute "as precluding an indirect purchaser of goods or services from bringing a private action against the seller who engages in anticompetitive practices in the sale of those goods or services." [Id., 66](#); see also [id., 69](#) (discussing [Illinois Brick Co. v. Illinois](#), [431 U.S. 720, 97 S. Ct. 2061, 52 L. Ed. 2d 707 \[1977\]](#), which "held that an indirect purchaser could not bring an antitrust action and offensively use the pass on theory to recover under . . . the Clayton Act"). We then relied on the legislative history of [\*\*\*35] the Antitrust Act, and specifically the history and text of [§ 35-44b](#), which "make explicit [the legislature's] intent that the judiciary shall interpret the [\*\*979] Antitrust Act in accordance with the federal courts' interpretation of federal [antitrust law](#)." [Vacco v. Microsoft Corp., supra, 72-73](#). We rejected the plaintiff's claim that the adoption of the indirect purchaser rule would render superfluous the text of [§ 35-35](#), because that statute, unlike the parallel provision of the federal Clayton Act, explicitly provides "consumers" with a right of action under the Antitrust Act. [Id., 74-76](#). We noted that the federal precedent with respect to indirect purchasers [\*808] remained persuasive as applied to the plaintiff in Vacco because of other well established federal case law allowing consumers to bring claims under the Clayton Act. [Id., 76](#), citing [Reiter v. Sonotone Corp.](#), [442 U.S. 330, 338-42, 99 S. Ct. 2326, 60 L. Ed. 2d 931 \(1979\)](#). We then concluded that "allowing only those consumers who purchase directly from the antitrust defendant to bring suit under our state [antitrust law](#) ensures that the Antitrust Act remains harmonious with federal antitrust statutes." [\*\*\*36] "<sup>21</sup> [Vacco v. Microsoft Corp., supra, 76-77](#).

[\*\*\*37] We conclude that [§ 35-44b](#) does not require us to incorporate the federal case law defining state action immunity into our construction of [§ 35-31 \(b\)](#). The applicability of [§ 35-44b](#) to the facts and legal landscape of the present case is questionable, at best. First and foremost, state action immunity under the Connecticut Antitrust Act is based on a standard set forth in a specific statutory provision, namely, [§ 35-31 \(b\)](#), while that same immunity under federal law has its origins in case law construing the more generalized provision of the Sherman Act, [15 U.S.C. § 1](#). See, e.g., [Parker v. Brown, supra, 317 U.S. 348-49](#); [Electrical Inspectors, Inc. v. East Hills, supra, 320 F.3d 118](#); see footnote 17 of this opinion for the text of the Sherman Act. Indeed, we have recognized that [§ 35-31 \(b\)](#) "has no parallel in the federal antitrust statutes." <sup>22</sup> [\*\*\*40] [Mazzola v. Southern New England](#)

<sup>19</sup> [General Statutes § 35-35](#) provides: [HN21](#) "The state, or any person, including, but not limited to, a consumer, injured in its business or property by any violation of the provisions of this chapter shall recover treble damages, together with a reasonable attorney's fee and costs."

<sup>20</sup> The relevant provision of the Clayton Act, [15 U.S.C. § 15](#), provides in relevant part: [HN22](#) "(a) Amount of recovery; prejudgment interest

"Except as provided in subsection (b) of this section, any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee. . . ."

<sup>21</sup> In so concluding, we also noted the extensive legislative history behind the failure of numerous "Illinois Brick repealer bills," which attempted to nullify at the state level the United States Supreme Court holding in [Illinois Brick Co. v. Illinois, supra, 431 U.S. 735](#); [Vacco v. Microsoft Corp., supra, 260 Conn. 77-82, 77 n.22](#); as well as the "the inferential value of failed attempts to amend existing laws with respect to the intent of the legislature to acquiesce in prevailing judicial interpretations of such laws." (Internal quotation marks omitted.) [Id., 79](#).

<sup>22</sup> Discussed at oral argument before this court, another example of a federal-state antitrust distinction is Congress' express prohibition on the recovery of damages from a municipality under the Clayton Act, an enactment that has no parallel in the state statutory scheme. See [15 U.S.C. § 35 \(a\)](#) ("no damages, interest on damages, costs, or attorney's fees may be recovered under

Telephone Co., supra, 169 Conn. 359. It is well settled that [HN23](#) [↑] "where statutes contain specific and general references covering the same subject matter, the specific references prevail over the general." [Galvin v. Freedom of Information Commission, 201 Conn. 448, 456, 518 A.2d 64 \(1986\)](#). [\*\*\*38] Moreover, although there is legislative history supporting the defendants' argument that [§ 35-44b](#) was intended to "create one, national body of law,"<sup>23</sup> [\*\*\*41] [HN24](#) [↑] neither that history [\*\*980] nor the language of the statute as enacted requires: (1) the repeal of antitrust statutes unique to our state, without a parallel provision in the federal scheme; or (2) the overruling of state case law interpreting those statutes that are specific to Connecticut.<sup>24</sup> [\*\*\*42] Accordingly, we must conclude that [§ 35-44b](#) [\*810] merely gave legislative imprimatur to what this court had been doing long before its enactment, namely, looking to case law construing relevant federal statutes as persuasive authority. See, e.g., [Westport Taxi Service, Inc. v. Westport Transit District, supra, 235 Conn. 15](#), quoting [State v. Hossan-Maxwell, Inc., 181 Conn. 655, 660, 436 A.2d 284 \(1980\)](#) ("our construction of the Connecticut Antitrust Act is aided by reference to judicial opinions interpreting the federal antitrust statutes" [internal quotation marks omitted]); see [Elida, Inc. v. Harmar Realty Corp., 177 Conn. 218, 226-27, 413 A.2d 1226 \(1979\)](#); [Mazzola v. Southern New England Telephone Co., supra, 348.](#) [\*\*\*39] Indeed, in [Westport Taxi Service, Inc.](#), a case decided after the enactment of [§ 35-44b](#), and citing that statute, this court emphasized that "we follow federal precedent when we interpret the act unless the text of our antitrust statutes, or other pertinent state law, requires us to interpret it differently." [Westport Taxi Service, Inc. v. Westport Transit District, supra, 15-16](#); see also [id., 39-45](#) [\*\*981] (concluding that interpretation of text of Connecticut Antitrust Act as precluding awards of prejudgment interest is

section 4, 4A, or 4C of the Clayton Act [[15 U.S.C. §§ 15, 15a, or 15c](#)] from any local government, or official or employee thereof acting in an official capacity").

<sup>23</sup> We note that the legislative history of [§ 35-44b](#) indicates that the legislature's purpose in enacting that statute was to "mirror what Connecticut has done with unfair trade practices. Under the Connecticut Unfair Trade Practices Act . . . Connecticut looks to Federal Unfair Trade Practices Act, jurisprudence. [[Section 35-44b](#)] would attempt to do the same thing with antitrust law. The goal being to have a single antitrust jurisprudence in the United States. This is vital if corporations are going to be able to make critical decisions about research and development projects, that they may undertake."

"[This is like] corporate ventures in general, where antitrust laws may pose an obstacle. This would allow them to look to a single case law jurisprudence, in order to know whether they're in compliance with our laws or not. Currently, a corporation in Connecticut or elsewhere, may have to look to [fifty] different sets of jurisprudence. This would move towards a national jurisprudence, and I believe it will strongly enhance the international competitiveness of Connecticut, and of American manufacturing and research companies, wherever they may be." 35 H.R. Proc., Pt. 7, 1992 Sess., pp. 2386-87, remarks of Representative Thomas Moukawsher; see also Conn. Joint Standing Committee Hearings, Commerce and Exportation, Pt. 2, 1992 Sess., p. 735, testimony of Joseph Brennan, vice president of legislative affairs for Connecticut Business and Industry Association ("The Connecticut Antitrust Act, however, is inconsistent in its language and its application to federal antitrust law. The possibility of multiple enforcement by agencies applying different standards can create serious problems for businesses engaged in interstate commerce.").

<sup>24</sup> A brief review of the legislation and case law of other states demonstrates that had the legislature desired the wholesale incorporation of federal law into the state scheme, it could have done so. See [Duck Tours Seafari, Inc. v. Key West, 875 So. 2d 650, 653 \(Fla. App. 2004\)](#) ("Under Florida law, 'Any activity or conduct . . . exempt from the provisions of the antitrust laws of the United States is exempt from the provisions of this chapter [542].'" [§ 542.20, Fla. Stat.](#) (1995). Thus, the doctrine of state action immunity which has developed under federal antitrust law is also an available defense to a suit against a municipality for a violation of Florida's antitrust laws."), review denied, Docket No. SC04-1382, [890 So. 2d 1114, 2004 Fla. LEXIS 2183 \(November 22, 2004\)](#); see also [Dill v. Board of County Commissioners, 928 P.2d 809, 815-16 \(Colo. App. 1996\)](#) ("any person exempt or immune under federal antitrust law is exempt from the [Colorado Antitrust Act of 1992](#)"). Moreover, statutes such as [§ 35-44b](#) do not necessarily counsel blind adherence to all things federal. See [Fine Airport Parking, Inc. v. Tulsa, 2003 OK 27, 71 P.3d 5, 10-11 \(Okla. 2003\)](#) (acknowledging statute requiring state antitrust law to "be interpreted and applied consistent with federal antitrust law," but stating that "the principles of federalism supporting the *Parker* doctrine are meaningless in an analysis of municipal liability under [state antitrust statutes]" because "the state is the sovereign and the municipality is a political subdivision of the state").

consistent [\*811] with relevant federal precedent). Accordingly, [§ 35-44b](#) simply is inapplicable in the present case, which concerns a state antitrust statute without federal parallel.<sup>25</sup>

[\*\*\*43] [\*812] Moreover, the [HN27](#)<sup>↑</sup> "the General Assembly is always presumed to know all the existing statutes and the effect that its action or non-action will have upon any one [\*\*982] of them"; (internal quotation marks omitted) [Hatt v. Burlington Coat Factory](#), [263 Conn. 279, 310, 819 A.2d 260 \(2003\)](#); as well as "the interpretation which the courts have placed upon one of its legislative enactments and of the effect that its own nonaction, thereafter may have." (Internal quotation marks omitted.) [State v. Ramos](#), [271 Conn. 785, 797, 860 A.2d 249 \(2004\)](#); id. ("the legislature's failure to act upon our interpretation of [General Statutes] § 29-38 in [State v. Scully](#), [\[195 Conn. 668, 678, 490 A.2d 984 \(1985\)\]](#), suggests that the legislature agrees with it"). Accordingly, we will not torture the language of [§ 35-44b](#) to reach the results, disfavored in our jurisprudence, of overruling past decisions construing [§ 35-31 \(b\)](#), or impliedly repealing that same statute.<sup>26</sup> See, e.g., [Waterbury v. Washington](#), [260 Conn. 506, 538, 800 A.2d 1102 \(2002\)](#) [HN28](#)<sup>↑</sup> ("The doctrine of stare decisis counsels that a court

<sup>25</sup> The concurring opinion concludes that "because [§ 35-31 \(b\)](#) is more specific than [§ 35-44b](#), its terms should prevail in this case. Thus, there is no need to go beyond the plain and unambiguous language of the statute." The concurrence further states that it "sees no need" for much of the analysis herein, including our "lengthy" explanation of how federal antitrust state action immunity relates to Connecticut's antitrust state action immunity. We take this opportunity to express briefly our respectful disagreement with much of the concurrence's analysis.

We first note that the concurring opinion, while professing to follow strictly [§ 1-2z](#), in fact departs from the analysis directed by that statute by invoking the canon of statutory construction that provides, "where statutes contain specific and general references covering the same subject matter, the specific references prevail over the general." [Galvin v. Freedom of Information Commission](#), *supra*, [201 Conn. 456](#). If the statutes at issue were in fact as plain and unambiguous as the concurrence states, resort to [HN25](#)<sup>↑</sup> this canon, which is itself a form of "extratextual evidence of the meaning of the statute"; [General Statutes](#) § [1-2z](#), simply would be unnecessary. Moreover, [HN26](#)<sup>↑</sup> while canons certainly do have their place in the construction of statutes, it strikes us as unwise to elevate them over all other forms of "extratextual evidence" because, for almost every maxim found in the "grab bag" of canons, an equal and opposite proposition may be found. We have stated: "Although the so-called canons of statutory construction may at times serve as useful tools in deciphering legislative meaning, to rely on any one of them as a compelling factor in the interpretive process is problematic, because as Professor Karl Llewellyn persuasively has demonstrated, 'there are two opposing canons on almost every point.' K. Llewellyn, 'Remarks on the Theory of Appellate Decision and the Rules or Canons About How Statutes Are to Be Construed,' 3 Vand. L. Rev. 395, 401 (1950). The so-called 'canons' are not that, at least in the sense that any one of them reliably can be determined to apply or not to apply in any given case. They are, instead, merely guides drawn from experience, to be employed or not to be employed carefully and judiciously, depending on the circumstances. See F. Frankfurter, 'Some Reflections on the Reading of Statutes,' 47 Colum. L. Rev. 527, 544-45 (1947); see also [United Illuminating Co. v. New Haven](#), [240 Conn. 422, 455, 692 A.2d 742 \(1997\)](#). 'To permit them to displace the conclusions that careful interpretation yields . . . would be a disservice to the legislative process, as well as to the judicial exercise of interpreting legislative language based upon the premise that the legislature intends to enact reasonable public policies.' [United Illuminating Co. v. New Haven](#), *supra*, [455](#). [Burke v. Fleet National Bank](#), [252 Conn. 1, 23-24, 742 A.2d 293 \(1999\)](#).

We also disagree with the analysis contained in footnote 3 of the concurring opinion, namely, that "federal [antitrust law](#) pertaining to state action immunity is more lenient than [§ 35-31 \(b\)](#), but is just as specific. The reason that we should not follow federal law in this case is that the provisions of [§ 35-31 \(b\)](#) are more specific than the provisions of [§ 35-44b](#) and, therefore, to the extent that there is a patent inconsistency between the plain language of [§ 35-31 \(b\)](#) and the federal law, the provisions of [§ 35-44b](#) requiring us to follow federal law do not apply." We do not perceive the resolution of this case as turning on whether [§ 35-31 \(b\)](#) is more specific than [§ 35-44b](#), because the statutes fundamentally are different. [Section 35-31 \(b\)](#) is a substantive rule of law pertaining directly to the parties' conduct while, in contrast, [§ 35-44b](#) evinces the legislature's intent with respect to the interpretation of substantive antitrust statutes like [§ 35-31 \(b\)](#). The concurrence's analysis misstates the central issue herein, which is the applicability of [§ 35-44b](#), and to resolve that question, we necessarily must compare [§ 35-31 \(b\)](#) and [15 U.S.C. § 1](#), to ascertain the relevant similarities and differences between the state and federal enactments.

<sup>26</sup> We also note that adoption of the federal standard would diminish the strict construction that we give to the exceptions under [§ 35-31](#), including [§ 35-31 \(b\)](#). [Cheryl Terry Enterprises, Ltd. v. Hartford](#), [270 Conn. 619, 628, 854 A.2d 1066 \(2004\)](#), citing [Mazzola v. Southern New England Telephone Co.](#), *supra*, [169 Conn. 355](#).

should [\*\*\*44] not overrule its earlier decisions unless the most cogent reasons and inescapable logic require it. . . . In assessing the force [\*813] of stare decisis, our case law has emphasized that we should be especially cautious about overturning a case that concerns statutory construction." [Citation omitted; internal quotation marks omitted.]; *Nash v. Yap*, 247 Conn. 638, 648, 726 A.2d 92 (1999) HN29<sup>↑</sup> ("implied repeal of a statute is not favored and will not be presumed where, as here, the old and new statutes can coexist peaceably"). We, therefore, reaffirm the continuing vitality of *Mazzola v. Southern New England Telephone Co., supra*, 169 Conn. 365-66, as the controlling interpretation of a state antitrust statute without a federal parallel, and we decline to consider the evolved state action doctrine of *Parker v. Brown*, *supra*, 317 U.S. 341, as either mandatory or persuasive in the construction and application of § 35-31 (b).

[\*\*\*45] II

## WHETHER THE TRIAL COURT PROPERLY CONCLUDED THAT THE STATUTORY SCHEME "SPECIFICALLY DIRECTED OR REQUIRED" THE DEFENDANTS' ACTIVITIES

Having concluded that § 35-31 (b), as explained by *Mazzola v. Southern New England Telephone Co., supra*, 169 Conn. 361, provides the governing standard to apply in the present case, we now consider whether the trial court applied it properly to the facts pleaded by the plaintiffs when viewed in light of the statutes and regulations governing the activities of municipal water companies. The plaintiffs claim that the defendants are not entitled to immunity under § 35-31 (b) because their conduct with respect to the wholesale water market was not "specifically directed or required" as: (1) they voluntarily subjected themselves to the comprehensive statutory and regulatory scheme governing water companies; (2) regulatory approval or acceptance of water supply contracts and plans by state agencies [\*814] that are not charged with antitrust enforcement does not constitute the required specific statutory command or direction; and (3) the statutory mandate of a "safe and adequate supply of water" under § 25-33c does not satisfy the specificity [\*\*\*46] requirement of § 35-31 (b). The defendants, citing the plethora of statutes and regulations, including § 25-33c, that govern the activities of water companies, contend [\*\*983] in response that their allegedly anticompetitive actions were required by the "totality of [that] mandate . . ." We agree with the plaintiffs.

A

### Definition of the Relevant Market

We note at the outset that HN30<sup>↑</sup> proper analysis in an antitrust case first requires determination of the "relevant market . . ." *AD/SAT v. Associated Press*, 181 F.3d 216, 225 (2d Cir. 1999); id. ("as is frequently the case in antitrust litigation, the court's definition of the relevant market was dispositive"); accord *Westport Taxi Service, Inc. v. Westport Transit District*, *supra*, 235 Conn. 16 ("monopoly power is power to fix or control prices or to exclude or control competition in the relevant market" [internal quotation marks omitted]). "The relevant market for purposes of antitrust litigation is the 'area of effective competition' within which the defendant operates." *AD/SAT v. Associated Press*, *supra*, 227. Market definition generally "is a deeply fact-intensive inquiry [\*\*\*47] . . ." *Todd v. Exxon Corp.*, 275 F.3d 191, 199 (2d Cir. 2001); see also *Hayden Publishing Co. v. Cox Broadcasting Corp.*, 730 F.2d 64, 70 (2d Cir. 1984) ("in our view, there were clearly genuine issues of fact concerning the definition of the relevant market, thus precluding even partial summary judgment").

The plaintiffs contend, both in their brief and at oral argument before this court, that the trial court improperly conducted its state action analysis in a manner that [\*815] implicitly accepted the defendants' argument that, as a factual proposition, the relevant wholesale water market does not exist. The plaintiffs argue that, at the very least, a genuine issue of material fact with respect to the relevant market exists, thereby precluding summary judgment. Our review of the trial court's memorandum of decision shows that the court acknowledged the plaintiffs' claim with respect to the relevant market, but neither ruled on the existence of a distinction between the retail and wholesale markets, nor explained how any such distinction affected its analysis.

Having reviewed the pleadings and factual record in this case in the context of the relevant [\*\*\*48] statutes, we conclude that there is, at the very least, a genuine issue of material fact as to the existence of a wholesale water

market in southeastern Connecticut.<sup>27</sup> [\*\*\*50] The plaintiffs have pleaded their intention to sell water from the pond to other water utilities, including the defendants, in the New London area for subsequent distribution. Moreover, the difference between the wholesale and retail markets was explained by Schacht in an affidavit submitted to the trial court in connection with the defendants' motion for [\*\*984] summary judgment. In that affidavit, Schacht stated that retail customers are individuals or [\*816] businesses that purchase water from individual utility companies through "service connections" to water mains. Wholesale water customers, by contrast, are utility companies themselves, which purchase water in bulk for resale to retail customers. Schacht noted that the retail relationships are compulsory and not subject to competitive market factors because the department of public health designates exclusive service areas, wherein one utility is assigned responsibility for providing retail water service. See also [HN31](#)[<sup>↑</sup>] [General Statutes § 25-33d \(c\)](#) (defining [\*\*\*49] "exclusive service area" as "an area where public water is supplied by one system"). Schacht averred that, in contrast, the wholesale market is voluntary and independent of the exclusive service area system. Accordingly, viewing the relevant market in the light most favorable to the plaintiffs; see, e.g., [Zhang v. Omnipoint Communications Enterprises, Inc.](#), 272 Conn. 627, 633, 866 A.2d 588 (2005); we conclude that our analysis of the relevant statutes and regulations must take place in the context of the wholesale water market.<sup>28</sup>

## B

### The Statutory Scheme Relevant to the Defendants' Activities

Municipalities and other entities in the water business, especially at the retail level, unquestionably are subject to a vast array of statutes and regulations. Nevertheless, [HN35](#)[<sup>↑</sup>] the "mere pervasiveness of a regulatory scheme does not immunize an industry from antitrust liability for conduct that is voluntarily initiated." [MCI Communications Corp. v. American Telephone & Telegraph](#) [<sup>\*</sup>817] Co., 708 F.2d 1081, 1103 (7th Cir.), cert. denied, 464 U.S. 891, 104 S. Ct. 234, 78 L. Ed. 2d 226 (1983); id. ("although the [Federal Communications Commission] has authority to compel interconnection under [47 U.S.C. § 1201\(a\)](#) of [\*\*\*51] the [Federal Communications] Act, the initial decision whether to interconnect rests with the utility, and the record shows that the [Federal Communications Commission] did not control or approve of [the defendant's] actions here"). Accordingly, we must review the bevy of statutes and regulations produced by the defendants in search of the specific direction or requirement that they argue exists.<sup>29</sup>

[HN36](#)[<sup>↑</sup>] Regulation of water companies begins at their inception. Water companies may not be formed without a special act of the General Assembly after investigation and a report by the department of environmental protection, the department of public health and [\*\*\*52] the department of public utility control into, *inter alia*, the proposed company's financial solvency, its water supply system adequacy and potability, and "the effect on water supplies of other systems . . . ." [General Statutes § 2-20a](#); see also [General Statutes § 7-234](#) (municipalities "may acquire,

<sup>27</sup> We note that further explication on this point by the trial court would have greatly aided our review of the market definition issue, and that the better practice would have been for the plaintiffs, who as the [HN32](#)[<sup>↑</sup>] appellants bear responsibility for providing an adequate record for review, to move for an articulation pursuant to [Practice Book § 66-5](#). Nevertheless, the plaintiffs' claim remains reviewable because: (1) the underlying facts are undisputed in light of the trial court's decision to treat the defendants' summary judgment motion as one of judgment on the pleadings; see footnote 5 of this opinion; (2) [HN33](#)[<sup>↑</sup>] whether the trial court properly granted a motion for summary judgment is a question of law subject to de novo review; and (3) the relevant documents are part of the record on appeal. See [Ammirata v. Zoning Board of Appeals](#), 264 Conn. 737, 744-45, 745 n.10, 826 A.2d 170 (2003) (res judicata and collateral estoppel claims); [Niehaus v. Cowles Business Media, Inc.](#), 263 Conn. 178, 185, 819 A.2d 765 (2003) (whether agreement was clear and unambiguous).

<sup>28</sup> We note that the applicable department of public health regulations also contemplate a wholesale market, as [HN34](#)[<sup>↑</sup>] the definition of "available water" includes water supplied by contract, as well as that obtained through "active sources . . . ." [Regs., Conn. State Agencies § 25-32d-1a \(4\)](#). To be "available," however, the contract must not be "subject to cancellation or suspension . . ." Id.

<sup>29</sup> We have reviewed the myriad of statutes and regulations cited by the defendants in the synopsis contained in their appendix, as well as those actually discussed in their brief. We do not, however, discuss *all* of them in this opinion because many are, despite their pervasive verbosity, nevertheless tangential or irrelevant to the issues discussed herein.

construct and operate a municipal water supply system where [1] there is no existing private waterworks system, [2] [\*\*985] the owner or owners of a private waterworks system are willing to sell or transfer all or part of such system to the municipality, or [3] a public regional waterworks system within said town, city or borough or district is willing to sell or transfer all or part of the system to the municipality").<sup>30</sup>

[\*\*\*53] [\*818] The extensive regulatory scheme is in furtherance of the legislative finding and general statement of policy articulated in [§ 25-33c](#), which was mentioned by the trial court,<sup>31</sup> and provides: [HN37](#) "The General Assembly finds that an *adequate supply* of potable water for domestic, commercial and industrial use is vital to the health and well-being of the people of the state. Readily available water for use in public water systems is limited and should be developed with a minimum of loss and waste. In order to maximize efficient and effective development of the state's public water supply systems and to promote public health, safety and welfare, *the Department of Public Health shall administer a procedure to coordinate the planning of public water supply systems.*"<sup>32</sup> (Emphasis [\*\*986] added.) [General Statutes § 25-33c](#). [\*819] Indeed, the regulatory scheme envisioned by the legislature is not toothless, as [General Statutes § 25-32e](#) gives the department of public health the authority to impose civil penalties upon water companies for violations of the water supply statutes and regulations promulgated thereto, as well as "any regulation in the Public [\*\*\*54] Health Code relating to the purity and adequacy of water supplies or to the testing of water supplies or any report of such testing . . ." [General Statutes § 25-32e \(a\)](#).

<sup>30</sup> We note that both the plaintiffs and the defendants engage in extensive discussions of the special act through which the General Assembly established the Southeastern Connecticut Water Authority in 1967. See Special Acts 1967, No. 381. The plaintiffs rely on language in the special act that expressly mentions the authority of the Southeastern Connecticut Water Authority to obtain and sell water at wholesale to water utilities. See Special Acts 1967, No. 381, § 14 (h). The defendants, in contrast, rely on the Southeastern Connecticut Water Authority's eminent domain power, which it received despite concerns of investor-owned water utilities that were expressed in committee hearings. See Special Acts 1967, No. 381, § 14 (c). We conclude that, although this special act supports the plaintiffs' contentions with respect to the distinction between wholesale and retail water markets; see part II A of this opinion; it is otherwise tangential to the present case because it does not provide water companies or municipalities with any relevant powers.

<sup>31</sup> We note that the trial court's decision in the present case cited and quoted only [§ 25-33c](#) in discussing the statutory and regulatory scheme, but acknowledged that the defendants provided it with a comprehensive synopsis of the entire scheme.

<sup>32</sup> Accordingly, the legislature also gives the department of public health jurisdiction over "all matters concerning the purity and adequacy of any water supply source used by any municipality, public institution or water company for obtaining water, the safety of any distributing plant and system for public health purposes, the adequacy of methods used to assure water purity, and such other matters relating to the construction and operation of such distributing plant and system as may affect public health." [General Statutes § 25-32 \(a\)](#).

By way of illustration, the defendants cite several examples of the department of public health's extensive jurisdiction over water companies and their properties, such as the requirement of a written permit for the transfer, lease, assignment or change in the use of watershed lands. See [General Statutes § 25-32 \(b\), \(c\), \(d\)](#) and [\(e\)](#). Moreover, a water company may not agree to sell water reserves in excess of what it needs to provide adequate services without a permit to do so from the department of public health. [General Statutes § 22a-358](#). Similarly, a water company may not abandon a water supply source without approval of the department of public health, which shall not be granted if that source would be necessary in an emergency or "the proposed abandonment would impair the ability of such company to provide a pure, adequate and reliable water supply for present and projected future customers," for fifty years from the date of application. [General Statutes § 25-33k \(c\) \(2\)](#).

Indeed, a water company desiring to sell even a potential or abandoned source of water must notify the department of public health, which shall order that company to notify "other water companies that may reasonably be expected to utilize the source, potential source or abandoned source of its intention and the price at which it intends to sell such source. . ." [General Statutes § 25-33 \(a\)](#). That statute also prescribes a procedure for other water companies to buy that source, and empowers the department of public health to determine who may buy the source if it is desired by multiple water companies. [General Statutes § 25-33l \(b\)](#).

[\*\*\*55] The defendants point out correctly that [HN38](#)<sup>↑</sup> the statutes and regulations do envision a significant degree of cooperation, and indeed, regional coordination of water companies. For example, water utility coordinating committees are required to "prepare a coordinated water system plan in the public water supply management area" that "shall promote cooperation among public water systems," and to submit that plan to the department of public health. [General Statutes § 25-33h \(a\)](#).<sup>33</sup> Indeed, part of this cooperation is avoiding duplication [[\\*820](#)] of service, as directed by [General Statutes § 16-262m](#), which prescribes requirements that must be met before a water company constructs a new water supply system or expands an existing one. To obtain the requisite "certificate of public convenience and necessity for [such] construction or expansion" from the department of public utility control and the department of public health, the departments first must determine that "(1) *no feasible interconnection with an existing system is available to the applicant*, (2) the applicant will complete the construction or expansion in accordance with engineering [[\\*\\*\\*56](#)] standards established by regulation by the Department of Public Utility Control for water supply systems, (3) the applicant has the financial, managerial and technical resources to operate the proposed water supply system in a reliable and efficient manner and to provide continuous adequate service to consumers served by the system, (4) the *proposed construction or expansion will not result in a duplication of water service in the applicable service area* and (5) the applicant meets all federal and state standards for water supply systems . . ." (Emphasis added.) [General Statutes § 16-262m \(b\)](#).

[\*\*\*57] The statutes also envision extensive planning in conjunction with that coordination. Under [General Statutes § 25-32d \(a\)](#),<sup>34</sup> water companies are required to submit [[\\*821](#)] [[\\*\\*987](#)] a water supply plan to the department of public health for approval "with the concurrence of the Commissioner of Environmental Protection."<sup>35</sup> [[\\*\\*\\*59](#)] A water supply plan is required to "evaluate the water supply needs in the service area of the water company submitting the plan and propose a strategy to meet such needs. . ." [General Statutes § 25-32d \(b\)](#). The plan must "include: (1) A description of existing water supply systems; (2) an analysis of future water supply demands; (3) an assessment of alternative water supply sources which may include sources receiving sewage and sources located on state land; (4) contingency procedures for public drinking water supply emergencies, including emergencies concerning the contamination of water, the failure of a water supply system or the shortage of water; (5) a recommendation for new water system development; (6) a forecast of any future land sales, an identification which includes the acreage and location of any land proposed [[\\*\\*\\*58](#)] to be sold, sources of public water supply to be abandoned and any land owned by the company which it has designated, or plans to designate, as class III land; (7) provisions for strategic groundwater monitoring; (8) an analysis of the impact of water conservation practices and a strategy for implementing supply and demand management measures; and (9) on and after January 1, 2004, an evaluation of source water protection measures for all sources of the water supply, based on the identification of

<sup>33</sup> [General Statutes § 25-33h \(a\)](#) provides: "Each water utility coordinating committee shall prepare a coordinated water system plan in the public water supply management area. Such plan shall be submitted to the Commissioner of Public Health for his approval not more than two years after the first meeting of the committee. The plan shall promote cooperation among public water systems and include, but not be limited to, provisions for (1) integration of public water systems, consistent with the protection and enhancement of public health and well-being; (2) integration of water company plans; (3) exclusive service areas; (4) joint management or ownership of services; (5) satellite management services; (6) interconnections between public water systems; (7) integration of land use and water system plans; (8) minimum design standards; (9) water conservation; (10) the impact on other uses of water resources; and (11) acquisition of land surrounding wells proposed to be located in stratified drifts."

<sup>34</sup> [General Statutes § 25-32d \(e\)](#) directs notice and the content thereof to municipalities when water companies submit a plan or revised plan that "involves a forecast of land sales, abandonment of any water supply source, sale of any lands, or land reclassification . . .".

<sup>35</sup> [General Statutes § 25-32d \(d\)](#) requires the department of public health to adopt implementing regulations, "in consultation with" the department of environmental protection and the public utilities control authority, and that "such regulations shall include a method for calculating safe yield, the contents of emergency contingency plans and water conservation plans, the contents of an evaluation of source water protection measures, a process for approval, modification or rejection of plans submitted pursuant to this section, a schedule for submission of the plans and a mechanism for determining the completeness of the plan. . .".

critical lands to be protected and incompatible land use activities with the [\*822] potential to contaminate a public drinking water source."<sup>36</sup> [General Statutes § 25-32d \(b\)](#).

[\*\*\*60] Similar planning occurs on the level of the water utility coordinating committees, who are required to conduct preliminary assessments, in consultation with the department of environmental protection and the department of public health, of water supply conditions and problems in their areas. See [General Statutes § 25-33g \(a\)](#). As part of this process, the water utility coordinating committees "shall establish preliminary exclusive service area boundaries, [\*\*988] based on the final assessment, for each public water system within the management area, and may change such boundaries. . . . If there is no agreement by the committee on such boundaries, or on a change to such boundaries, the committee shall consult with the Department of Public Utility Control. If there is no agreement by the committee after such consultation, the Commissioner of Public Health shall establish or may change such exclusive service area boundaries taking into consideration any [\*823] water company rights established by statute, special act or administrative decisions. In establishing such boundaries the commissioner shall maintain existing service areas and consider the orderly and efficient development [\*\*\*61] of public water supplies. In considering any change to exclusive service area boundaries, the commissioner shall maintain existing service areas, consider established exclusive service areas, and consider the orderly and efficient development of public water supplies." [General Statutes § 25-33g \(b\)](#).

Indeed, "each water utility coordinating committee shall prepare a coordinated water system plan in the public water supply management area. Such plan shall be submitted to the Commissioner of Public Health for his approval not more than two years after the first meeting of the committee. The plan shall promote cooperation among public water systems and include, but not be limited to, provisions for (1) integration of public water systems, consistent with the protection and enhancement of public health and well-being; (2) integration of water company plans; (3) exclusive service areas; (4) joint management or ownership of services; (5) satellite management services; (6) interconnections between public water systems; (7) integration of land use and water system plans; (8) minimum design standards; (9) water conservation; (10) the impact on other uses of water resources; [\*\*\*62] and (11) acquisition of land surrounding wells proposed to be located in stratified drifts."<sup>37</sup> [General Statutes § 25-33h \(a\)](#).

<sup>36</sup> Agency regulations implementing [§ 25-32d](#) prescribe a process for the submission, completion and approval of the plan. [Section 25-32d-5 \(c\) \(1\) of the Regulations of Connecticut State Agencies](#) provides a timeline for the process by which the department of public health consults with the department of environmental protection and the department of public utility control. [Section 25-32d-5 \(c\) \(3\) of the Regulations of Connecticut State Agencies](#) requires the commissioner to approve, reject, or approve the plan "with conditions" within sixty days of department of environmental protection or department of public utility control comment, or if there has been no such comment, "in no case more than one hundred and fifty days after written notice that the plan has been deemed complete . . . ."

[Section 25-32d-5 \(c\) \(2\) of the Regulations of Connecticut State Agencies](#) provides factors for the department of public health to consider "in making a decision to approve, modify or reject a plan," including "(A) the ability of the company to provide a pure, adequate and reliable water supply for present and projected future customers;

"(B) adequate provision for the protection of the quality of future and existing sources;

"(C) comments from state agencies; and

"(D) consistency with state regulations and statutes."

<sup>37</sup> [General Statutes § 25-33h \(b\)](#) prescribes a procedure for the adoption of the plan, and requires that the committee seek comments from, inter alia, the department of public health, on "the availability of pure and adequate water supplies, potential conflicts over the use of such supplies, and consistency with the goals of [sections 25-33c to 25-33j](#), inclusive."

[Section 25-33h-1 \(d\) of the Regulations of Connecticut State Agencies](#) prescribes the contents of the coordinated water supply plans promulgated pursuant to [General Statutes § 25-33h](#). It requires that "the coordinated water system plan shall include, but not be limited to, the following:

[\*\*\*63] [\*824] [\*\*989] Moreover, the department of public health permits may only be issued in accordance with the coordinated plans adopted pursuant to [§ 25-33h](#); see [General Statutes § 25-33i \(a\)](#); "no public water supply system may be approved within a public water supply management area after the Commissioner of Public Health has convened a water utility coordinating committee unless (1) an existing public water supply system is unable to provide water service or (2) the committee recommends such approval." [General Statutes § 25-33i \(b\)](#).

C

#### Application of [§ 35-31 \(b\)](#) to the Water Company and Supply Statutes

The defendants argue that these statutes and regulations "seek to promote the cooperation and interconnection [\*825] of water companies, and, by contrast, do not seek to promote the creation of new, independent owners of water sources." They claim that "it is simply inaccurate to state as do the plaintiffs that there exists in Connecticut a wholly unregulated wholesale market for water. The comprehensive scheme of regulation in place in Connecticut regulates all activities of Connecticut water companies and it is at the very least reasonably foreseeable [\*\*\*64] that 'virtual monopolies' might result in some areas with regard to the purchase and sale of bulk water. The creation of exclusive service areas requires and entails marshalling, allocation, and protection of water sources, including interconnection, hence [it] regulates all aspects of the defendants' operations."

We note, at the outset, that we need not determine whether a monopoly is the "reasonably foreseeable" result of this statutory scheme. That inquiry would have its basis in the broader state action standards found under federal case law following *Parker*, and is, therefore, incompatible with the narrower analysis demanded by [§ 35-31 \(b\)](#). See part I A of this opinion. As discussed previously in part I C of this opinion, this court's decision in [Mazzola v. Southern New England Telephone Co., supra, 169 Conn. 344](#), remains the controlling construction of [§ 35-31 \(b\)](#). Case law following *Mazzola* that applied [§ 35-31 \(b\)](#) demonstrates that the Connecticut immunity statute, which

"(1) The individual water system plan of each public water system within a public water supply management area, required to file such plan pursuant to [section 25-32d of the Connecticut General Statutes](#); and

"(2) An areawide supplement that shall address areawide water system concerns pertaining to the public water supply management area which are not otherwise included in each water company's individual water system plan. The areawide supplement consists of a water supply assessment, exclusive service area boundaries, integrated report, and executive summary. The areawide supplement shall include at least the following:

##### "(A) Water Supply Assessment

"A water supply assessment shall be developed to evaluate water supply conditions and problems within the public water supply management area. The [water utility coordinating committee] shall prepare a preliminary and then a final water supply assessment. The water supply assessment shall be a factual and concise report including at least the following topics as they relate to public water systems in the public water supply management area:

"(i) Description of existing water systems, including

"(aa) History of water quality, reliability, service, and supply adequacy;

"(bb) General fire fighting capability of the utilities; and

"(cc) Identification of major facilities which need to be expanded, altered, or replaced.

"(ii) Availability and adequacy of any future water source(s).

"(iii) Existing service area boundaries and public water system limits established by statute, special act or administrative decision, including a map of established boundaries, and identification of systems without boundaries.

"(iv) Present and projected growth rates, including population data, land use patterns and trends, and identification of lands available for development.

"(v) Status of water system planning, land use planning and coordination between public water systems. . . ." [Regs., Conn. State Agencies § 25-33h-1 \(d\)](#).

requires that the challenged activities be "specifically directed or required by a statute," demands a more exacting analysis. Put differently, the cases demonstrate that [\*\*\*65] § 35-31 (b) immunity from antitrust liability will attach only if the statute under which protection is sought speaks directly to the challenged conduct. HN39<sup>↑</sup> Generalized statements of policy or implications from the sheer pervasiveness of a regulatory scheme as a whole, therefore, simply do not have the requisite specificity under § 35-31 (b).<sup>38</sup> [\*826] Indeed, [\*\*990] this is consistent with the ordinary meaning of the word "specific" used in the statute. The American Heritage College Dictionary (4th Ed. 2002) defines "specific" in relevant part as: "1. Explicitly set forth; definite. . . . 4a. Intended for, applying to, or acting on a particular thing . . ." Accordingly, we emphasize that mere approval or acquiescence by a regulatory agency will not cloak an entity with antitrust immunity pursuant to § 35-31 (b). See Mazzola v. Southern New England Telephone Co., supra, 357-58.

[\*\*\*66] Apart from this court's leading decision in *Mazzola*, the case law applying § 35-31 (b) is entirely contained in state and federal trial court decisions.<sup>39</sup> In Mazzola v. Southern New England Telephone Co., supra, 169 Conn. 353, which was discussed in part I B of this opinion, the plaintiff brought an action against the telephone company, claiming antitrust violations resulting from the company's practices with respect to answering machines and message-taking devices, specifically the requirement that individuals obtaining such services from sources other than the telephone company were required to purchase or lease linking apparatus from the company. This court concluded that the telephone company was not immune from antitrust liability under § 35-31 (b), rejecting its argument that its activities had [\*827] been approved by the public utilities commission in accordance with the rate-setting procedure prescribed by § 16-19. Id., 357-58. The court concluded that § 35-31 (b) "has no parallel in the federal antitrust statutes," and that "in enacting this provision the Connecticut legislature also did not choose to follow the example set by several [\*\*\*67] other states of specifically and unqualifiedly exempting from antitrust liability the activities of industries and other organizations subject to the supervision of the state regulatory agency equivalent to our public utilities commission." Id., 359. This court emphasized that § 35-31 (b) was narrower than the holding of Parker v. Brown, supra, 317 U.S. 350-51, and concluded that the telephone company's activities satisfied neither standard because under the public utility rate-setting process of § 16-19, "the role that is statutorily assigned to the [public utility commission] in rendering effective tariffs proposed by companies such as the defendant amounts to little more than acquiescence in a program originated by the defendant. In no sense, then, can activities of the defendant such as the kind of activities challenged by the plaintiff, purportedly authorized by a tariff filed with and approved by the [public utility commission], be characterized as 'compelled by direction of the state acting as a sovereign' under the *Parker* doctrine as it has been judicially interpreted." Id., 365-66.

[\*\*\*68] In Professional Ambulance Service, Inc. v. Blackstone, 35 Conn. Sup. 136, 137, 400 A.2d 1031 (1978), the plaintiff was a private ambulance company who, along with two other private ambulance companies, previously had been dispatched by the [\*\*991] East Hartford police department on a rotating basis to provide emergency medical services to the town. The defendant mayor of East Hartford subsequently notified the plaintiff that the state office of emergency medical services and the North Central Emergency Medical Services Council had [\*828] designated another ambulance company, the Ambulance Service of Manchester, Inc., as the "'R-2 service company for East Hartford,'" which meant that only it could provide emergency ambulance service in the town. Id., 138. The mayor then issued to the police department a directive to that effect, and the police thereafter notified only Ambulance Service of Manchester, Inc., when ambulance service was needed. Id. The town also "passed an ordinance prohibiting ambulance companies from advertising their services as 'emergency services' or 'emergency personnel.'

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<sup>38</sup> The defendants rely heavily on the phrase "totality of the mandate," as coined by Judge Covello in Professional Ambulance Service, Inc. v. Blackstone, 35 Conn. Sup. 136, 143, 400 A.2d 1031 (1978), in support of their argument that the water supply statutes, in sum, "specifically commanded or directed" their conduct. We emphasize, however, that § 35-31 (b) immunity requires a statute that addresses the challenged conduct directly and explicitly, and accordingly, is not triggered by implication alone.

<sup>39</sup> HN40<sup>↑</sup> Trial court opinions are, "although entitled to serious consideration . . . not binding authority in this court." Commission on Hospitals & Health Care v. Lakoff, 214 Conn. 321, 333, 572 A.2d 316 (1990). Nevertheless, the trial court cases discussed herein provide particularly cogent illustrations of the correct application of § 35-31 (b), and their inclusion is warranted because that issue has been addressed only once on the appellate level, by this court's decision in *Mazzola*.

As a result, the plaintiff . . . noted a significant reduction in the number [\*\*\*69] of its calls for emergency ambulance services with a corresponding loss in revenues." Id. The plaintiff then brought a state antitrust action, claiming that "the designation of Ambulance Service of Manchester, Inc., as the single R2 responder for the East Hartford primary service area and the prohibition against advertising have had the effect of creating a monopoly and are in violation of these antitrust statutes." *Id.*, 140.

The court, *Covello*, J., relied on *Mazzola*, and concluded that, "the parties sought to be enjoined from alleged antitrust activities are not the officers of a private company regulated by a state agency, but are the officials of the state and municipal agencies themselves, pursuing emergency medical service functions directed by the statutes." *Id.*, 142. The court stated that the ambulance service regulations at issue were promulgated pursuant to the "totality of the mandate set out" in the emergency medical services statutes. *Id.*, 143. It concluded that the mayor's activities "represent the product of specifically directed state action," namely, regulations restricting ambulance advertising and ambulance primary service [\*\*\*70] areas.<sup>40</sup> *Id.*

[\*\*\*71] [\*829] We next consider the more recent federal District Court decision, also authored by Judge Covello, in *Wheelabrator Environmental Systems, Inc. v. Galante*, 136 F. Supp. 2d 21, 2000 WL 863029 (D. Conn. [\*992] 2001). The plaintiff and the defendants in that case were waste management companies, and the plaintiff had entered into an agreement with the Housatonic Resources Recovery Authority (recovery authority), an organization with eleven member municipalities that had "joined together to arrange for the orderly disposal of municipal solid waste . . . in accordance with state and regional solid waste plans." *136 F. Supp. 2d 21, Id. at \*1*. The defendants provided waste management services to some of the recovery authority municipalities by processing the waste and delivering it to the plaintiff's facilities to be burned and to generate electricity. *136 F. Supp. 2d 21, Id. at \*2*. The plaintiff brought a breach of contract action against the defendants, claiming that they failed to deliver waste to the plaintiff's management facility as was required by their contract. *Id.* The defendants counterclaimed against the plaintiff, arguing that it violated the Connecticut Antitrust [\*\*\*72] Act and the [\*830] federal Sherman Act in its attempts to preserve its monopoly over trash disposal services in the recovery authority market. *136 F. Supp. 2d 21, Id. at \*3*.

In addressing the plaintiff's argument that the state antitrust counterclaims should be dismissed under § 35-31 (b), the court relied on *Mazzola* and *Professional Ambulance Service, Inc.*<sup>41</sup> *136 F. Supp. 2d 21, Id. at \*6*. The court noted that the "allegedly anticompetitive conduct . . . arises solely from the [plaintiff's] waste agreement with the [recovery authority]." *Id.* It found the "specific authorization" required under the statute in "the totality of the mandate" of the waste management statutes that: (1) required municipalities to "make provisions for the safe and

<sup>40</sup> The trial court in *Professional Ambulance Service, Inc. v. Blackstone*, *supra*, 35 Conn. Sup. 138-39, stated that the mayor's actions were "the product of the implementation of a series of state regulations promulgated by the Connecticut department of health in furtherance of the emergency medical services program authorized by *General Statutes § 19-73u et seq.* [now *General Statutes § 19a-175 et seq.*]. [General Statutes § 19-73ee [now *General Statutes § 19a-183*] authorizes the establishment of a series of regional emergency medical service councils. The council for the geographic area which includes East Hartford is known as the North Central Emergency Medical Services Council. . . .

"Among their other duties, those councils are required by state regulation to designate so-called 'Primary Service Areas' for the various communities within their region. A primary service area . . . is simply a defined or known geographic area. [Sections] 19-73w-404 (B) and 19-73w-400 (D) [of the Regulations of Connecticut State Agencies] both require that within each primary service area there shall be only one firm assigned for a given category of service."

The court also noted § 19-73w-307 of the Regulations of Connecticut State Agencies, which provided: "'Ambulance services shall not advertise emergency medical services or emergency personnel for any political subdivision which has designated a phone number to be used to obtain EMS [Emergency Medical Service]. . . .' " *Professional Ambulance Service, Inc. v. Blackstone*, *supra*, 35 Conn. Sup. 140 n.5.

<sup>41</sup> The court dismissed the Sherman Act counterclaims after conducting a separate analysis pursuant to *Parker v. Brown*, *supra*, 317 U.S. 341, and its progeny. *Wheelabrator Environmental Systems, Inc. v. Galante*, *supra*, 136 F. Supp. 2d 21, 2000 WL 863029, at \*8.

sanitary disposal of all solid wastes which are generated within [their] boundaries"; [General Statutes § 22a-220 \(a\)](#); and (2) authorized the municipalities to enter into long-term contracts for waste management. [General Statutes § 7-273bb \(b\)](#); <sup>42</sup> [\\*\\*\\*74](#) see also [General Statutes § 22a-221 \(a\)](#) ("the state, any municipality or any municipal or regional authority may make contracts for the exercise of its corporate [\\*\\*\\*73](#) or municipal powers with respect to the collection, transportation, separation, [\[\\*831\]](#) volume reduction, processing, storage and disposal of its solid wastes for a period not exceeding thirty years and may pledge its full faith and credit for the payment of obligations under such contracts"). <sup>43</sup>

[\[\\*\\*\\*75\]](#) [\[\\*\\*993\]](#) We conclude that the present case is readily distinguishable from [Professional Ambulance Service, Inc.](#), and [Wheelabrator Environmental Systems, Inc.](#), because, in those cases, the applicable statutes and regulations spoke directly to all of the challenged conduct. In [Professional Ambulance Service, Inc.](#), the applicable regulations gave the town no choice except to designate one emergency ambulance service provider, and the advertising ordinance was authorized by a regulation directly on point. Similarly, in [Wheelabrator Environmental Systems, Inc.](#), it was the very existence of the waste manager's contract with the municipality that was the sole challenged conduct, which was plainly and specifically authorized by statute.

In contrast, the plaintiffs in the present case have alleged sufficient facts, viewed in the context of the [\[\\*832\]](#) statutory and regulatory scheme, to render improper the trial court's grant of the defendants' summary judgment motion. Although the statutes plainly envision *retail* monopolies through the designation of exclusive service areas, and some of the defendants' conduct was in fact mandated, namely, the inclusion of the pond in their water supply [\[\\*\\*\\*76\]](#) plans; see [General Statutes § 25-32d \(b\) \(3\)](#); [Regs., Conn. State Agencies § 25-33h-1 \(d\) \(2\) \(A\) \(ii\)](#); the remainder of the facts allege anticompetitive conduct well beyond the pale of the statutes, and therefore, not immune under [§ 35-31 \(b\)](#). Our reading of the statutes, which are quite comprehensive, reveals no mention of, for example: (1) authorization for contract clauses requiring water company parties to "use their best efforts to deter the construction and operation of new independent water systems"; and (2) manipulation of water supply figures in order to avert the declaration of a supply emergency, thus opening a previously closed market for additional water sources. Accordingly, action by state regulatory authorities in this case was limited to *acquiescence* to the defendants' anticompetitive activities with respect to the relevant wholesale water market, which like the telephone rate approval process considered in [Mazzola v. Southern New England Telephone Co., supra, 169 Conn. 344](#), does not supply the state direction required for immunity under [§ 35-31 \(b\)](#).

<sup>42</sup> [General Statutes § 7-273bb \(b\)](#) gives powers to municipal and regional resource recovery authorities and provides: "It is the intention of this chapter that the authorities shall be granted all powers necessary to fulfill the purposes of this chapter and to carry out their assigned responsibilities and that the provisions of this chapter are to be construed liberally in furtherance of this intention." See also [General Statutes § 7-273bb \(a\) \(12\)](#) (recovery authority may "do all things necessary for the performance of its duties, the fulfillment of its obligations, the conduct of its operations, the maintenance of its working relationships with the state, other municipalities, regions and persons, and the conduct of a comprehensive program for solid waste disposal and resources recovery, and for solid waste management services, in accordance with the provisions of the state or local solid waste management plan, applicable statutes and regulations and the requirements of this chapter").

<sup>43</sup> In contrast, we note *Interstate Aviation, Inc. v. Meriden*, Superior Court, judicial district of New Haven at Meriden, Docket No. CV92-0240874S (May 26, 1995), wherein the plaintiff unsuccessfully bid on the opportunity to operate a municipal airport. The plaintiff brought an action against the city and the successful bidder, claiming violations of municipal competitive bidding laws and antitrust statutes. With respect to the antitrust claims, the city claimed immunity pursuant to [§ 35-31 \(b\)](#), and moved for summary judgment. The trial court denied the motion for summary judgment, relying on *Mazzola* and concluding that the statute, [General Statutes § 13b-43](#), provided only that "any municipality . . . may establish, maintain and operate an airport at any location within the state approved by the commissioner and by the municipality or municipalities within which such airport is to be established, and may take any land or interest therein necessary for such establishment at such location upon paying just compensation to the owner of such land or interest therein. . . ." The court stated that the [HN41](#) ↑ "use of the term 'may' does not support the notion that such action is specifically directed or required by statute," and also that because the enabling legislation provided for acquisition of competitors, but only "in exchange for payment, it 'very clearly negates any defense claim of entitlement to impunity or immunity.'" *Interstate Aviation, Inc. v. Meriden*, *supra*.

The judgment is reversed and the case is remanded to the trial [\*\*\*77] court with direction to deny the defendants' motion for summary judgment and for further proceedings according to law.

In this opinion BORDEN, PALMER and VERTEFEUILLE, Js., concurred.

**Concur by:** SULLIVAN

## Concur

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SULLIVAN, C. J., concurring. I agree with the result reached by the majority, but disagree with its method [\*833] of statutory analysis. This case requires us to resolve an apparent inconsistency in the antitrust statutes. While [\*\*994] [General Statutes § 35-31 \(b\)](#)<sup>1</sup> provides that the antitrust provisions of chapter 624 do not apply to activities that are "specifically directed or required by a statute of this state, or of the United States," [General Statutes § 35-44b](#)<sup>2</sup> provides that, in interpreting the antitrust provisions, "the courts of this state shall be guided by interpretations given by the federal courts to federal antitrust statutes." As the defendants, the city of New London, the town of Waterford and their respective water pollution control authorities, point out, federal courts have concluded that the state action exemption applies to municipal activities that are the "'foreseeable result' of what the statute authorizes." [Electrical Inspectors, Inc. v. East Hills](#), 320 F.3d 110, 119 (2d Cir. 2003). [\*\*\*78] The statutory authorization need not be explicit. See id.

The defendants argue, in effect, that the plain and unambiguous language of both statutes cannot be given effect and, therefore, federal state action immunity standards should be read into [§ 35-31 \(b\)](#), contrary to the plain language of that statute. The apparent inconsistency between these statutes can be reconciled, however, by application of the principle that "where statutes contain specific and general references [\*\*\*79] covering the same subject matter, the specific references prevail over the general."<sup>3</sup> [Galvin v. Freedom of Information](#) [\*\*995] [\*834]

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<sup>1</sup> [General Statutes § 35-31 \(b\)](#) provides: "Nothing contained in this chapter shall apply to those activities of any person when said activity is specifically directed or required by a statute of this state, or of the United States."

<sup>2</sup> [General Statutes § 35-44b](#) provides: "It is the intent of the General Assembly that in construing [sections 35-24 to 35-46](#), inclusive, the courts of this state shall be guided by interpretations given by the federal courts to federal antitrust statutes."

<sup>3</sup> The majority applies this principle to conclude that [§ 35-31 \(b\)](#) should apply over the more general provisions of the Sherman Act, [15 U.S.C. § 1](#), as construed by the federal courts. I disagree. Federal [antitrust law](#) pertaining to state action immunity is more lenient than [§ 35-31 \(b\)](#), but is just as specific. The reason that we should not follow federal law in this case is that the provisions of [§ 35-31 \(b\)](#) are more specific than the provisions of [§ 35-44b](#) and, therefore, to the extent that there is a patent inconsistency between the plain language of [§ 35-31 \(b\)](#) and the federal law, the provisions of [§ 35-44b](#) requiring us to follow federal law do not apply. I recognize that [§ 35-44b](#) requires us, as a threshold matter, to compare the plain language of [§ 35-31 \(b\)](#) with the relevant federal law to determine whether such an inconsistency exists in the first instance. Once it has been determined that such an inconsistency exists, however, we are no longer bound by [§ 35-44b](#) in construing the meaning of [§ 35-31 \(b\)](#).

The majority argues that my analysis is internally inconsistent because the canon of statutory construction providing that specific statutes prevail over more general statutes is, itself, a form of "extratextual evidence . . . ." I disagree. I believe that "we may apply the ordinary canons of judicial construction in seeking the plain meaning" of the statutory scheme. (Emphasis added.) [State v. Courchesne](#), 262 Conn. 537, 634, 816 A.2d 562 (2003) (Zarella, J., dissenting, joined by Sullivan, C. J.). Thus, this canon informs us, before we ever look to federal law, that if there is an inconsistency between federal law and [§ 35-31 \(b\)](#), [§ 35-31 \(b\)](#) prevails over [§ 35-44b](#).

Finally, the majority argues that the canon providing that the specific prevails over the general does not apply because [§ 35-31 \(b\)](#) and [§ 35-44b](#) are fundamentally different. At the heart of the majority's analysis, however, is its recognition that the general rule that we follow federal precedent when interpreting the Connecticut Antitrust Act does not apply when the specific text of our

Commission, 201 Conn. 448, 456, 518 A.2d 64 (1986). Because § 35-31 (b) is more specific than § 35-44b, its terms should prevail in this case. Thus, there is no need to go beyond the plain and unambiguous language of the statute. See General Statutes § 1-2z ("The meaning of a statute shall, in the first instance, be ascertained from the text of the statute itself and its relationship to other statutes. If, after examining such text and considering such relationship, the meaning of such text is plain and unambiguous and does not yield absurd or unworkable results, extratextual [\*835] evidence of the meaning of the statute shall not be considered."). Accordingly, I believe that the statutory analysis should begin and end with the application of § 1-2z. I see no need for the majority's lengthy "examination of the interplay . . . between federal case law . . . governing state action immunity, and the statutory state action immunity standard set forth by § 35-31 (b)" or its application of the standards set forth in Manifold v. Ragaglia, 272 Conn. 410, 419, 862 A.2d 292 (2004) [\*\*\*80] (this court's "fundamental objective is to ascertain and give effect to the apparent intent of the legislature" [emphasis added; internal quotation marks omitted]) and Jagger v. Mohawk Mountain Ski Area, Inc., 269 Conn. 672, 679, 849 A.2d 813 (2004) (court looks to "words of the statute itself, to the legislative history and circumstances surrounding its enactment, to the legislative policy it was designed to implement, and to its relationship to existing legislation and common law principles governing the same general subject matter" [internal quotation marks omitted]).

[\*\*\*81]

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antitrust statutes requires us to do otherwise. See Westport Taxi Service, Inc. v. Westport Transit District, 235 Conn. 1, 15-16, 664 A.2d 719 (1995). This is an application of the very canon that the majority purports to reject. Thus, my disagreement with the majority is not with its general approach to the issue or its conclusion, but with its apparent unwillingness to state simply and explicitly that, because the language of § 35-31 (b) is plain and unambiguous, we are bound by that language and, because § 35-31 (b) is more specific than § 35-44b, we are not bound by § 35-44b.



## **Bradburn Parent Teacher Store, Inc. v. 3M**

United States District Court for the Eastern District of Pennsylvania

June 9, 2005, Decided

CIVIL ACTION NO. 02-7676

### **Reporter**

2005 U.S. Dist. LEXIS 11375 \*; 2005-2 Trade Cas. (CCH) P74,921

BRADBURN PARENT TEACHER STORE, INC., On Behalf of Itself and Others Similarly Situated v. 3M  
(MINNESOTA MINING AND MANUFACTURING COMPANY)

**Subsequent History:** Motion granted by [\*Bradburn Parent Teacher Store, Inc. v. 3M, 2005 U.S. Dist. LEXIS 15815 \(E.D. Pa., Aug. 2, 2005\)\*](#)

**Prior History:** [\*Bradburn Parent Teacher Store, Inc. v. 3M, 2005 U.S. Dist. LEXIS 5315 \(E.D. Pa., Mar. 30, 2005\)\*](#)

## **Core Terms**

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prices, monopoly power, collateral estoppel, exclusionary, power to control, predatory, tape, reconsideration motion, time period, argues, relevant market, harmed, transparent, willfully, period of time, jury's verdict, preclusion, invisible, possessed, interlocutory appeal, power to exclude, clear error, competitors, antitrust

## **LexisNexis® Headnotes**

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Civil Procedure > Judgments > Relief From Judgments > Altering & Amending Judgments

Civil Procedure > Judgments > Relief From Judgments > General Overview

Civil Procedure > ... > Relief From Judgments > Grounds for Relief from Final Judgment, Order or Proceeding > Newly Discovered Evidence

Civil Procedure > Appeals > Standards of Review > Clearly Erroneous Review

### **HN1[] Relief From Judgments, Altering & Amending Judgments**

The purpose of a motion for reconsideration is to correct manifest errors of law or fact or to present newly discovered evidence. A motion for reconsideration will only be granted if the moving party establishes: (1) the existence of newly available evidence; (2) an intervening change in the controlling law; or (3) a need to correct a clear error of law or prevent manifest injustice. Reconsideration of a previous order is an extraordinary remedy to be employed sparingly in the interests of finality and conservation of judicial resources.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN2** [down] **Estoppel, Collateral Estoppel**

Courts apply federal common law principles of issue preclusion when determining the preclusive effect of a prior federal action.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN3** [down] **Estoppel, Collateral Estoppel**

Under the doctrine of issue preclusion, once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits based on a different cause of action involving a party to the prior litigation. The doctrine of issue preclusion is derived from the simple principle that later courts should honor the first actual decision of a matter that has been actually litigated. Collateral estoppel has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN4** [down] **Estoppel, Collateral Estoppel**

A litigant who was not a party to a prior judgment may nevertheless use that judgment "offensively" to prevent a defendant from relitigating issues resolved in the earlier proceeding. This form of issue preclusion is also known as offensive non-mutual collateral estoppel.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judicial Officers > Judges > Discretionary Powers

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN5** [down] **Estoppel, Collateral Estoppel**

A party seeking estoppel must show that the following four elements are satisfied: (1) the issue sought to be precluded is the same as that involved in the prior action; (2) that issue was actually litigated; (3) that issue was

determined by a final and valid judgment; and (4) the determination was essential to the prior judgment. In addition, the application of offensive non-mutual collateral estoppel is subject to an overriding fairness determination by a trial judge. A trial court has broad discretion to determine when collateral estoppel should be applied.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Evidence > Inferences & Presumptions > General Overview

Civil Procedure > ... > Jury Trials > Verdicts > General Overview

Civil Procedure > ... > Jury Trials > Verdicts > General Verdicts

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

#### **HN6** [down arrow] **Estoppel, Collateral Estoppel**

Collateral estoppel is properly applied to factual inferences drawn from a general jury verdict when such findings are necessarily implied by the prior verdict. Inferences are necessarily implied by a prior verdict if they are as a practical matter necessary to support that verdict, and a rational jury thus must have made such findings. In determining whether or not an implicit factual finding was necessary for a prior verdict, courts may consider the reasonableness of various interpretations of the evidence.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

#### **HN7** [down arrow] **Monopolies & Monopolization, Actual Monopolization**

The United States Court of Appeals for the District of Columbia Circuit has explained that, while monopoly power is broadly defined as the power to control prices or exclude competition, more precisely, a firm is a monopolist if it can profitably raise prices substantially above the competitive level.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

#### **HN8** [down arrow] **Monopolies & Monopolization, Actual Monopolization**

The goal of a monopolist who has attained the power to control prices is not to drive the price of its product up as high as possible, but rather to increase the price of its product to the point at which it will maximize its profit.

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

#### **HN9** [down arrow] **Market Definition, Relevant Market**

The ability of consumers to restrain a company from raising prices above the competitive level by decreasing their demand for the monopolist's product is well-recognized, and generally taken into account in the relevant market definition.

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Sherman Act > Scope > General Overview

## **HN10** [blue] **Actual Monopolization, Anticompetitive & Predatory Practices**

The antitrust laws were enacted for the protection of competition not competitors. To establish unlawful maintenance of a monopoly under [§ 2](#) of the Sherman Act, proof of predatory or exclusionary practices in themselves are not sufficient. There must be proof that competition, not merely competitors, has been harmed. A finding of no anticompetitive market effect would not suffice to dispose of a claim under [§ 2](#) of the Sherman Act, because injury to competition is presumed to follow from the conduct proscribed by [§ 2](#). Harm to competition itself is a sine qua non for a [§ 2](#) violation.

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**Judges:** John [\*2] R. Padova, J.

**Opinion by:** John R. Padova

## **Opinion**

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### **MEMORANDUM**

**Padova, J.**

Plaintiff, Bradburn Parent Teacher Store, Inc. ("Bradburn"), has brought this antitrust class action against Defendant 3M for damages arising out of 3M's anti-competitive conduct during the time period from October 2, 1998 through

the present. Presently before the Court is 3M's Motion for Reconsideration of the Court's March 30, 2005 Memorandum and Order finding certain material facts to be without substantial controversy and established upon the trial of this action or, in the alternative, Motion for Certification of Interlocutory Appeal. For the reasons that follow, said Motion is granted in part and denied in part.

## I. BACKGROUND

The conduct of 3M which forms the basis of this class action lawsuit was the subject of a prior lawsuit in this Court, [Le Page's, Inc. v. 3M, 2000 U.S. Dist. LEXIS 3087, Civ. A. No. 97-3983 \(E.D. Pa.\)](#). In that suit, LePage's, Inc., a competing supplier of transparent tape, sued 3M alleging, inter alia, unlawful maintenance of monopoly power in violation of Section 2 of the Sherman Act, [15 U.S.C. § 2](#). After a nine-week trial, the jury found in favor of LePage's on its unlawful [\*3] maintenance of monopoly power claim. The jury awarded damages in the amount of \$ 22,828,899.00, which were subsequently trebled to \$ 68,486,697.00. See [Le Page's, Inc. v. 3M, 2000 U.S. Dist. LEXIS 3087, Civ. A. No. 97-3983, 2000 WL 280350 \(E.D. Pa. Mar. 14, 2000\)](#). 3M filed a Motion for Judgment as a Matter of Law, which this Court denied on March 14, 2000. See [id.](#) [3M, 2000 U.S. Dist. LEXIS 3087](#) thereafter appealed this Court's denial of its Motion for Judgment as a Matter of Law to the United States Court of Appeals for the Third Circuit ("Third Circuit"). A Third Circuit panel initially reversed this Court's Order upholding the jury's verdict and directed the Court to enter judgment for 3M on LePage's' unlawful maintenance of monopoly power claim. [LePage's, Inc. v. 3M, 277 F.3d 365 \(3d Cir. 2002\)](#) ("LePage's I"). Upon rehearing en banc, the Third Circuit vacated the panel decision and reinstated the original jury verdict against 3M. [LePage's, Inc. v. 3M, 324 F.3d 141 \(3d Cir. 2003\)](#) ("LePage's II"), cert. denied 542 U.S. 953, 159 L. Ed. 2d 835, 124 S. Ct. 2932 (2004).

The Complaint in the instant litigation alleges one count of monopolization in violation of [Section 2 of the Sherman Act](#) [\*4]. The Complaint asserts that 3M unlawfully maintained monopoly power in the transparent tape market through its bundled rebate programs<sup>1</sup> [\*6] and through exclusive dealing arrangements with various retailers. The Complaint further alleges that, as a result of 3M's conduct, Bradburn and other class members<sup>2</sup> have "suffered antitrust injury." (Compl. P 27). The damages period in this case runs from October 2, 1998 to the present. (*Id.* P 2). Bradburn filed a Motion for Partial Summary Judgment on the basis that several issues had been fully and fairly litigated in the *LePage's* case so that collateral estoppel now applied. By Memorandum and Order dated March 30, 2005, the Court denied Bradburn's Motion, but held that collateral estoppel nonetheless applied to establish the following facts upon the trial of the instant action:

1. For the time period from June 11, 1993 to October 13, 1999, the relevant market in this matter is the market for invisible and transparent tape for home and office use in the United States;
2. For the time period from June 11, 1993 to October 13, 1999, 3M possessed monopoly power in the relevant market, including the power to control prices and exclude [\*5] competition in the relevant market;
3. For the time period from June 11, 1993 to October 13, 1999, 3M willfully maintained such monopoly power by predatory or exclusionary conduct; and
4. For the time period from June 11, 1993 to October 13, 1999, 3M's predatory or exclusionary conduct harmed competition.

(03/30/2005 Memorandum and Order at 41.) In the instant Motion, 3M moves the Court to reconsider its March 30, 2005 Memorandum and Order with regard to all issues which the Court deemed established for purposes of the trial of this action, with the exception of its determination that, for the time period from June 11, 1993 to October 13, 1999, the relevant market in this matter is the market for invisible and transparent tape for home and office use in the United States. In the alternative, 3M has moved the Court to certify this matter for interlocutory appeal.

<sup>1</sup> As described at length in the *LePage's* litigation, 3M's bundled rebate programs provided purchasers with significant discounts on 3M's products. However, the availability and size of the rebates were dependant upon purchasers buying products from 3M from multiple product lines. See [LePage's II, 324 F.3d at 154-55.](#)

<sup>2</sup> On August 18, 2004, the Court certified as a class "all persons who directly purchased invisible or transparent tape from 3M between October 2, 1998 and the present, who have not purchased, for resale under the class member's own label, any 'private label' invisible or transparent tape from 3M or any of 3M's competitors at any time from October 2, 1988 to the present." (August 18, 2004 Memorandum and Order.)

## II. LEGAL STANDARD

**HN1** [↑] "The purpose of a motion for reconsideration is to correct manifest errors of law or fact or to present newly discovered evidence." *Harsco Corp. v. Zlotnicki*, 779 F.2d 906, 909 (3d Cir. 1985). A motion for reconsideration will only be granted if the moving party establishes: (1) the existence of newly available evidence; (2) an intervening change in the controlling law; or (3) a need to correct a clear error of law or prevent manifest injustice. *Pub. Interest Research Group of N.J. v. Magnesium Elektron*, 123 F.3d 111, 116-17 (3d Cir. 1997). Reconsideration of a previous order is an extraordinary remedy to be employed sparingly [\*7] in the interests of finality and conservation of judicial resources. *Moyer v. Italwork s.a.s.*, 1997 U.S. Dist. LEXIS 7912, Civ. A. No. 95-2264, 1997 WL 312178, at \*3 (E.D. Pa. June 3, 1997). Plaintiff does not allege the existence of newly available evidence or an intervening change in the controlling law. Rather, Plaintiff argues that the Court made clear errors of law when it applied collateral estoppel to deem certain issues established for the purposes of this trial.

## III. DISCUSSION

**HN2** [↑] Courts apply federal common law principles of issue preclusion when determining the preclusive effect of a prior federal action. *Burlington N. R.R. v. Hyundai Merch. Marine Co.*, 63 F.3d 1227, 1231 (3d Cir. 1995).<sup>3</sup> **HN3** [↑] Under the doctrine of issue preclusion, "once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits based on a different cause of action involving a party to the prior litigation." *Montana v. United States*, 440 U.S. 147, 153, 59 L. Ed. 2d 210, 99 S. Ct. 970 (1979). The doctrine of issue preclusion is derived from "the simple principle that later courts should honor the first actual decision of [\*8] a matter that has been actually litigated." *Burlington*, 63 F.3d at 1231 (citation omitted). Collateral estoppel "has the dual purpose of protecting litigants from the burden of relitigating an identical issue with the same party or his privy and of promoting judicial economy by preventing needless litigation." *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 326, 58 L. Ed. 2d 552, 99 S. Ct. 645 (1979).

Here, Bradburn, which was not a party to the *LePage*'s litigation, sought to use issue preclusion offensively against 3M, which was a party to *LePage*'s. It is well-settled that **HN4** [↑] "a litigant who was not a party to a prior judgment may nevertheless use that judgment 'offensively' to prevent a defendant from [\*9] relitigating issues resolved in the earlier proceeding." *Parklane*, 439 U.S. at 326. This form of issue preclusion is also known as offensive non-mutual collateral estoppel.<sup>4</sup> *Burlington*, 63 F.3d at 1232.

**HN5** [↑] The party seeking estoppel must show that the following four elements are satisfied: "(1) the issue sought to be precluded [is] the same as that involved in the prior action; (2) that issue [was] actually litigated; (3) that issue [was] determined by a final and valid judgment; and (4) the determination [was] essential to the prior judgment." *AMTRAK v. Pa. PUC*, 342 F.3d 242, 252 (3d Cir. 2003) [\*10] (quoting *AMTRAK v. Pa. PUC*, 288 F.3d 519, 525 (3d Cir. 2002)). In addition, the application of offensive non-mutual collateral estoppel is "subject to an overriding fairness determination by the trial judge." *Burlington*, 63 F.3d at 1232. The trial court has "broad discretion to determine when [collateral estoppel] should be applied." *Parklane*, 439 U.S. at 331, 99 S. Ct. at 651.

### A. Power to Control Prices and Exclude Competition

3M argues that the Court made a clear error of law when it found pursuant to *Rule 56(d)* that "3M possessed . . . the power to control prices and exclude competition in the relevant market." (03/30/2005 Memorandum and Order at 41.) 3M does not argue that the jury in *LePage*'s did not determine that 3M had the power to exclude competition. Rather, 3M contends that it would be improper to also infer from the jury's verdict in *LePage*'s that 3M had the

<sup>3</sup>Throughout this opinion the Court will use the phrase "issue preclusion" and "collateral estoppel" interchangeably. See *Witkowski v. Welch*, 173 F.3d 192, 198 (3d Cir. 1999) (noting that the doctrine of collateral estoppel is now commonly referred to as issue preclusion).

<sup>4</sup>For the sake of simplicity, the Court will refer to the doctrine of offensive non-mutual collateral estoppel as "collateral estoppel" and "offensive collateral estoppel" when addressing the legal rule which governs the preclusive effect of a prior judgment in this case. See *Raytech Corp. v. White*, 54 F.3d 187, 190 n.5 (3d Cir. 1995).

power to control prices, because 3M presented evidence at trial that the market was dominated by customers much larger than 3M, who were in a position to retaliate on a broad range of product purchases if 3M were to charge supra-competitive [\*11] prices for transparent or invisible tape. 3M argues that a rational jury in *LePage's* could, therefore, have found that although 3M had the ability to exclude competition, it did not have the power to control prices.

**HN6**<sup>↑</sup> Collateral estoppel is properly applied to factual inferences drawn from a general jury verdict when such findings are necessarily implied by the prior verdict. *Ag. Servs. of Am., Inc. v. Nielsen*, 231 F.3d 726, 731 (10th Cir. 2000) (citing *Butler v. Pollard*, 800 F.2d 223, 225 (10th Cir. 1986); *Chew v. Gates*, 27 F.3d 1432, 1438 (9th Cir. 1994); see also *Ohio-Sealy Mattress Mfg. Co. v. Sealy, Inc.*, 585 F.2d 821, 844 (7th Cir. 1978)). Inferences are necessarily implied by a prior verdict if they are as a practical matter necessary to support that verdict, and a rational jury thus must have made such findings. *Chew*, 27 F.3d at 1438; *In re Nangle*, 274 F.3d 481, 483 (8th Cir. 2001); *Hoult v. Hoult*, 157 F.3d 29, 31-32 (1st Cir. 1998). In determining whether or not an implicit factual finding was necessary for a prior verdict, courts may consider the [\*12] reasonableness of various interpretations of the evidence. 18 Charles A. Wright, et al., *Federal Practice and Procedure* § 4420, at 523 (2d ed. 2002).

In its March 30, 2005 Memorandum and Order, the Court found that 3M's power to control prices was essential to the jury's verdict in *LePage's* because the jury had determined that 3M had the power to exclude competition, and "the ability to exclude competition necessarily results in the ability to control prices." (03/30/2005 Memorandum and Order at 23.) The Court reasoned that

"Once a monopolist achieves its goal by excluding potential competitors, it can then increase the price of its product to the point at which it will maximize its profit." *LePage's II*, 324 F.3d at 164. Indeed, "the more competition a company faces, the less it can control prices because competitors will undercut its prices to secure market share. Conversely, a company that can exclude competition can sustain its ability to control prices." *PepsiCo, Inc. v. Coca-Cola Co.*, 315 F.3d 101, 107-08 (2d Cir. 2002) (citations omitted); see also *LePage's II*, 324 F.3d at 164 (exclusion of competitors allows [\*13] companies to increase price of products); *Barr Labs., Inc. v. Abbott Labs.*, 978 F.2d 98, 114 (3d Cir. 1992) (competition "would have prevented [defendant] from raising prices for any lengthy period of time"); *Columbia Metal Culvert Co. v. Kaiser Aluminum & Chem. Corp.*, 579 F.2d 20, 26 (3d Cir. 1978) (ongoing competition "guards against the ability of the dominant entity to increase prices"); see generally 2A Phillip E. Areeda, et al., *Areeda & Hovenkamp's Antitrust Law*, P 501, at 85-86 (2002).

(*Id.* at 24.) **HN7**<sup>↑</sup> The United States Court of Appeals for the District of Columbia Circuit has further explained that, while monopoly power is broadly defined as the power to control prices or exclude competition, "more precisely, a firm is a monopolist if it can profitably raise prices substantially above the competitive level." *United States v. Microsoft Corp.*, 346 U.S. App. D.C. 330, 253 F.3d 34, 51 (D.C. Cir. 2001) (citing 2A Phillip E. Areeda et al., *Antitrust Law* P 501, at 85 (1995)).

Contrary to 3M's assertion, the mere fact that 3M's larger customers could have retaliated had 3M raised prices beyond their [\*14] existing levels did not permit the jury in *LePage's* to find that 3M did not have the power to control prices. It is well-established that **HN8**<sup>↑</sup> the goal of a monopolist who has attained the power to control prices is not to drive the price of its product up as high as possible, but rather to "increase the price of its product to the point at which it will maximize its profit." *LePage's II*, 324 F.3d at 164. **HN9**<sup>↑</sup> The ability of consumers to restrain a company from raising prices above the competitive level by decreasing their demand for the monopolist's product is well-recognized, and generally taken into account in the relevant market definition. See *Microsoft*, 253 F.3d at 52.

While 3M's point of profit maximization for invisible and transparent tape may have been lower than usual due to the potential retaliation by its larger customers across 3M's product line, the potential for decreases in demand for 3M's products as a result of an increase in tape prices does not establish that 3M might not have had the power to control prices. Rather, the fact that 3M could have faced declining demand across its product range had it exercised its power to raise tape [\*15] prices merely establishes that the tape price at which 3M maximized its profit was the price which it was actually charging, and that any further price increase would have been unprofitable. See

LePage's II, 324 F.3d at 164. Accordingly, the evidence 3M presented in the *LePage*'s trial to suggest that some of its customers might have retaliated by refusing to buy 3M products had 3M raised the price for invisible and transparent tape is has no impact on the Courts determination that the power to exclude competition in this case necessarily results in the power to control prices. The Court thus correctly concluded in its March 30, 2005 Memorandum and Order that the jury in *LePage*'s necessarily determined that 3M possessed both the power to exclude competition and control prices.

3M further argues that a finding that it is established for the purposes of the trial of this action that 3M had the power to control prices creates an unfair risk that the jury in this case will either consider itself constrained to find that 3M did in fact control prices, or speculate that the *LePage*'s jury might have made such a finding. However, a finding that 3M had the power [\*16] to control prices does not establish that 3M in fact exercised that power to the detriment of Bradburn, and Bradburn retains the burden of proving this allegation at trial. Moreover, as the Court noted in its March 30, 2005 Memorandum and Order, 3M's fears of juror confusion can and will be fully addressed through appropriate jury instructions. Accordingly, the Court finds that it correctly concluded in its March 30, 2005 Memorandum and Order that the application of collateral estoppel to the issue of 3M's power to exclude competition and control prices is fair to 3M. 3M's Motion for Reconsideration is, therefore, denied in this respect.

#### B. Maintenance of Monopoly Power

3M also argues that the Court made a clear error of law when found pursuant do Rule 56(d) that "3M willfully maintained . . . monopoly power by predatory or exclusionary conduct." (03/30/2005 Memorandum and Order at 41.) 3M contends that this finding improperly suggests that 3M had unlawfully acquired a monopoly or would have lost its monopoly position absent the conduct challenged in *LePage*'s as predatory or exclusionary. However, the statement that 3M willfully maintained monopoly power in no way suggests [\*17] that 3M willfully acquired monopoly power or would have lost such power absent the conduct challenged in *LePage*'s. 3M therefore remains free to argue that it would have acquired and continued to possess its monopoly position even if 3M had not engaged in predatory or exclusionary conduct. (See *id.*)

3M further contends that it would be unduly prejudicial to apply collateral estoppel to a determination that 3M willfully maintained monopoly power by predatory or exclusionary conduct without being able to tell the jury specifically which of 3M's practices were predatory or exclusionary.<sup>5</sup> 3M argues that this holding will prevent a jury in the instant case from fully exploring the rational nexus between the actual conduct found to be unlawful in *LePage*'s and the claim of injury to Bradburn. However, the Court's March 30, 2005 Memorandum and Order in fact has the opposite effect. As noted in the March 30, 2005 Memorandum and Order, "even for the period from June 11, 1993 through October 13, 1999, Bradburn will still be required to offer proof that 3M's antitrust violations caused Bradburn injury of the type the antitrust laws were intended to prevent." (*Id.* at 41.) Thus, [\*18] it remains for the jury in this case to determine not only which of the five practices challenged in *LePage*'s were in fact predatory or exclusionary, but also whether a rational nexus exists between this unlawful conduct and any injury to Bradburn. Accordingly, the Court finds that it correctly concluded in its March 30, 2005 Memorandum and Order that the

<sup>5</sup> In its Motion for Partial Summary Judgment Bradburn had asked the Court to establish through the application of collateral estoppel that 3M's predatory or exclusionary conduct during the relevant period included:

- a) 3M's rebate programs, such as Executive Growth Fund, Partnership Growth Fund, Brand Mix Program;
- b) 3M's Market Development Fund, and other payments to customers conditioned on customers achieving certain sales goals or growth targets;
- c) 3M's efforts to control, or reduce, or eliminate private label tape;
- d) 3M's efforts to switch customers to 3M's more expensive branded tape; and
- e) 3M's efforts to raise the price consumers pay for Scotch tape.

The Court, however, declined to apply collateral estoppel to this issue because the jury in *LePage*'s could have "based its finding of predatory or exclusionary conduct on any one of the five examples alone," and thus "none of the five alleged predatory or exclusionary practices were essential to the judgment in *LePage*'s." (03/30/2005 Memorandum and Order at 27.)

application of collateral estoppel to the issue of 3M's unlawful maintenance of monopoly power by predatory or exclusionary practices is fair to 3M. 3M's Motion for Reconsideration is, therefore, denied in this respect.

#### [\*19] C. Harm to Competition

3M further argues that the Court made a clear error of law when it found pursuant to [Rule 56\(d\)](#) that "3M's predatory or exclusionary conduct harmed competition." (03/30/2005 Memorandum and Order.) 3M argues that the *LePage*'s jury was never instructed that it was required to find harm to competition; that although the jury found that plaintiff in *LePage*'s had been harmed, there was evidence that competition in general was benefitted; and that a finding of harm to competition in any event was not essential to the jury's verdict.

It is well-established that [HN10](#) [↑] "the antitrust laws . . . were enacted for the protection of competition not competitors." [Angelico v. Lehigh Valley Hosp., Inc.](#), 184 F.3d 268, 275 n.1 (3d Cir. 1999) (quoting [Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.](#), 429 U.S. 477, 488, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977)). To establish unlawful maintenance of a monopoly under [section 2 of the Sherman Act](#), therefore, proof of "predatory or exclusionary practices in themselves are not sufficient. There must be proof that competition, not merely competitors, has been harmed." [United States v. Dentsply Int'l, Inc.](#), 399 F.3d 181, 187 (3d Cir. 2005) [\*20] (citing [LePage's II](#), 324 F.3d at 162). Nonetheless, "a finding of no anticompetitive market effect would not suffice to dispose of [a] claim under [section 2 of the Sherman Act](#)," [Angelico](#), 184 F.3d at 275 n.5 (citing [Mahone v. Addicks Util. Dist.](#), 836 F.2d 921, 939 (5th Cir. 1988)), because "injury to competition is presumed to follow from the conduct proscribed by [section 2](#)." [Mahone](#), 836 F.2d at 939 (emphasis added). In other words, "harm[] to competition itself [is] a sine qua non for a § 2 violation." [LePage's II](#), 324 F.3d at 162.

Thus, even though the Court in *LePage*'s properly noted that harm to competition was not an element of a [section 2](#) claim and did not instruct the jury that it was required to find harm to competition, such finding was necessarily implied by the jury's determination that 3M had unlawfully maintained monopoly power in violation of [section 2](#). Accordingly, in reviewing the jury's verdict in *LePage*'s, the Third Circuit explicitly stated that "3M's exclusionary conduct not only impeded [plaintiff's] ability to compete, but also it harmed competition itself." [\*21] *Id.* The Court thus finds that it correctly concluded in its March 30, 2005 Memorandum and Order that the application of collateral estoppel to the issue that 3M's predatory or exclusionary conduct harmed competition is appropriate and fair to 3M. 3M's Motion for Reconsideration is, therefore, denied in this respect.

#### D. Applicable Time Period

Finally, 3M argues that the Court made a clear error of law when it applied collateral estoppel to the jury's findings in *LePage*'s for "the time period from June 11, 1993 to October 13, 1999." (03/30/2005 Memorandum and Order at 41.) 3M argues that, due to the general nature of the verdict rendered in *LePage*'s, it impossible to discern the exact time period for which the jury in *LePage*'s found that 3M possessed monopoly power, willfully maintained such power, and harmed competition. Accordingly, 3M contends that it was incorrect for the Court to apply collateral estoppel to the jury's findings in *LePage*'s for the entire period from June 11, 1993 to October 13, 1999.

The jury in *LePage*'s returned a general verdict which contained no special interrogatories relating to the time period during which it found that 3M had [\*22] engaged in unlawful conduct. Similarly, the jury charge did not instruct the jury to find that 3M had acted in violation of [section 2](#) from June 11, 1993 until the present. Consequently, the Court agrees that although the jury in *LePage*'s considered evidence for the period from June 11, 1993 until October 13, 1999, the date on which the jury rendered its verdict, it is not possible to infer from the jury's verdict that 3M had engaged in unlawful conduct throughout the entire June 11, 1993 to October 13, 1999 period of time. Collateral estoppel, therefore, can only be applied to establish that 3M engaged in unlawful behavior for some period of time between June 11, 1993 and October 13, 1999. Accordingly, the Court reconsiders its March 30, 2005 Memorandum and Order with respect to the application of collateral estoppel for the period of time from June 11, 1993 through October 13, 1999, and finds that collateral estoppel is properly applied to establish only that, for some period of time between June 11, 1993 and October 13, 1999, 3M possessed monopoly power, willfully

maintained such power and harmed competition. 3M's Motion for Reconsideration is, therefore, granted in this respect. **[\*23]**<sup>6</sup>

#### IV. CONCLUSION

For the foregoing reasons, 3M's Motion for Reconsideration is granted in part and denied in part. As 3M's Motion for Reconsideration grants 3M substantial relief, the Court further concludes that it need not reach 3M's alternative Motion for Certification of Interlocutory Appeal. Should 3M desire certification of this matter for interlocutory appeal despite the Court's reconsideration of its March 30, 2005 Memorandum and Order, 3M may renew its Motion within ten days of the date of this Memorandum and Order.

An appropriate Order follows.

#### **ORDER**

**AND NOW**, this 9th day of June, 2005, upon consideration of Defendant 3M's Motion for Reconsideration of March 30, 2005 Order (Doc. No. 215), all documents **[\*24]** submitted in response thereto, and the Argument held on May 9, 2005, **IT IS HEREBY ORDERED** that said Motion is **GRANTED IN PART** and **DENIED IN PART**, and the Court's March 30, 2005 Memorandum and Order (Doc. No. 211) **IS HEREBY AMENDED** to read as follows:

1. For the time period from June 11, 1993 and October 13, 1999, the relevant market in this matter is the market for invisible and transparent tape for home and office use in the United States;
2. For some period of time between June 11, 1993 and October 13, 1999, 3M possessed monopoly power in the relevant market, including the power to control prices and exclude competition in the relevant market;
3. For some period of time between June 11, 1993 and October 13, 1999, 3M willfully maintained such monopoly power by predatory or exclusionary conduct; and
4. For some period of time between June 11, 1993 and October 13, 1999, 3M's predatory or exclusionary conduct harmed competition.

**IT IS FURTHER ORDERED** that 3M's alternative Motion for Certification of Interlocutory Appeal (Doc. No. 215) is **DISMISSED AS MOOT WITHOUT PREJUDICE** to renew said Motion within ten days of the date **[\*25]** of this Order.

BY THE COURT:

/s/ John R. Padova, J.

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<sup>6</sup>The Court notes that this amendment to the March 30, 2005 Memorandum and Order has no impact on this Court's determination that the application of collateral estoppel in this case is fair to 3M and will serve judicial economy. See (03/30/2005 Memorandum and Order at 27-41.)

## **Novell, Inc. v. Microsoft Corp. (In re Microsoft Corp. Antitrust Litig.)**

United States District Court for the District of Maryland

June 10, 2005, Decided

MDL 1332, Civil No. JFM-05-1087

**Reporter**

2005 U.S. Dist. LEXIS 11520 \*; 2005-1 Trade Cas. (CCH) P74,830

In Re: Microsoft Corp. Antitrust Litigation; Novell, Inc. v. Microsoft Corp.

**Subsequent History:** Motion granted by [Novell, Inc. v. Microsoft Corp. \(In re Microsoft Corp. Antitrust Litig.\), 2005 U.S. Dist. LEXIS 17988 \(D. Md., Aug. 19, 2005\)](#)

Affirmed by [Novell, Inc. v. Microsoft Corp., 2007 U.S. App. LEXIS 24101 \(4th Cir. Md., Oct. 15, 2007\)](#)

**Prior History:** [Peek v. Microsoft Corp. \(In re Microsoft Corp. Antitrust Litig.\), 2005 U.S. Dist. LEXIS 10935 \(D. Md., June 3, 2005\)](#)

## **Core Terms**

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operating system, tolled, monopoly, markets, antitrust, Counts, anticompetitive, asserted claim, monopolization, word processing, spreadsheet, competitor, damages

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

### **HN1[ Private Actions, Standing]**

Competitors and consumers in a given market are favored plaintiffs, and, just as certainly, the list of those presumptively disfavored is far longer. However, the U.S. Supreme Court has not established a litmus test for antitrust standing based upon a plaintiff's status. Rather, the Court has instead articulated a series of factors to be considered in deciding the standing question.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Tolling

### **HN2[ Private Actions, Remedies]**

Under [15 U.S.C.S. § 16\(i\)](#) the limitations period is tolled for every private right of action based in whole or in part on any matter complained of in an antitrust action brought by the United States.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Tolling

#### [\*\*HN3\*\*](#) **Private Actions, Remedies**

A party cannot be permitted to circumvent the purpose of [15 U.S.C.S. § 16\(i\)](#) by simply joining tolled and untolled claims in the same complaint.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Tolling

#### [\*\*HN4\*\*](#) **Private Actions, Remedies**

The governing test for whether a claim is tolled under [15 U.S.C.S. § 16\(i\)](#) is whether the matters complained of in the private action "bear a real relation" to a matter complained of in the government suit. The private plaintiff is not required to allege that the same means were used to achieve the same objectives of the same conspiracies by the same defendants, but simply must allege a significant, although incomplete, overlap of subject matter to toll the statute, even as to the differences. In general, consideration of the applicability of [§ 16\(i\)](#) must be limited to a comparison of the two complaints on their face. [Section 16\(i\)](#) is not to be given a niggardly construction and must be read in light of Congress' belief that private antitrust litigation is one of the surest weapons for effective enforcement of the antitrust laws.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Tolling

#### [\*\*HN5\*\*](#) **Private Actions, Remedies**

Limitations are not tolled under [15 U.S.C.S. § 16\(i\)](#) when the government and subsequent private suits arose in distinct markets. That proposition is supported by cases which hold that differences between geographic and product markets in the government suits and private actions prevented tolling under [§ 16\(i\)](#).

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Tolling

#### [\*\*HN6\*\*](#) **Private Actions, Remedies**

While [15 U.S.C.S. § 16\(i\)](#) properly serves the purpose of permitting private plaintiffs to wait to bring private claims encompassed within a government enforcement action until that action has come to an end, it should not be construed to permit private plaintiffs to sit on their rights and assert claims so much broader than those asserted by the government that they open entirely new vistas of litigation.

**Counsel:** [\*1] For Novell, Inc., Plaintiff: Jeffrey M Johnson, David L Engelhardt, Milton A Marquis, R Bruce Holcomb, Dickstein Shapiro Morin and Oshinsky LLP, Washington, DC; Max D Wheeler, Stanley J Preston, Snow Christensen and Martineau, Salt Lake City, UT.

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**Judges:** J. FREDERICK MOTZ, UNITED STATES DISTRICT JUDGE.

**Opinion by:** J. FREDERICK MOTZ

## Opinion

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Dear Counsel:

As I mentioned at the close of the hearing held on June 7, 2005, there is a series of motions pending in another proceeding in which I am involved to which I will have to turn my attention in the coming weeks. I expressed to you my concern that as a result, it might take me more time than I would like to rule upon Microsoft's motion to dismiss in this case. After the hearing, however, I concluded that [\*2] close and difficult though the issues are, I am prepared to decide them now, particularly while your excellent arguments are still fresh in my mind.

It is neither in your interest nor in the public interest to delay resolution of your dispute any longer. Therefore, instead of postponing my rulings until my schedule would permit me to write a more extensive opinion, I have decided to issue my rulings now, setting forth my reasoning in this short memorandum to you. I hope you understand that the form and nature of the opinion does not mean that I have not considered the questions presented as thoroughly and carefully as I can. As I have previously done in these MDL proceedings, I am simply following my own adage of "writing for the parties, not for the ages."

Microsoft's motion is denied as to Counts I and VI but granted as to Counts II, III, IV, and V.

### Counts I and VI

In Count I Novell alleges that Microsoft unlawfully "obtained and maintained its monopoly power in the Intel-compatible operating systems market by engaging in anticompetitive conduct" and that as a result Novell was damaged, specifically through lost sales of "office productivity applications" (including WordPerfect, [\*3] a word processing program, and Quattro Pro, a spreadsheet program). Microsoft acknowledges that the claim asserted in Count I is not time-barred because the focus of the government case against Microsoft (during the pendency of which limitations of private rights of action were tolled under [15 U.S.C. § 16\(i\)](#)) was upon Microsoft's monopoly in the operating system market. Count VI is based upon Microsoft's exclusionary agreements with OEMs, which allegedly were in unreasonable restraint of trade. Although Microsoft does not expressly concede the point, such agreements also were a subject of the government case. Thus, limitations has been tolled as to the claim asserted in Count VI.

In regard to Count I Microsoft makes two contentions, neither of which is meritorious. First, it argues that Novell no longer owns the claim asserted in that count because it transferred the claim to Caldera in connection with the sale of the DOS operating system, related technology, and claims relating "directly or indirectly" to it. The fallacy in this argument is that the claim asserted in Count I, while arising from Microsoft's monopoly in the operating system market, is for damage [\*4] not to DOS or any other operating system but for damage to applications software. It is a far stretch to infer (and Microsoft has presented nothing to establish) that simply because DOS competed in the

operating system market, such a claim was either a "direct" or "indirect" claim intended to be transferred from Novell to Caldera. Of course, Novell did also have claims against Microsoft for damage caused to DOS and related technology, but these claims (which were settled after Caldera sued Microsoft) are not part of the present action.

Microsoft next argues that Novell lacks antitrust standing as to Count I because the office productivity applications alleged to have been damaged did not compete in the operating system market. According to Microsoft, there is a black-letter rule that only competitors or consumers in a relevant market have standing to sue for harm caused by anti-competitive behavior in that market. Microsoft overstates the proposition. Certainly, [HN1](#) [↑] competitors and consumers in a given market "are favored plaintiffs," and, just as certainly, "the list of those presumptively disfavored is far longer." [SAS of Puerto Rico, Inc. v. Puerto Rico Tel. Co., 48 F.3d 39, 45 \(1st Cir. 1995\)](#). [\*5] See also [White v. Rockingham Radiologists, Ltd., 820 F.2d 98, 104 \(4th Cir. 1987\)](#); [Lucas v. Bechtel Corp., 800 F.2d 839, 845-46 \(9th Cir. 1986\)](#). However, the Supreme Court has not established a litmus test for antitrust standing based upon a plaintiff's status. Rather, in [Associated General Contractors v. California State Council of Carpenters, 459 U.S. 519, 74 L. Ed. 2d 723, 103 S. Ct. 897 \(1983\)](#), the Court -- while pointing out that the plaintiff whom it found not to have antitrust standing "was neither a consumer nor a competitor in the market in which trade was restrained," [id. at 539](#) -- did not simply rely upon that fact but instead articulated a series of factors to be considered in deciding the standing question. [Id. at 537-45](#).

In the present case the gravamen of the claim asserted in Count I is that Microsoft specifically targeted Novell for the purpose of maintaining its monopoly in the operating system market. According to Novell, WordPerfect and Quattro Pro, its popular office productivity applications, posed a threat to Microsoft's operating system monopoly because Novell had engineered them to exploit Novell's existing [\*6] cross-platform technologies, such as OpenDoc and AppWare. Moreover, because these applications were being developed to run independently of any operating system, particularly Windows, and because the consumer demand for them was great, Microsoft saw the need to attack them. In support of this view, Novell, citing an internal Microsoft email, contends that "Microsoft recognized that it had to control the office productivity applications market to fend off that threat to its operating systems monopoly." The Microsoft email stated as follows:

If we own the key franchises' built on top of the operating system, we dramatically widen the "moat" that protects the operating system business. . . . We hope to make a lot of money off these franchises, but even more important is that they should protect our Windows royalty per PC. . . . And success in those businesses will help increase the opportunity for future pricing discretion.

E-mail from Jeff Raikes, Microsoft, to Warren Buffet (Aug. 17, 1997).

Novell also alleges that it was a company of particular concern to Microsoft. Paragraph 7 of the Complaint avers:

Bill Gates, Microsoft's Chairman and Chief Executive Officer, [\*7] targeted Novell's applications by name in documents recording Microsoft's anticompetitive schemes, in which he explained that the integration of browsing functions into Windows, coupled with Microsoft's refusal to publish certain of these functions, was a primary strategy for excluding Novell's applications from the markets. He candidly admitted that Microsoft's own products could not compete without the benefit of these anticompetitive acts.

Against this background, it is clear to me that Novell meets the various parts of the multi-factored test established by [Associated General Contractors](#) for antitrust standing. First, there is a direct causal connection between the anticompetitive acts Microsoft allegedly took against Novell's office productivity applications for the purpose of maintaining its operating systems monopoly and the damage claimed in Count I. Second, Microsoft allegedly targeted Novell specifically because it perceived Novell as an innovator in the industry. This targeting demonstrates that, at the least, Microsoft perceived Novell to be a competitor. See [Reazin v. Blue Cross & Blue Shield of Kan., Inc., 899 F.2d 951, 962-63 \(10th Cir. 1990\)](#). [\*8] Third, destruction of a competitor's product for the purpose of maintaining a monopoly self-evidently is the type of harm for which the antitrust laws are intended to provide redress. Fourth, Novell's claim is direct and straightforward. Fifth, although there were other victims of other anticompetitive acts committed by Microsoft for the purpose of maintaining its monopoly in the operating system market, Novell is the only victim who could bring suit for the acts taken by Microsoft in regard to WordPerfect and

Quattro Pro -- acts which ultimately had an enormous impact upon the shape of the applications software market.<sup>1</sup> Finally, no problem of speculative damages or complex apportionment of damages is presented because Novell is the only person with a claim for the damages it allegedly suffered in connection with WordPerfect and Quattro Pro between 1994 and 1996 when it sold those products to Corel.

[\*9] 2. Counts II, III, IV, and V

**HN2** Under [15 U.S.C. § 16\(i\)](#) the limitations period is tolled for "every private right of action . . . based in whole or in part on any matter complained of" in an antitrust action brought by the United States. For the reasons I have just stated, I find that the claims asserted in Counts I and VI are tolled under this section. As Microsoft contends, however, the mere fact that limitations are tolled as to two counts in a complaint is not sufficient to toll all other counts in the complaint. [Section 16\(i\)](#) refers not to "complaints" but to "right[s] of action," and self-evidently **HN3** a party cannot be permitted to circumvent the purpose of the statute by simply joining tolled and untolled claims in the same complaint

The broad principles governing the tolling issue may be briefly stated. **HN4** The governing test is whether the matters complained of in the private action "bear a real relation" to a matter complained of in the government suit. [Leh v. Gen. Petroleum Corp., 382 U.S. 54, 59, 15 L. Ed. 2d 134, 86 S. Ct. 203 \(1965\)](#). "The private plaintiff is not required to allege that the same means were used to achieve the same objectives of the same conspiracies [\*10] by the same defendants," [id. at 59](#), but simply must allege "a significant, although incomplete, overlap of subject matter" to toll the statute, "even as to the differences." [Morton's Market, Inc. v. Gustafson's Dairy, Inc., 198 F.3d 823, 830 \(11th Cir. 1999\)](#). "In general, consideration of the applicability of . . . [section 16(i)] must be limited to a comparison of the two complaints on their face." [Leh, 382 U.S. at 65; Greyhound Corp. v. Mt. Hood Stages, Inc., 437 U.S. 322, 331, 57 L. Ed. 2d 239, 98 S. Ct. 2370 \(1978\).](#)<sup>2</sup> [Section 16\(i\)](#) is not to be given a "niggardly construction" and must be "read in light of Congress' belief that private antitrust litigation is one of the surest weapons for effective enforcement of the antitrust laws." [Leh, 382 U.S. at 59](#) (quoting [Minn. Mining & Mfg. Co. v. N.J. Wood Finishing Co., 381 U.S. 311, 318, 14 L. Ed. 2d 405, 85 S. Ct. 1473 \(1965\)](#)).

[\*11] In its complaint in this action, Novell refers frequently to allegations and findings made in the government case against Microsoft. These reference are incorporated by reference into counts II through V. Those counts, however, assert claims for monopolization and attempted monopolization in the word processing and spreadsheet applications markets: claims that were never asserted by the government. While there was a single conclusory averment in the government's complaint that Microsoft engaged in anticompetitive activities both to protect its operating system monopoly and "to extend . . . [that] monopoly into other software markets," Gvt. Compl., at P 5, the only markets defined and focused upon in the government complaint were the operating system and browser markets. Word processing and spreadsheet programs are specifically mentioned only once in the government

<sup>1</sup> It would seem that an implication of Microsoft's contention that Novell lacks antitrust standing as to the claim asserted in Count I is that Sun and Netscape also lacked antitrust standing to the extent that they were not direct competitors in the operating system market, i.e., owners of alternative operating systems, but rather developers of middleware products that threatened to render Microsoft's operating system obsolete. Even if that is not so, however, I am satisfied that for the reasons I have stated, Novell may (just as Netscape and Sun did) assert antitrust claims for harm allegedly caused to its non-operating system products as a result of Microsoft's anticompetitive behavior designed to protect its Windows monopoly.

<sup>2</sup> As Novell notes, several courts have glimpsed at the record in the government suit in order to evaluate the comparability of the government and private actions. See, e.g., [Morton's Market, 198 F.3d at 830-32](#). That approach, however, does not provide any greater support for Novell than does a simple comparison of its complaint and the complaint in the United States' action against Microsoft. The record in the government suit confirms that while an occasional expert may have referred to abuses that occurred in related software markets, those references did not result in any charge of monopolization or attempted monopolization in the office productivity applications market. Indeed, the greatest difference between the complaint in the government action and the ultimate resolution of the case was that whereas the complaint alleged anticompetitive behavior both in the operating system market and in a browser market, the Court of Appeals ultimately found that the evidence did not substantiate the existence of the latter market. [United States v. Microsoft, 346 U.S. App. D.C. 330, 253 F.3d 34, 81-81 \(D.C. Cir. 2001\)](#).

complaint, and only in the section describing the operating system market and only as applications that are "controlled" and "directed" by operating systems. *Id.* at P 54.

Novell accepts, as of course it must, that operating systems and office productivity applications are distinct products and are in [\*12] separate markets. It also accepts as "unremarkable" the bright-line rule stated by Professor Areeda that HN5[<sup>↑</sup>] limitations are not tolled when "the government and subsequent private suits . . . arose in distinct markets." 2 Philip E. Areeda & Herbert Hovenkamp, Antitrust Law P 321a, at 241 (2d ed. 2000). That proposition is supported by such cases as In re Coordinated Pretrial Proceedings in Petroleum Products Antitrust Litigation, 782 F. Supp. 481 (C.D. Cal. 1991), and Charley's Tour and Transportation, Inc. v. Interisland Resorts, Ltd., 618 F. Supp. 84 (D. Haw. 1985), which held, respectively, that differences between geographic and product markets in the government suits and private actions prevented tolling under Section 16(i). Novell argues, however, that because the operating system and applications markets are closely, indeed symbiotically related, this bright-line rule should not apply. Cf. In re Arizona Dairy Prods. Litig., 1984 U.S. Dist. LEXIS 22199, No. CIV 74-569A (D. Ariz. Nov. 5, 1984)(finding claim for private action for price-fixing conspiracy in retail milk market tolled based on government suit for price-fixing conspiracy in wholesale milk market); In re Antibiotic Antitrust Actions, 333 F. Supp. 317, 320-21 (S.D.N.Y. 1971) [\*13] (finding claim for damage suffered in a foreign market for agricultural consumption tolled by government suit for conduct in domestic market relating to human consumption). I am not persuaded. The nature of the relationship between the markets is important to an understanding of the dynamics of the industry, and it is central to my earlier holding that Novell has antitrust standing for harm allegedly caused to WordPerfect and Quattro Pro by Microsoft's maintenance of its Windows monopoly. However, the government case focused solely upon the operating system market (and an asserted browser market, ultimately found by the Court of Appeals to be unsubstantiated by the evidence), and Novell has provided no adequate explanation for not applying the bright-line rule recited by Professor Areeda in this case.

Undoubtedly, if the government had pursued additional charges of monopolization and attempted monopolization in the word processing and spreadsheet markets, there would have been some overlap in evidence concerning the conduct in which Microsoft engaged. However, the government deliberately chose not to lodge any such charges,<sup>3</sup> and in my judgment the existence of such a potential overlap [\*14] does not justify tolling under Section 16(i). HN6[<sup>↑</sup>] While Section 16(i) properly serves the purpose of permitting private plaintiffs to wait to bring private claims encompassed within a government enforcement action until that action has come to an end, it should not be construed to permit private plaintiffs to sit on their rights and assert claims so much broader than those asserted by the government that they open entirely new vistas of litigation. If Novell wanted to assert claims for monopolization and attempted monopolization in the word processing and spreadsheet markets, it should have done so long ago. Its inaction entitles Microsoft to the comfort of repose. Cf. Greyhound Corp. v. Mt. Hood Stages, Inc., 437 U.S. 322, 334, 57 L. Ed. 2d 239, 98 S. Ct. 2370 (1978)(citing Dungan v. Morgan Drive-Away, Inc., 570 F.2d 867, 869 (1978) for the proposition that the limitations statute is one of "repose").

[\*15] Despite the informal nature of this letter, it should be flagged as an opinion and docketed as an order.

Very truly yours,

June 10, 2005

J. Frederick Motz

United States District Judge

<sup>3</sup>That such a charge could have been asserted certainly was not unknown. State Attorney Generals originally included a claim for harm for a market for office productivity applications in the complaint they filed. (See Complaint filed in *New York v. Microsoft Corp.* PP 88-95, 98, 117-19, No. 98-1233 (D.D.C. filed May 18, 1998)). Of course, the filing of this claim did not toll limitations because section 16(i) applies only to actions brought by the United States. In any event, within two months the Attorney Generals abandoned that claim when filing an amended complaint. (See First Amended Complaint filed in *New York v. Microsoft Corp.*, No. 98-1233 (D.D.C. filed July 17, 1998)).

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## J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc.

United States District Court for the Southern District of Ohio, Western Division

June 13, 2005, Decided ; June 13, 2005, Filed

Case No. 1:01-cv-704, Case No. 1:03-cv-781

**Reporter**

2005 U.S. Dist. LEXIS 11676 \*; 2005 WL 1396940

J.B.D.L. Corp., d/b/a Beckett Apothecary, et al., Plaintiffs, vs. Wyeth-Ayerst Laboratories, Inc., et al., Defendants. CVS Meridian, Inc. and Rite Aid Corp., Plaintiffs, vs. Wyeth, Defendant.

**Subsequent History:** Affirmed by [J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc., 485 F.3d 880, 2007 U.S. App. LEXIS 11003 \(6th Cir.\), 2007 FED App. 168P \(6th Cir. Ohio, May 10, 2007\)](#)

**Prior History:** [J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc., 225 F.R.D. 208, 2003 U.S. Dist. LEXIS 26082 \(S.D. Ohio, May 12, 2003\)](#)

[Ferrell v. Wyeth-Ayerst, Labs., Inc., 2004 U.S. Dist. LEXIS 15127 \(S.D. Ohio, June 30, 2004\)](#)

**Disposition:** [\*1]

## Core Terms

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contracts, products, competitors, rebates, formulary, pricing, market share, estrogen, Plaintiffs', antitrust, increased price, manufacturers, sales, pharmaceutical, discounts, pharmacy, retail, relevant market, prescription, conjugated, purchases, summary judgment, district court, marketing, placement, purposes, anti-competitive, generic, summary judgment motion, exclusionary

## LexisNexis® Headnotes

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

Civil Procedure > ... > Summary Judgment > Supporting Materials > Discovery Materials

**HN1** [] Entitlement as Matter of Law, Appropriateness

The standards for summary judgment are well established. Summary judgment is proper if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. [Fed. R. Civ. P. 56\(c\).](#)

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

## [\*\*HN2\*\*](#) **Summary Judgment, Opposing Materials**

The party opposing a properly supported summary judgment motion may not rest upon the mere allegations or denials of his pleading, but must set forth specific facts showing that there is a genuine issue for trial. The court is not duty bound to search the entire record in an effort to establish a lack of material facts. Rather, the burden is on the non-moving party to present affirmative evidence to defeat a properly supported motion for summary judgment, and to designate specific facts in dispute.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

## [\*\*HN3\*\*](#) **Burdens of Proof, Movant Persuasion & Proof**

The non-moving party upon a motion for summary judgment must do more than simply show that there is some metaphysical doubt as to the material facts.

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

## [\*\*HN4\*\*](#) **Summary Judgment, Evidentiary Considerations**

The court upon a motion for summary judgment construes the evidence presented in the light most favorable to the non-movant and draws all justifiable inferences in the non-movant's favor. The court's function is not to weigh the evidence and determine the truth of the matter, but to determine whether there is a genuine issue for trial. The court must assess whether there is the need for trial -- whether, in other words, there are any genuine factual issues that properly can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party. If the evidence is merely colorable, or is not significantly probative, the court may grant judgment.

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Scintilla Rule

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN5** **Summary Judgment, Evidentiary Considerations**

Upon a motion for summary judgment, the mere existence of a scintilla of evidence in support of the plaintiff's position will be insufficient; there must be evidence on which the jury could reasonably find for the plaintiff. The judge's inquiry, therefore, unavoidably asks whether reasonable jurors could find by a preponderance of the evidence that the plaintiff is entitled to a verdict. Hence the "mere possibility" of a factual dispute will not suffice.

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

#### **HN6** **Summary Judgment, Evidentiary Considerations**

Summary judgment is not appropriate simply because the weight of the evidence favors the moving party. The issue of material fact required to entitle a party to proceed to trial is not required to be resolved conclusively in favor of the party asserting its existence; rather, all that is required is that sufficient evidence supporting the claimed factual dispute be shown to require a jury or judge to resolve the parties' differing versions of the truth at trial.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN7** **Summary Judgment, Entitlement as Matter of Law**

Although summary judgment must be used with extreme caution since it operates to deny a litigant his day in court, the United States Supreme Court has stated that the summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to secure the just, speedy and inexpensive determination of every action.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > Sherman Act

#### **HN8** **Antitrust & Trade Law, Sherman Act**

The Sherman Act, [15 U.S.C.S. § 1](#), prohibits contracts or agreements that unreasonably restrain trade or commerce. The contracts at issue in this case are evaluated under the "rule of reason" test. This analysis must take into account a variety of factors, including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint's history, nature, and effect. The first, and critical, step in any rule of reason analysis is that the plaintiff must prove that the challenged action has had an actual adverse effect on

competition as a whole in the relevant market. Under the rule-of-reason analysis, the antitrust plaintiff must show, *inter alia*, an adverse effect on competition.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > Exclusive Dealing

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

#### **HN9** [down] Exclusive & Reciprocal Dealing, Exclusive Dealing

Exclusivity provisions in contracts can serve useful, pro-competitive purposes. It is only when such provisions cross the line into the arena of exclusive dealing that substantially and negatively affects market competition, that the antitrust statutes, including the Sherman Act, [15 U.S.C.S. § 1](#), come into play.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > Exclusive Dealing

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

#### **HN10** [down] Exclusive & Reciprocal Dealing, Exclusive Dealing

Exclusive dealer contracts did not violate the Sherman Act, [15 U.S.C.S. § 1](#), where the defendant's actions do not foreclose competitors from gaining a foothold in the market.

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

#### **HN11** [down] Sherman Act, Claims

A claim under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), requires proof of two elements: (1) the possession of monopoly power in a relevant market; and (2) the willful acquisition, maintenance, or use of that power by anti-competitive or exclusionary means as opposed to growth or development resulting from a superior product, business acumen, or historic accident.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN12** [blue icon] Monopolies & Monopolization, Actual Monopolization

"Monopoly power" for purposes of [15 U.S.C.S. § 2](#) can be something greater than market power under [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > Predatory Pricing

## **HN13** [blue icon] Monopolies & Monopolization, Actual Monopolization

The United States Supreme Court has acknowledged the viability of [15 U.S.C.S. § 2](#) claims brought by a competitor that go beyond allegations of predatory pricing.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

Antitrust & Trade Law > Sherman Act > General Overview

## **HN14** [blue icon] Monopolies & Monopolization, Attempts to Monopolize

Unlawful exclusionary conduct for purposes of Sherman Act, [15 U.S.C.S. § 2](#), liability has been described as acts that are reasonably capable of creating, enlarging or prolonging monopoly power by impairing the opportunities of rivals and that either do not benefit consumers at all, are unnecessary for the particular consumer benefits that the acts produce, or produce harms disproportionate to the resulting benefits. To this end, it must be kept in mind that when considering an allegation of exclusionary or anti-competitive conduct, the antitrust laws are intended to protect competition, not a competitor.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

## **HN15** [blue icon] Monopolies & Monopolization, Actual Monopolization

Exclusionary conduct that uses above-cost price discounting is actionable under [Section 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

## **HN16** [blue icon] Monopolies & Monopolization, Actual Monopolization

Under the best of circumstances, applying the requirements of [section 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), can be difficult because the means of illicit exclusion, like the means of legitimate competition, are myriad. Mistaken inferences and the resulting false condemnations are especially costly, because they chill the very conduct the antitrust laws are designed to protect.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN17** [ ] **Private Actions, Remedies**

A private plaintiff may not recover damages under the antitrust laws merely by showing an injury causally linked to an illegal presence in the market. Antitrust laws are intended to prevent injuries to competition, and thus provide a remedy only for those losses that stem from the competition-reducing aspects of a defendant's conduct. There must be a distinct causal link between that challenged conduct, and the harm which Plaintiffs allege they have suffered. The United States Court of Appeals for the Sixth Circuit has been zealous in ensuring that this element of an antitrust claim is satisfied.

**Counsel:** For JBDL Corporation, individually and on behalf of all others similarly situated doing business as Beckett Apothecary, Plaintiff: Jay S Cohen, Eugene A Spector, Spector Roseman & Kodroff PC, Philadelphia, PA; John Charles Murdock, Theresa L. Groh, Murdock Goldenberg Schneider & Groh LPA, Cincinnati, OH; Kendall S Zylstra, Schiffriin & Barroway LLP, Radnor, PA; Ruthanne Gordon, David F Sorensen, Eric L Cramer, H Laddie Montague, Peter Kohn, Berger & Montague PC, Philadelphia, PA; Andrew Kelly, Stuart Des Roches, Odom & Des Roches, LLC, New Orleans, LA.

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For Wyeth-Ayerst Laboratories Inc, Defendant: Grant Spencer Cowan, James Ralph Adams, Frost Brown Todd LLC, Cincinnati, OH; Mark R Merley, David S Eggert, Matthew D Meisner, Son B Nguyen, William J Baer, Arnold & Porter LLP, Washington, DC; Asim Varma, Douglas L Wald, Arnold & Porter, Washington, DC; Brian D Werner, Brooke B Ward, Dan K Webb, Peggy M Balesteri, W Gordon Dobie, Winston & Strawn, Chicago, IL.

For American Home Products Corporation, Defendant: Grant Spencer Cowan, James Ralph Adams, Frost Brown Todd LLC, Cincinnati, OH; Mark R Merley, Arnold & Porter, Washington, DC.

**Judges:** Sandra S. Beckwith, Chief Judge, United States District Judge.

**Opinion by:** Sandra S. Beckwith

## **Opinion**

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### ORDER

#### I. Introduction

Plaintiff J.B.D.L. Corp., for itself and a class of direct purchasers, alleges that Defendants Wyeth and Wyeth [\*3] Pharmaceuticals (collectively "Wyeth"), violated the [Sherman Act](#). Plaintiffs CVS Meridian and Rite Aid Corporation opted out of the J.B.D.L. class, and filed a separate Sherman Act complaint. All Plaintiffs contend that they were

forced to pay a supracompetitive price for Wyeth's drug Premarin because Wyeth engaged in anti-competitive and exclusionary conduct towards one of its rivals, Duramed.

The Court has studied the extensive briefs filed by all parties in connection with Wyeth's motion for summary judgment. The Court finds that oral argument would not aid the Court in resolving the motion. The Court will grant Wyeth's motion and enter judgment in favor of Wyeth.

## II. Factual Background

Wyeth manufactures Premarin. Premarin is Wyeth's trade name for its conjugated estrogen product approved for several therapeutic purposes: for treatment of vasomotor symptoms associated with menopause; treatment of vulval and vaginal atrophy; and to prevent osteoporosis, along with more specialized uses for more rare medical conditions. See Carlton Deposition, Table 1 (Doc. 135, Appendix C-1). Wyeth has manufactured and sold Premarin since 1942. No one disputes the fact that Premarin is [\*4] the largest selling estrogen replacement drug (and one of the largest selling prescription medications) in the United States.

Premarin is an **estrogen** replacement drug. Estrogen replacement therapy (ERT) is typically prescribed for women without a uterus (as after a hysterectomy). Wyeth also manufactures products for use in **hormone** replacement therapy, which involves a combination of estrogen and progestin. Hormone replacement therapy (HRT) is typically prescribed for women with intact uteruses. The two categories of therapy are related but are distinct. Premarin can be used in combination with progestin in HRT. Wyeth's products PremPro and Premphase combine estrogen and progestin into one dose.

For all of the relevant time periods, several other ERT products were available in the market. None, however, were "conjugated" estrogen products, as is Premarin. There are no generic equivalents of Premarin approved by the FDA.

Duramed<sup>1</sup> manufactures Cenestin, its trade name for a newer conjugated estrogen product. Duramed obtained FDA approval to market Cenestin as a branded pharmaceutical in March 1999. Duramed had originally attempted to gain FDA approval of Cenestin as a [\*5] generic equivalent to Premarin, but was not successful. It is important to note that Premarin and Cenestin are not therapeutic equivalents. See, e.g., Wyeth's Exhibit B-3, an FDA "Question and Answer" sheet about Cenestin. Cenestin, unlike Premarin, is not approved for long-term use, and thus cannot be prescribed for the prevention of osteoporosis.

Wyeth kept itself well informed of Duramed's efforts to secure FDA approval for Cenestin. Indeed, much of Plaintiffs' recitation of facts in opposition to Wyeth's motion for summary judgment is devoted to a review of Wyeth's documentation of the progress of its rival through the FDA process, and Wyeth's plans to address the impact of Cenestin's entry into the marketplace. Plaintiffs repeatedly refer to Wyeth's "Premarin Preemptive Plan", dated February 11, 1999 (Class Plaintiffs Exhibit P96, Doc. 143), as the key component of Wyeth's anti-competitive [\*6] conduct.

The "Plan" was a multi-faceted market strategy to maintain Premarin's dominant market share. One of its stated objectives was to hold "Cenestin to less than two percent of prescription market share in 1999, approximately \$ 20 million in assumed sales." (*Id.* at WYE 132253). One part of the Plan was a demonstration for retail pharmacies on the advantageous pricing of Premarin vs. Cenestin, which Wyeth estimated would be priced below the average wholesale price (AWP) of Premarin. The demonstration showed that a pharmacy filling an ERT prescription would increase its net revenue by filling the prescription with the more expensive Premarin. Another part of the Plan was to advertise and promote Premarin's clinical differences - primarily its long-term use approval - and its longer track record. And yet another part of the "Plan" presented a strategy of limiting Duramed's "contracting opportunities" with third party payors, with whom Wyeth had in place various contracts. The "value" of these contracts to the third party payors is in the rebates Wyeth was paying for sales of various Wyeth products.

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<sup>1</sup> Duramed Pharmaceuticals was purchased by Barr Laboratories in 2001. The company will be referred to as "Duramed" in this Order.

Wyeth kept a close eye on its market competitors. While Plaintiffs suggest this [\*7] is part of Wyeth's anti-competitive scheming, such conduct appears to be a rational part of any market seller's business planning. See, for example, Class Plaintiffs Exhibit 97 (Doc. 143), a Wyeth "Premarin Family Business Brief" from June 21, 1999, that summarizes "Competitive Activity" from Duramed's Cenestin, but also from EVISTA, Lilly's Raloxifene, and a potential new entrant called "Activelle." In fact Wyeth appears to be closely tracking the effects of the March 1998 launch of EVISTA on its product sales; see WYE 089614 and 089621 (Class Plaintiffs Exhibit 97), showing that Premarin prescriptions actually declined (as a share of Wyeth family product sales) after EVISTA's market entry.

**A. Wyeth's PBM Contracts:** The record in this case fairly establishes that rebate and "access" contracts between pharmaceutical manufacturers and third party payors are a widespread industry practice. See, e.g., deposition testimony of Dr. White, chief clinical officer of HealthNet, at pp. 180-82 (Wyeth's Exhibit E-21, Doc. 135); Dept. of Health & Human Services, "Report to the President - Prescription Drug Coverage, Spending, Utilization, and Prices" (April 2000) (excerpts at Exh. B-9, Doc. [\*8] 135). The "third party payors" include not only traditional HMOs or insurers, but "pharmacy benefit managers" (PBMs). In overly simplistic terms, the rise of managed care, coupled with an increasing concern among employers and insurers with rising health care costs, created the pharmacy benefit manager and the drug formulary. (Some insurers manage plan pharmacy benefits internally, while others use an independent entity. For ease of reference, the Court will refer to both of these types of arrangements simply as "PBMs".)

The Plaintiffs generally contend that Wyeth's rebate/formulary contracts with many large PBMs permitted Wyeth to illegally maintain its monopoly in the ERT market, and to raise its prices after Cenestin's entry into the marketplace. Plaintiffs and their experts argue that the synergistic effects of Wyeth's "sole conjugated estrogen" clauses together with Wyeth's formulas for rebates to PBMs, effectively foreclosed competition from Duramed's Cenestin.

The PBM is not involved in the actual sales transaction for the pharmaceuticals it "manages." Rather, the PBM negotiates both with the pharmaceutical manufacturers and the pharmacies that actually fill the prescriptions [\*9] (many of the direct purchasers here). Manufacturers contract with a PBM for favorable formulary placement, or exclusive formulary listing in a given therapeutic drug classification. Manufacturers pay for these placements with rebates and other incentive payments.

The PBM also negotiates contracts with the pharmacies that actually buy the drugs and fill the plan members' prescriptions. These contracts are price contracts. Dr. White, of HealthNet, discussed this aspect of PBM contracts. She testified that, generally, the PBM-pharmacy contracts specify a reimbursement rate composed of the drug cost and a dispensing fee. For branded drugs, the cost is generally based on the average wholesale price of the drug less a negotiated discount. Dispensing fees also vary depending on the pharmacy and geographic location. Under the type of contract terms Dr. White describes, if the average wholesale price of a drug should go up, the pharmacy's reimbursement from the PBM would also go up.

Wyeth submitted copies of its PBM contracts (Doc. 135, Exhibits H-1 through H-95). One of these contracts that the Plaintiffs analyze is with PCS Health Services, and is dated June 1996. (Plaintiffs Exhibit 92, [\*10] Doc. 143) The term of this contract is thirty months, but Section 6.2.3 permits either party, with or without cause, to terminate with sixty days written notice. The contract obligates PCS to disclose to its plan sponsors all amounts Wyeth pays PCS (in rebates and other similar types of payments), while the actual distribution of those amounts is left to PCS and its plan sponsors.

Exhibit A lists the Wyeth products that are included in the PCS "Core Formulary." These include the various available dosages of Premarin. Section II states that all rebates paid under the agreement are contingent on Premarin being listed as the Core Formulary's "exclusive conjugated estrogen." The parties agreed that, in the event of a generic competitor's market entry, PCS would "consult" with Wyeth prior to placement of the generic on the formulary. (The contract also provides an "out" for both parties in the event that PCS and Wyeth could not agree on how to properly address a generic entry.)

The contract provides for "access" rebates and "market share" rebates, based on the number of prescriptions filled by PCS plan members for various Wyeth products, including Premarin. The market share rebate is [\*11] defined

for the "Estrogen and Estrogen/Progestin" therapeutic class as the "Premarin family" (Premarin, Prempro and Premphase tablets.) Other products for which Wyeth paid rebates include several oral contraceptives; an antidepressant (Effexor); the NSAIDs Lodine and Oruvail; an antibiotic (Suprax); a calcium channel blocker (Verelan); and a beta-blocker (Ziac).

#### B. Wyeth's "Sole CE" Contract Clauses.

Wyeth attempted to include "sole conjugated estrogen" clauses, like the one in the PCS contract discussed above, in most of its PBM contracts. (Prior to Cenestin's approval by the FDA, Premarin was the **only** "conjugated estrogen" product on the market.) Wyeth's index of its PBM contracts indicates that, as of 1/1/2000, 31 out of 74 contracts contained a "sole conjugated estrogen" clause. (See Doc. 135, Exhibit H-13) By 1/1/2002, the clause was in 23 out of 60 contracts. (Of course, these numbers do not reflect the size of the PBMs and the "number of lives" each PBM represented.)

Plaintiffs recite a number of examples of Wyeth relying on its "sole CE" clause to "force" various PBMs to refuse a place for Cenestin on their formularies. Plaintiffs Exhibit 116 is an internal Wyeth [\*12] memo titled "October 1999 Highlights," summarizing news and developments in many areas of Wyeth's business, including Premarin sales and marketing. Plaintiffs quote from page 3, which states in pertinent part: "A signed agreement with Duramed, which had added Cenestin to the Express Scripts formulary, was reversed by quick, concerted action between national account sales and CD&A.<sup>2</sup> To date, no known managed care accounts have Cenestin on formulary." The document goes on to note the creation of a "Premarin 2000 task force assigned to develop a strategy to counter the threat of an AB-rated generic conjugated estrogen anticipated in 2001."

Class Plaintiffs review Wyeth's negotiations concerning the contracts with several large PBMs (Prescription Solutions, Medco, Wellpoint, Advance PCS, Integrated Pharmaceutical Services, Aetna) and with Kaiser, a managed care organization that purchased directly from Wyeth for its members. (See Doc. 143, [\*13] pp. 37 to 51). In each case, Plaintiffs claim that the presence of a "sole CE" clause in the Wyeth contract gave Wyeth the leverage to "threaten" these PBMs with contract cancellation, and the attendant loss of Wyeth rebates, if the PBM added Cenestin to its formulary.

#### C. Wyeth's Price Increases for Premarin.

Wyeth does not dispute the fact that, after Cenestin was approved by the FDA in March 1999, Wyeth raised its prices for Premarin in a series of price increases. According to Class Plaintiffs' expert Dr. Leitzinger, "For the years 1999, 2000 and 2001, Wyeth increased Premarin's price twice annually for total annual increases of 11.8%, 12.4% and 16.8%, respectively. These price increases were not the result of any increase in Premarin costs. Nor did they reflect a response by Wyeth to price increases initiated by other ERT sellers." Leitzinger Report at p. 13 (Doc. 135, Exhibit C-7). Leitzinger also claims that for 1996-1998, Wyeth's "average rate of price increase" for Premarin was 7.58%. (Leitzinger Report at p. 47) Leitzinger, Keith Leffler (expert for CVS/Rite Aid) and Stephen Schondelmeyer (an economic pharmaceutical expert for both the Class and CVS/RiteAid) all opine [\*14] that Wyeth's price increases were possible only because Wyeth successfully foreclosed Cenestin from the ERT market through the use of its illegal PBM contracts.

Wyeth uses a longer view for purposes of evaluating its Premarin pricing. Wyeth's expert Christopher James submits a table (James Exhibit 2) calculating the annual growth rate in Premarin Average Price (for the most widely prescribed 0.625 mg dose) from 1989 to 2003. James calculates the increase from 1989 to 1990 at almost 20%, while the lowest increase for that period (1992 to 1993) was only 4%. Viewed in this longer-term fashion, Wyeth contends that its post-1998 price increases are not out of the ordinary.

#### D. Wyeth's Market Share

As initially noted above, Premarin has been on the market since 1942 and has had a majority market share for decades. In 1998, Premarin's overall ERT market share was 75.3%. Based on IMS data (a national source cited by

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<sup>2</sup> "National account sales" and "CD&A" are both internal Wyeth departments.

all parties that provides statistical information on drug costs and utilization), Premarin's share of the oral ERT market declined in the period 1998 to 2003. In 1999, Premarin's share was 73.9%; by June 2003, its share was 68.6%. The fastest growing drug in the oral ERT [\*15] market during that same time was estradiol, which grew its share from 9.4% in 1998 to 18.5% by June 2003. (See Exhibit B-11, Doc. 135).

#### E. The Women's Health Initiative Study

In June 2002, the Womens' Health Initiative study released preliminary results of its long-term HRT study. (See generally, the WHI website at <http://www.nhlbi.nih.gov/whi>.) The WHI announced its intention to prematurely stop its study of the long-term use of HRT. The WHI found that the overall risks of HRT outweighed the benefits. WHI found that HRT increased the risk of breast cancer, heart disease, stroke, and blood clots. This announcement negatively impacted sales of both HRT and ERT products (although the estrogen-only WHI study continued after June 2002). The Court agrees with Dr. Leitzinger and Dr. James, who both believe that the WHI announcement impacted the ERT market in such a major way that market behavior after that date cannot be relied on for purposes of analyzing liability or damages in this case.

#### III. Procedural Background of This Litigation.

In September 2000, approximately fifteen months after Cenestin was first commercially available on the market, Duramed sued Wyeth in this [\*16] district, alleging that Wyeth's contracts with PBMs violated the antitrust statutes.<sup>3</sup> This Court denied Wyeth's initial motion to dismiss Duramed's complaint, but that case settled prior to any dispositive rulings or a trial on the merits.

J.B.D.L.'s complaint in this case, filed in October 2001, alleged that Wyeth's contracts and its post-1998 price increases violated Sections 1 and 2 of the Sherman Act.<sup>4</sup> This Court certified a direct purchaser class under F.R.C.P. 23 (Doc. 54, Order of May 12, 2003). The class, represented by J.B.D.L., includes both wholesalers and retail pharmacies who purchase directly from Wyeth. The class does not include the insurers, managed care organizations and pharmacy benefit managers who entered into the challenged rebate contracts with Wyeth.

[\*17] Plaintiffs CVS and RiteAid, two retail pharmacies, opted out of the J.B.D.L. class and filed a separate Sherman Act complaint; their action has been consolidated with the Class Plaintiffs' action. After extensive discovery, Wyeth moved for summary judgment against Class Plaintiffs and CVS/RiteAid (Doc. 135). Class Plaintiffs (Doc. 143) and CVS/RiteAid (Doc. 144) filed lengthy opposition briefs, to which Wyeth replied (Doc. 155). Class Plaintiffs and CVS/RiteAid have sought leave to file sur-replies (Doc. 159 and 160), which Wyeth opposes (Doc. 164). Wyeth's motion has been exhaustively briefed and is ripe for decision.

## **ANALYSIS**

#### I. Summary Judgment Standards

**HN1** The standards for summary judgment are well established. Summary judgment is proper "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed.R.Civ.P. 56(c). **HN2** The party opposing a properly supported summary judgment motion "may not rest upon the mere allegations or denials [\*18] of his pleading, but ... must set forth specific facts showing that there is a genuine issue for trial." Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986) (quoting First Nat'l Bank of Arizona v. Cities Serv. Co., 391 U.S. 253, 20 L. Ed. 2d 569, 88 S. Ct. 1575 (1968)). The Court is not duty bound to search the entire record in an effort to establish a lack of material facts. Guarino v. Brookfield Township Trs., 980 F.2d 399, 404 (6th Cir. 1992); InterRoyal Corp. v. Sponseller, 889 F.2d

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<sup>3</sup> See Case No. 1:00-cv-735.

<sup>4</sup> Case No. 1:01-cv-745, McHugh Pharmacy Wynnewood, Inc. V. Wyeth-Ayerst Laboratories, Inc., was consolidated with this case, and the J.B.D.L. complaint is the operative complaint for both actions.

[108, 111 \(6th Cir. 1989\)](#), cert. den., *Superior Roll Forming Co. v. InterRoyal Corp.*, 494 U.S. 1091, 108 L. Ed. 2d 967, 110 S. Ct. 1839 (1990). Rather, the burden is on the non-moving party to "present affirmative evidence to defeat a properly supported motion for summary judgment...", [Street v. J.C. Bradford & Co.](#), 886 F.2d 1472, 1479-80 (6th Cir. 1989), and to designate specific facts in dispute. [Anderson](#), 477 U.S. at 250. **HN3**[<sup>18</sup>] The non-moving party "must do more than simply show that there is some metaphysical doubt as to the material facts." [Matsushita Electric Industries Co. v. Zenith Radio Corp.](#), 475 U.S. 574, 586, 89 L. Ed. 2d 538, 106 S. Ct. 1348 (1986). **HN4**[<sup>19</sup>] The court [\*19] construes the evidence presented in the light most favorable to the non-movant and draws all justifiable inferences in the non-movant's favor. [United States v. Diebold Inc.](#), 369 U.S. 654, 655, 8 L. Ed. 2d 176, 82 S. Ct. 993 (1962).

The court's function is not to weigh the evidence and determine the truth of the matter, but to determine whether there is a genuine issue for trial. [Anderson](#), 477 U.S. at 249. The court must assess "whether there is the need for trial -- whether, in other words, there are any genuine factual issues that properly can be resolved only by a finder of fact because they may reasonably be resolved in favor of either party." *Id.* at 250. "If the evidence is merely colorable, . . . , or is not significantly probative, . . . , the court may grant judgment." [Anderson](#), 477 U.S. at 249-50 (citations omitted). The Supreme Court has held:

**HN5**[<sup>20</sup>] The mere existence of a scintilla of evidence in support of the plaintiff's position will be insufficient; there must be evidence on which the jury could reasonably find for the plaintiff. The judge's inquiry, therefore, unavoidably asks whether reasonable jurors could find by a preponderance [\*20] of the evidence that the plaintiff is entitled to a verdict...

*Id.* at 252. Hence the "mere possibility" of a factual dispute will not suffice. [Mitchell v. Toledo Hospital](#), 964 F.2d 577, 582 (6th Cir. 1992), quoting [Gregg v. Allen-Bradley Co.](#), 801 F.2d 859, 863 (6th Cir. 1986).

**HN6**[<sup>21</sup>] Summary judgment is not appropriate simply because the weight of the evidence favors the moving party. [Poller v. Columbia Broadcasting Systems, Inc.](#), 368 U.S. 464, 472, 7 L. Ed. 2d 458, 82 S. Ct. 486 (1962). The issue of material fact required "to entitle a party to proceed to trial is not required to be resolved conclusively in favor of the party asserting its existence; rather, all that is required is that sufficient evidence supporting the claimed factual dispute be shown to require a jury or judge to resolve the parties' differing versions of the truth at trial." [Cities Serv. Co., supra](#), 391 U.S. at 288-89.

**HN7**[<sup>22</sup>] Although summary judgment must be used with extreme caution since it operates to deny a litigant his day in court, [Smith v. Hudson](#), 600 F.2d 60, 63 (6th Cir. 1979), cert. dismissed, 444 U.S. 986, 100 S. Ct. 495, 62 L. Ed. 2d 415 (1979), the [\*21] United States Supreme Court has stated that the "summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to 'secure the just, speedy and inexpensive determination of every action.'" [Celotex Corp. v. Catrett](#), 477 U.S. 317, 327, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986) (citations omitted).

## II. Antitrust Analysis

### A. Class Plaintiffs' Claim Under Section 1 of the Sherman Act.

Class Plaintiffs (but not CVS/RiteAid) assert that Wyeth's PBM contracts are illegal "exclusive dealing" contracts that substantially foreclosed competition in the relevant market, and thus violate [Section 1](#). Wyeth seeks summary judgment on this claim, arguing that its conduct does not violate [Section 1](#) as a matter of law.

Wyeth argues that its PBM contracts are not "exclusive dealing" contracts because those contracts do not forbid placement of alternate ERT products on the formularies of the contracting PBMs. Nor do the contracts forbid PBMs from purchasing or reimbursing their members' purchases of competing ERT products, including Cenestin. Wyeth describes its contracts as "mere preferential treatment [\*22] of one product over another" rather than exclusive dealing.

Wyeth also argues that its PBM contracts did not substantially foreclose competition in the relevant ERT market. Wyeth argues that the contracts' short termination notice provisions (30 to 60 days) prevent the contracts from

being characterized as illegal exclusive dealings as a matter of law. Wyeth also attacks the market foreclosure rates calculated by Plaintiffs' experts as fatally flawed, as they fail to properly account for Cenestin's availability on many of the "open" PBM formularies and in the non-PBM cash market. Wyeth claims that once properly reduced, the rates are simply too low to create a triable issue concerning an "unreasonable" foreclosure rate.

**HN8** [Section 1] prohibits contracts or agreements that **unreasonably** restrain trade or commerce. The contracts at issue in this case are evaluated under the "rule of reason" test. See generally, *State Oil Co. v. Khan*, 522 U.S. 3, 10, 139 L. Ed. 2d 199, 118 S. Ct. 275 (1997). This analysis must take into account a variety of factors, "including specific information about the relevant business, its condition before and after the restraint was imposed, and the restraint's history, nature, [\*23] and effect." *Id. at 10*. The first, and critical, step in any rule of reason analysis is that the plaintiff must prove that "the challenged action has had an actual adverse effect on competition as a whole in the relevant market." *K.M.B. Warehouse Distributors, Inc. v. Walker Mfg. Co.*, 61 F.3d 123, 127 (2d Cir. 1995) (citation omitted). See also, *PSI Repair Services, Inc. v. Honeywell, Inc.*, 104 F.3d 811, 815 n. 12 (6th Cir. 1997) ["Under the rule-of-reason analysis, the antitrust plaintiff must show, inter alia, an adverse effect on competition."]

The key questions at this juncture are (1) the appropriate definition of the relevant market, and (2) whether Wyeth's PBM contracts had an "actual adverse effect on competition as a whole" in that relevant market (or, in exclusive dealing parlance, whether the contracts substantially foreclosed competition in that market).

**Relevant Market:** Class Plaintiffs' expert Jeffrey Leitzinger defines the relevant product market as oral ERT products. According to Leitzinger, competing products to Premarin include Cenestin, Estratab/Menest (esterefied estrogens), Estrace/Gynodiol (micronized [\*24] estradiol), Ogen/Ortho-Est (estropipate), and Estinyl (ethinyl estradiol), as well as generic versions of several of these drugs, including estradiol. (See Leitzinger Report at p. 6, n.4 and pp. 9-12.) The relevant geographical market is the United States. Wyeth's motion does not take a definitive position on the relevant market, but concedes that it is "at least" the market for oral ERT products.

The definition of the relevant market can be a complex and difficult issue. In this case, it may well be that the relevant market is broader than just the oral ERT therapeutic category. However, Plaintiffs have put forward an acceptable definition and the reasons for it, and Wyeth does not seriously challenge this definition. For purposes of ruling on Wyeth's motion, the Court will accept Plaintiffs' definition for purposes of analyzing Class Plaintiffs' claim.

**Premarin's Market Power:** The record establishes (and Wyeth does not dispute) that Premarin has always had a dominant share of the oral ERT market. But majority or dominant market share does not equal "market power." It must be shown that Wyeth's large market share translated to market power that enabled Wyeth to foreclose competition [\*25] in that market.

**Actual Market Foreclosure:** The record in this case establishes that pharmaceutical manufacturers value advantageous formulary placement. It is beyond dispute that Wyeth and its competitors (both in the oral ERT market and in the pharmaceutical market generally) seek favorable formulary placement from PBMs, and are willing to pay large sums to obtain those placements. This favorable treatment can include favorable access (preferred brand status or formulary "tier" placement), favorable pricing (rebates to PBMs and lower co-pays to PBM members), or both. Wyeth's contract with PCS (discussed above) provided for rebates not only on Premarin, but a number of other drugs.

These formulary arrangements can be pro-competitive, as the CVS/RiteAid expert Keith Leffler admits. Rebates effectively lower the cost paid for the product by the plan sponsor. PBM rebates, when passed on to the plan sponsor, lower the sponsor's cost of providing the benefit.

It is undisputed that many of Wyeth's PBM rebate contracts also contained "sole conjugated estrogen" clauses, which in operation did not permit those PBMs to include Cenestin, approved as a "conjugated estrogen," on the formulary. [\*26] If the PBM did so, it risked contract cancellation and loss of Wyeth rebates. But it is also quite clear that these clauses did not prevent PBMs from listing **other** oral ERT products (products that are not "conjugated estrogens") on their formularies. And, Wyeth submits evidence from Duramed's own documents that "open" formularies (during the period 1999 to June 2002, at least) were more prevalent than Class Plaintiffs wish to

recognize. Under "open" formularies without the exclusivity clause, Premarin would not have a preferred status over Cenestin, and the co-pay for Cenestin and Premarin would be equal. Duramed itself analyzed its status with PCS, where (according to Duramed) Cenestin was available at the same copay level for at least 90% of PCS business, or over 45 million lives. Duramed notes that Cenestin's low market share at PCS (approximately 1%) was reflective of its national market conditions. Duramed concluded that "considering the fact that the overwhelming majority of PCS business is open, with no restrictions on Cenestin," low market share simply demonstrated the need to **help drive formulary decisions by increased efforts with its field sales force**. See, DUR [\*27] 010716 (Exhibit G-4, Doc. 135). To similar effect is Duramed's 8/5/99 "Update" on Cenestin, where Duramed concludes it can take a "conservative approach with regards to managed care contracting, because over 70% of managed care lives are enrolled in open formularies, meaning the majority of scripts go through with no issues and because we provide a 30 day sample." (DUR 010916, Wyeth's Exh G-5) Duramed's calculations as of 12/15/00 for the number of "lives" covered by HMOs and PBMs with access to open formularies shows that HMO open lives were 73,359,394, 85% of the identified HMOs with a total of 113,078,707 covered lives. For thirteen PBMs, covering 222,000,000 lives, the open formulary lives were 137,800,000 or 62%. (DUR010961-966, Exhibit G-6, Doc. 135)

It has often been noted that [HN9](#) exclusivity provisions in contracts can serve useful, pro-competitive purposes. See, e.g., [Jefferson Parish Hospital Dist. No. 2 v. Hyde, 466 U.S. 2, 45, 80 L. Ed. 2d 2, 104 S. Ct. 1551 \(1989\)](#) (O'Connor, J., concurring). It is only when such provisions cross the line into the arena of exclusive dealing that substantially and negatively affects market competition, that the antitrust statutes come into play.

In [U.S. v. Microsoft, 346 U.S. App. D.C. 330, 253 F.3d 34 \(D.C. Cir 2001\)](#), [\*28] the Court of Appeals discussed the trial court's conclusion that Microsoft's "exclusive dealing" contracts with internet access and service providers ("IAPs") did not violate [Section 1](#). Under the terms of Microsoft's contracts, Microsoft licensed its Internet Explorer browser and an IE "access kit" to hundreds of IAPs at no cost. Microsoft then entered into rebate contracts with, or made outright payments to, the ten "most important" IAPs (such as AOL) to promote IE and "exile" Microsoft's largest browser competitor, Netscape Navigator. "Under that agreement Microsoft puts the AOL icon in the OLS folder on the Windows desktop and AOL does not promote any non-Microsoft browser, nor provide software using any non-Microsoft browser except at the customer's request, and even then AOL will not supply more than 15% of its subscribers with a browser other than IE." [Id. at 68](#).

The [Microsoft](#) district court, in analyzing the [§ 1](#) claim, concluded that "unless the evidence demonstrates that Microsoft's agreements excluded Netscape altogether from access to roughly forty percent of the browser market, the Court should decline to find such agreements in violation of [§ 1](#)." [\*29] This was true even though Microsoft had substantially excluded Netscape from "the most efficient channels for Navigator to achieve browser usage share," e.g., the internet access providers like AOL.

Similarly, in the recent Third Circuit case of [United States v. Dentsply, 399 F.3d 181, 2005 U.S. App. LEXIS 3219 \(Feb. 24, 2005\)](#), the district court found that Dentsply's [HN10](#) exclusive dealer contracts did not violate [Section 1](#), because Dentsply's actions had not foreclosed competitors from "gaining a foothold in the market." [Id. at \\*7](#) (quoting from [U.S. v. Dentsply, 277 F.Supp.2d 387, 453 \(D. Del. 2003\)](#)). This was so even though the challenged dealer contracts prohibited Dentsply's authorized dealers from selling **any** competitor's products.<sup>5</sup>

This Court agrees with the analysis of the district courts in both [Microsoft](#) and [Dentsply](#). The Plaintiffs must establish that Wyeth's [\*30] conduct **substantially** foreclosed actual competition in the relevant market, oral ERT products. While favorable PBM formulary placement is no doubt an effective method for sales of a drug, it is clearly not the only route Duramed had to sell its new product Cenestin. The Court cannot conclude that Wyeth's favorable or exclusive formulary placement for Premarin in many PBMs equates to actionable market foreclosure.

The parties disagree about the appropriate basis for calculation of a foreclosure rate. For instance, Leitzinger opines that 42% of Premarin sales in fourth quarter 1999 were through PBMs with "sole CE" clauses, which he concludes is substantial market foreclosure. (Leitzinger Report pp. 39-40) But, as Wyeth points out, Leitzinger fails

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<sup>5</sup> The district court rulings on [Section 1](#) claims were not appealed in either [Microsoft](#) or [Dentsply](#).

to account for the fact that many PBMs would reimburse for a Cenestin prescription even though it was not a "favored" drug and listed on the PBM's formulary. The Duramed documents discussed above show that Cenestin did have access, even if it may not have had the best or most preferred formulary position vis-a-vis Premarin. Leitzinger also assumes that his calculated 42% foreclosure rate, based on 4th quarter 1999 data only a few months [\*31] after Cenestin was actually available on the market, should hold for the entire time period at issue. This assumption is faulty, given the volume of information in the record about changing market conditions, including Duramed's activities to try to increase Cenestin's market share. His assumption also ignores the fact that most formularies have a "waiting period" during which new drugs are evaluated for addition to a PBM's formulary. Dr. White, of HealthNet, testified that a six-month period for review prior to placement is typical. Most importantly, however, Class Plaintiffs assume that because Cenestin could not gain full or complete access to all PBM formularies in the year it entered the market, that "competition in general" was harmed as a result. The fact that other oral ERT products were not only available but were simply not impacted by Wyeth's "sole CE" contract clauses, belies such an assumption.

The Court need not resolve the dispute about the specific, appropriate foreclosure rate, because the Court finds that Class Plaintiffs have simply not established actual market foreclosure. The Court will therefore grant summary judgment to Wyeth on Class Plaintiffs' [Section 1](#) [\*32] claim.

#### B. Section 2 Monopolization Claim.

Class Plaintiffs and CVS/RiteAid allege that Wyeth violated [Section 2 of the Sherman Act](#). [HN11](#)[] A claim under [Section 2](#) requires proof of two elements: (1) the possession of monopoly power in a relevant market; and (2) the willful acquisition, maintenance, or use of that power by anti-competitive or exclusionary means as opposed to 'growth or development resulting from a superior product, business acumen, or historic accident.' [Aspen Skiing Co. v. Aspen Highlands Skiing Corp.](#), 472 U.S. 585, 595-96, 86 L. Ed. 2d 467, 105 S. Ct. 2847 (1985); [Conwood Co. v. U.S. Tobacco Company](#), 290 F.3d 768, 782 (6th Cir. 2002). [HN12](#)[] "Monopoly power" for purposes of [section 2](#) can be "something greater than market power under [section 1](#)." [Eastman Kodak Co. v. Image Technical Servs., Inc.](#), 504 U.S. 451, 481, 119 L. Ed. 2d 265, 112 S. Ct. 2072 (1992).

Wyeth concedes its "monopoly power" solely for purposes of its summary judgment motion.<sup>6</sup> And, as noted above, Wyeth apparently concedes (at least for summary judgment purposes) that the relevant market is oral ERT products.

[\*33] Wyeth argues that despite its conceded monopoly power, its PBM contracts are in fact pro-competitive and are a hallmark of competition in the pharmaceutical industry. Wyeth claims that its rebates formulas are just pricing systems, which are not actionable by the direct purchaser plaintiffs under [Section 2](#), absent predatory pricing. Since Wyeth's prices are clearly not "predatory" (in the classic sense of below-cost pricing to squeeze out a competitor), Wyeth argues that Plaintiffs have no viable [Section 2](#) claim.

Initially, the Court rejects Wyeth's somewhat simplistic argument that its lack of predatory pricing mandates dismissal of the [Section 2](#) claims. Plaintiffs' essential allegation is that Wyeth's contracts (rebate structure plus sole CE clauses) prevented Cenestin from becoming a competitive threat, and thus allowed Wyeth to unlawfully raise its Premarin prices after Cenestin's introduction. Moreover, [HN13](#)[] the Supreme Court has acknowledged the viability of [Section 2](#) claims brought by a **competitor** that go beyond allegations of predatory pricing. See, [Aspen Highlands, supra](#), and [Kodak, supra](#).<sup>7</sup> Thus it is not **solely** the Wyeth rebates [\*34] that Plaintiffs attack.<sup>8</sup>

<sup>6</sup>The Court recognizes that absent Wyeth's concession on this point, a careful analysis of the existence of monopoly power is required. See generally, [Re/Max Int'l, Inc. v. Realty One, Inc.](#), 173 F.3d 995, 1018-1019 (6th Cir. 1999). The Court also acknowledges that its concession will not prohibit Wyeth from challenging plaintiffs' allegation of its monopoly power in the event of a trial in this case.

<sup>7</sup>The Supreme Court subsequently described [Aspen Skiing](#) as "at or near the outer boundary of § 2 liability." [Verizon Communications v. Law Offices of Curtis V. Trinko](#), 540 U.S. 398, 409, 157 L. Ed. 2d 823, 124 S. Ct. 872 (2004).

Wyeth relies heavily on [\*NWS Michigan v. General Wine & Liquor, 58 Fed. Appx. 127 \(6th Cir. 2003\)\*](#), an unpublished decision which held that a liquor distributor lacked antitrust standing to sue its larger competitor when it failed to allege predatory pricing. The Court of Appeals held that "Whether or not General Wine's pricing mechanism violated state law, the prices themselves simply reflect the storage and transportation [\*35] efficiencies available to General Wine by virtue of its privileged status." That privileged status was conferred by an explicit legislative "grandfather" clause, permitting General Wine to deal in a wider market than NWS was able to do, thus achieving economies of scale denied to NWS.

The facts of that case do not "fit" the facts here. Nor does the Court view the case as supporting the sweeping proposition which Wyeth ascribes to it (e.g., no "rebate" program can be challenged absent predatory pricing). Moreover, the Sixth Circuit has often instructed that [Section 2](#) requires "a thorough analysis of each fact situation" in order to determine whether or not the monopolist's conduct is unreasonably anti-competitive and thus unlawful. See [\*Conwood, supra, 290 F.3d at 782\*](#) (quoting [\*Byars v. Bluff City News Co., 609 F.2d 843, 860 \(6th Cir. 1979\)\*](#)). The critical questions presented here are whether Plaintiffs have established a material factual dispute as to whether Wyeth willfully maintained its historic (and apparently legally obtained) monopoly power by unreasonable anti-competitive or exclusionary means, and if so whether the Plaintiffs suffered an antitrust [\*36] injury as a result.

#### Unreasonable Anti-Competitive Conduct

Areeda & Hovenkamp describe [HN14](#)[] unlawful exclusionary conduct as acts that "are reasonably capable of creating, enlarging or prolonging monopoly power by impairing the opportunities of rivals" and that either "do not benefit consumers at all," are "unnecessary for the particular consumer benefits that the acts produce," or "produce harms disproportionate to the resulting benefits." [\*\*Antitrust Law\*\*](#) P 749, at 141 (Supp. 2003), as quoted in "Comment: LePage's v. 3M: An Antitrust Analysis of Loyalty Rebates", [\*79 N.Y.U.L. Rev. 1605 \(October 2004\)\*](#).

And it must be kept in mind, when considering an allegation of exclusionary or anti-competitive conduct, that the antitrust laws are intended to protect competition, not a competitor. See, [\*Richter Concrete Corp. v. Hilltop Concrete Corp., 691 F.2d 818, 823 \(6th Cir. 1982\)\*](#) ["Anticompetitive conduct is conduct designed to destroy competition, not just to eliminate a competitor."] Plaintiffs and their experts repeatedly assert that Wyeth's "sole CE" clause - which impacted only one competitor, Duramed - together with Wyeth's rebates formulas harmed "competition" [\*37] in general. But there is little, if any, analysis of the effects of the challenged conduct on overall competition in the oral ERT market.

Despite this lack, Plaintiffs repeatedly point to Wyeth's expressed desire (as reflected in its "Premarin Plan" and various marketing documents in the record) to limit Cenestin's market share. But undisputed evidence that a manufacturer desires or intends to maintain or increase its product's market share at the expense of a new competitor, does not by itself create a triable issue of whether Wyeth's chosen means to achieve that desire violated the Sherman Act. See, e.g., [\*Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 116, 93 L. Ed. 2d 427, 107 S. Ct. 484 \(1986\)\*](#) ["The kind of competition Monfort alleges here, competition for increased market share, is not actively forbidden by the antitrust laws."]

Plaintiffs urge this Court to follow the recent Third Circuit decision in [\*LePage's v. 3M, 324 F.3d 141 \(3d Cir. 2003\)\*](#), and permit their [Section 2](#) claims to proceed to trial. But [LePage's](#) is not controlling on this Court. And absent persuasive authority that the Sixth Circuit would follow [LePage's](#) and agree with its conclusions, this Court [\*38] is not persuaded.

[LePage's](#) involved antitrust claims against 3M, the manufacturer of branded "Scotch" transparent tape, brought by LePage, 3M's competitor in the second-brand, or private label, transparent tape market. By 1992, LePage's had an

<sup>8</sup> The CVS/RiteAid expert Keith Leffler admitted in his deposition that the "more significant thing" in his analysis was the market share rebate, rather than the "sole CE" clause. See Leffler Deposition at p. 163-164. The Court does not view this testimony as limiting the CVS/RiteAid claim to Wyeth's rebate clauses, as Wyeth suggests.

88% market share in the second-brand market, and 3M decided it would enter that market and compete with LePage's. 3M started offering rebate programs to various retailers, who could earn rebates on a variety of 3M products. Several specific types of rebates were offered. These included "bundled" rebates, and "tiered" rebates earned based on sales across six different 3M product lines, including lines in which LePage's did not compete. 3M also offered minimum purchase level agreements to two of the largest retail outlets for tape (Office Depot and Staples) for its branded Scotch tape relative to the second-brand or private label tape; if the retailer achieved a set "growth" factor for the second-brand sales, it could obtain higher rebates.

LePage's claimed that 3M's multi-tiered and bundled rebates "plus" the agreements with the largest retailers violated [section 2](#), in that 3M was using its brand-name transparent (Scotch) tape monopoly to [\*39] gain an unfair advantage in the second-brand, private label market, by restricting the availability of LePage's lower-priced second-brand tapes.

The case was submitted to a jury, which found for LePage's on both its monopolization and attempted monopolization claims under [§ 2 of the Sherman Act](#). It found in 3M's favor on LePage's claims under [§ 1](#) of the [Sherman Act and § 3](#) of the [Clayton Act](#). The district court denied 3M's motions for judgment as a matter of law and for a new trial on the [Section 2](#) claim.

On appeal, a panel of the Third Circuit reversed the District Court's judgment on LePage's [§ 2](#) claim by a divided vote. [LePage's Inc. v. 3M, 277 F.3d 365 \(3d Cir. 2002\)](#). However, LePage's motion for rehearing en banc was granted, and the en banc court then affirmed the trial court's decision and the jury verdict. The en banc majority essentially concluded that [HN15](#) exclusionary conduct that used above-cost price discounting was actionable under [Section 2](#), and upheld a verdict against 3M of approximately \$ 68 million.

The [LePage's](#) dissent criticized the result because it erred in favor of protecting LePage's, an inefficient competitor, rather than protecting [\*40] overall competition. The jury punished 3M rather severely for engaging in above-cost, discount pricing coupled with some exclusive retail contracts, an arrangement that clearly permitted 3M to increase its market share and its profits, yet did not clearly harm competition or consumers. Nor, in reality, did 3M's conduct significantly harm LePage's secondary-brand market share (which declined from 88% to 67% in the years in which 3M's rebate programs were in effect). This latter conclusion is especially relevant, given the significant evidence in the record that LePage's market difficulties were caused by its own conduct and market decisions, and were not the result of 3M's challenged conduct.

The Third Circuit decision also leaves unclear (at least to this Court) the precise nature of 3M's violation of [Section 2](#). The verdict imposed a heavy penalty on 3M without producing consistent guidance for what is permissible price competition in the retail market for a simple item like transparent tape. That marketplace appears far less complex than the current United States marketplace for pharmaceuticals.

In contrast to [LePage's](#) is the Eighth Circuit decision in [Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039 \(8th Cir. 2000\)](#), [\*41] which Wyeth advocates. There, a group of power boat manufacturers sued Brunswick, the leading supplier of inboard and stern drive engines that the plaintiffs bought and used in their boats. Plaintiffs alleged that Brunswick engaged in anticompetitive conduct because it (1) began a market share discount pricing program in 1984, under which list price discounts were given for purchases of specified percentages of engine purchases made from Brunswick. Additional long term discounts could be earned for signing a market share agreement for up to three years. Volume discounts based strictly on sales quantity were also used. When one of Brunswick's largest competitors introduced a new stern drive in 1985, Brunswick responded by purchasing two of the largest domestic boat builders (Bayliner and Sea Ray), thus vertically integrating its business.

The plaintiffs later filed suit, contending that the synergistic effect of the market share/volume discount programs, and Brunswick's willful vertical integration efforts, resulted in plaintiffs being charged supracompetitive prices for Brunswick engines, and also drove other engine manufacturers out of the market. Brunswick's summary judgment motion [\*42] was denied, and after a ten week trial the jury awarded judgment for plaintiffs of over \$ 44 million. After unsuccessful post-trial motions seeking to set aside the verdict, the final award against Brunswick was \$ 142,165,931.12.

The Eighth Circuit reversed and remanded for entry of judgment in favor of Brunswick. Concerning plaintiffs [Section 2](#) claim, the Circuit noted the strong line of authority that above cost discounting is not anticompetitive conduct as a matter of law and sound policy. See generally, [Brooke Group Ltd. v. Brown & Williamson Tobacco Corp., 509 U.S. 209, 223, 125 L. Ed. 2d 168, 113 S. Ct. 2578 \(1993\)](#). While the Eighth Circuit rejected Brunswick's suggestion that above cost pricing is always per se lawful, it also rejected plaintiffs' argument that Brunswick's discounts "plus" - in that case Brunswick's vertical integration purchases along with several other instances of allegedly anticompetitive conduct - could together result in a violation of [Section 2](#). The Court noted that the boat builders were not required to refrain from purchasing from competitors, and were free to walk away from Brunswick's discounts if they got a better offer. The Court rejected the plaintiffs' arguments [\*43] that Brunswick's discounts created "golden handcuffs" that amounted to an impenetrable barrier to the entry of additional competitors.

The Supreme Court denied certiorari in both [Concord Boat](#) and in [LePage's](#).

The Plaintiffs here urge that the scale is tipped in favor of their position, and the reasoning of [LePage's](#), by two additional cases; [U.S. v. Dentsply, supra](#), and [Masimo v. Tyco Health Care Group, 2004 U.S. Dist. LEXIS 26916 \(C.D. Cal. 2004\)](#). Neither of these are of substantive assistance. [U.S. v. Dentsply](#) was an action by the Justice Department, seeking only injunctive relief against Dentsply's enforcement of its truly exclusive dealing clause in its purchase order contracts. Dentsply had historically sold its products through dealers, who in turn sell to dental laboratories that fabricate the final artificial teeth or dentures that dentists (and their patients) buy. Some of Dentsply's competitors also sold directly to the laboratories, but that outlet for sales was small. Dentsply had long "discouraged" its dealers from selling products of its competitors; but in 1993, it adopted an explicit contract provision that its authorized [\*44] dealers "may not add further tooth lines to their product offering." (The relationship between Dentsply and its dealers was on a purchase-order basis, which the Third Circuit characterized as "essentially terminable at will.") The district court found that the challenged contract clause did not violate [Section 2](#), but the Third Circuit reversed. Following [LePage's](#), the Court found that the contract provision essentially foreclosed all competition from the market, finding that "the firm that ties up the key dealers rules the market." [2005 U.S. App. LEXIS 3219 at \\*20](#). The Court believes a key difference between [Dentsply](#) and the case at bar lies in the fact that Dentsply's contract clause barred **all competition** from the dealer network, which was how the overwhelming majority of dental products were sold into the market.

[Masimo](#), a California district court opinion denying summary judgment on [section 1](#) and [2](#) claims, involves a disparate mix of strategies adopted by the defendant, Tyco Corp., in its sales of pulse oximetry sensors and patient cables, sold to hospitals, health networks and other equipment manufacturers. The conduct included "loyalty discounts" [\*45] to hospitals in exchange for agreements not to purchase more than 5 to 15% of their oximetry products from competitors; a few "sole source exclusive dealing arrangements" with hospital group purchasing organizations; offering "bundled rebates" to two of its customers which provided rebates when oximetry and non-oximetry products were purchased together; offering financing programs to hospitals that imposed penalties if the hospital switched to a competitor's oximetry products; and co-marketing contracts with original equipment manufacturers (OEMs) that required the OEMs that used Tyco's modules to also recommend that Tyco sensors be used, rather than those of Tyco's competitors, even when competitor sensors could have been used. The district court, relying on [LePage's](#), found that a jury could find that the combined effect of all of Tyco's conduct resulted in actionable anticompetitive conduct, and denied Tyco's summary judgment motion. This Court of course is not bound to adopt the reasoning of the California district court, and is not inclined to do so given its heavy reliance on [LePage's](#).

[Conwood v. U.S. Tobacco, supra](#), a Sixth Circuit decision that is [\*46] binding on this court and that Plaintiffs argue supports denial of Wyeth's motion, is distinguishable. There, U.S. Tobacco ("USTC") appealed a jury verdict in favor of Conwood on its antitrust claims; Conwood and U.S. Tobacco competed in the "moist snuff" market, with USTC the largest seller. The Sixth Circuit denied USTC's appeal from both the jury verdict and the trial court's denial of its summary judgment motion, noting that there was sufficient evidence of USTC's willful anticompetitive conduct to submit the case to the jury. USTC argued that Conwood's injury (undeniable loss of market share and profits in areas where the two companies were in direct competition) flowed only from USTC's exclusive selling agreements with retailers, which were entirely legal. But the evidence in that case of USTC's conduct included not

only exclusive retail agreements, but also evidence that USTC intentionally removed Conwood's package racks from retail stores without permission of store managers, and destroyed or discarded the racks, then put Conwood product cans into USTC's own racks in an attempt to "bury" Conwood's products; trained its sales representatives to trick store representatives and [\*47] clerks so that the Conwood racks and products could be moved or destroyed; and that USTC provided misleading and incorrect information about sales data for USTC and competitors' products, to encourage the retailers to stock more of USTC's products and less of the competitors products. No such tortious conduct is involved in the case before the Court.

Thus, this Court finds itself faced with somewhat imprecise and certainly conflicting standards by which to judge Plaintiffs allegations of Wyeth's monopolistic behavior. LePage's obviously favors letting a jury sort it out, using the same imprecise, conflicting Section 2 standards transformed into jury instructions. Concord Boat, on the other hand, illustrates the dangerous possibility of a tremendous waste of time and resources of all involved here in permitting a jury to "sort it out" when the appellate court may well find that there is no jury issue here.

Professor Elhauge has observed that there is a great deal of ambiguity and uncertainty in the current legal formulations of monopolization claims. He notes in particular the problem of submitting these sorts of claims to a jury: "And if the judges don't decide the issue, [\*48] the same problem will infect jury verdicts, for the typical set of jury instructions . . . leaves it up to the jury to divine the metaphysical difference between acquiring or maintaining monopoly power through (1) willful, anticompetitive, or exclusionary means or purposes, and (2) business acumen, superior products, competition on the merits, or valid and legitimate business reasons. Without more guidance, different jurors are likely to use completely different normative understandings about what all these terms mean." E. Elhauge, "Defining Better Monopolization Standards", [56 Stan. L. Rev. 253, 266-267 \(Nov. 2003\)](#).

The Supreme Court noted just last year that, HN16[<sup>1</sup>] "Under the best of circumstances, applying the requirements of Section 2 can be difficult because the means of illicit exclusion, like the means of legitimate competition, are myriad. . . . Mistaken inferences and the resulting false condemnations are especially costly, because they chill the very conduct the antitrust laws are designed to protect." [Verizon Communications v. Law Offices of Curtis Trinko, LLP, 540 U.S. 398, 414, 157 L. Ed. 2d 823, 124 S. Ct. 872 \(2004\)](#) (internal citations omitted).

Based on the record before the Court, [\*49] there is little doubt that Wyeth desired and intended to thwart Cenestin's market share growth with a vigorous multi-faced marketing campaign. Plaintiffs focus on one piece of that campaign, Wyeth's PBM contracts, and cry foul. But absent explicit, controlling appellate authority that Wyeth's conduct in executing those contracts, a practice that is widespread throughout the larger and unique pharmaceutical market in the U.S., runs afoul of the guiding principles of Section 2 liability, this Court believes that the approach adopted by the Eighth Circuit in Concord Boat is correct. Wyeth's pricing behavior "plus" - in this case the "plus" factor being the "sole CE" contract clause - did not violate Section 2 of the Sherman Act. Wyeth's motion for summary judgment against the Class Plaintiffs and CVS/RiteAid on the Section 2 claims is therefore granted.

### Antitrust Injury

Even if the Court were convinced that Plaintiffs' Section 2 claims survive Wyeth's motion, Plaintiffs must also establish that they have suffered an "antitrust injury" in order to proceed. The Sixth Circuit again recently noted that "antitrust standing to sue is at the center of all antitrust law and policy. [\*50] It is not a mere technicality. It is the glue that cements each suit with the purposes of the antitrust laws, and prevents abuses of those laws. . . . HN17[<sup>1</sup>] A private plaintiff may not recover damages under the antitrust laws merely by showing an 'injury causally linked to an illegal presence in the market.'" [Worldwide Basketball & Sport Tours, Inc. v. NCAA, 388 F.3d 955, 964-65](#) (Gibbons, J. concurring) (internal citations omitted). Antitrust laws are intended to prevent injuries to **competition**, and thus provide a remedy only for those losses that stem from the competition-reducing aspects of a defendant's conduct. There must be a distinct causal link between that challenged conduct, and the harm which Plaintiffs allege they have suffered. The Sixth Circuit has been zealous in ensuring that this element of an antitrust claim is satisfied. See, e.g., [Hodges v. WSM, Inc., 26 F.3d 36 \(6th Cir. 1994\)](#); [Valley Products v. Landmark, 128 F.3d 398 \(6th Cir. 1997\)](#); and [Indeck Energy Services v. Consumers Energy Co., 250 F.3d 972 \(6th Cir. 2000\)](#).

*In re Cardizem CD Antitrust Litigation, 332 F.3d 896 (6th Cir. 2003)* does not "lower the [\*51] bar" of this requirement, as Plaintiffs suggest. *Cardizem* involved an interlocutory appeal from the district court's denial of the defendant's Rule 12 motion to dismiss for failure to allege antitrust injury. At issue there, as described by the Sixth Circuit, was a "plain vanilla horizontal agreement to restrain trade in the form of a multi-million dollar cash payment," paid by the defendant to a competitor in order to delay the competitor's introduction of a generic substitute for Cardizem. *Id. at 914*. After ruling that the agreement was per se illegal, the Sixth Circuit also held that the district court correctly denied the motion to dismiss. Here, the Rule 56 standards apply, not Rule 12. And Wyeth's PBM contracts are clearly not illegal per se.

Here, understanding the antitrust injury Plaintiffs allege requires a two-step analysis. First, Cenestin's lower market share from 1999-2002 was caused by Wyeth's PBM contracting practices. Second, once Wyeth "realized" that it was successful in keeping Cenestin at that lower market share, Wyeth willfully and illegally raised its price for Premarin.

Class Plaintiffs and CVS/RiteAid rely on their economic experts [\*52] to establish the link between Wyeth's alleged exclusionary/anticompetitive conduct, and Wyeth's alleged supracompetitive price increases in the period 1999 to 2002. Leitzinger, Class Plaintiffs' expert, states that the increases were not tied to increases in Wyeth's costs to produce and market Premarin, nor to price increases in competitors' products. He therefore concludes (Leitzinger Report at pp. 40-45) that "By limiting Cenestin's development as a competitor and by restricting share growth by other oral ERT products, Wyeth maintained its hold on customers and avoided the need for any defensive pricing reactions. This enhanced Wyeth's market power relative to that it would have enjoyed had Cenestin's entry been unconstrained."

Leitzinger packs a series of assumptions into his conclusion. His primary assumption, of course, is that it was Wyeth's PBM contracts alone that "limited Cenestin's success," not Duramed's decisions or strategies for marketing its new product, nor any of the admitted clinical differences between Cenestin and Premarin, nor any other aspects of Wyeth's strategic planning for its ERT/HRT product line.

Concerning Duramed's marketing of Cenestin, Leitzinger relies [\*53] entirely upon the opinion of another of Plaintiffs' experts, Stephen Schondelmeyer, that Duramed undertook a "substantial, concerted marketing effort." (See Schondelmeyer Report, Wyeth's Exh C-11 at P92) Schondelmeyer, in turn, relies heavily upon testimony from Duramed and Solvay, its marketing partner, who (unsurprisingly) blame Wyeth almost exclusively for Cenestin's failure to achieve the market share Duramed desired. While an expert may rely on another expert's opinion under Rule 702, neither Leitzinger nor Schondelmeyer offer any objective study to confirm this point. Worse, they ignore substantial evidence in the record that contradicts their assumption. They ignore the data discussed above concerning Duramed's unfettered access to "open" formularies, a fact Duramed used as a part of its own marketing strategy. They ignore the fact that a 1.25 mg. dosage of Cenestin was not approved by the FDA until March 2000, and was unavailable on the market until May 3, 2000. This is the most popular dosage level for Premarin. (See Wyeth's Exhibit B-5) PCS Health Systems told Duramed that primary resistance to listing Cenestin on formulary was Duramed's lack of this popular dose. (See Wyeth's [\*54] Exhibit G-4, DUR010716)

Leitzinger also fails to note or take account of the undisputed clinical and therapeutic differences between Cenestin and Premarin. Those differences include Premarin's long history and track record of use, clinical studies, and long-term use for osteoporosis prevention. Wyeth used these differences in its "Premarin Strategy" advertising. And, PCS Health also told Duramed in June 2000 that Cenestin's lack of an osteoporosis indication would "likely result in a non-formulary status for 2001." (Wyeth's Exhibit G-4, DUR010717).

Plaintiffs' experts fail to address the fact that Premarin's nearest competitor in the oral ERT market, estradiol, actually doubled its market share from 1998 to 2003 (from 9.4% to 18.5%); Premarin's market share in the same period declined (from 75.3% to 68.6%). If "overall competition" was harmed by Wyeth's PBM contracts, this kind of growth in a competitor's market share should, at the least, be explained or distinguished.

Also of note is Duramed's report on United Health Care ("UHC"), a large insurer with 44 regional health plans that varied widely in the type of pharmacy benefit programs offered. In 2000, UHC agreed to allow Cenestin [\*55] equal

co-pay status with Premarin for a plan with 650,000 covered lives; the pilot program was designed to monitor market demand. Duramed notes that "unfortunately the results were less than favorable. The Cenestin market share fell far short of the targeted 5% UHC anticipated and needed to make the addition of Cenestin 'worthwhile.'" (Wyeth Exhibit G-4, DUR 010717). Indeed, Duramed's internal "review" of its managed care relations for July 2000 concludes that lack of physician demand for Cenestin was the first-listed cause of lower managed care access, "as monitored by competitive market share in unrestrictive open markets . . .". This admission significantly weakens Leitzinger's and Schondelmeyer's assumptions about Duramed's efficient, competitive marketing for Cenestin.

To similar effect is the fact that Cenestin's sales in the cash market segment, the Medicaid segment, and in the PBM-HMO segment, were all relatively stable throughout the period. If the PBM-HMO segment of the market is so critical, one would expect to see some variation between the three different segments. Plaintiffs' experts blame this on "spill over" or "threshold effect." (See, e.g., Schondelmeyer Report, [\*56] P131-132) This argument is that physicians will not write prescriptions for their patients if the drug is not listed on the patients' PBM formularies, because it may cost more (through a higher co-pay) or because the physician might get a phone call from a pharmacy. But given the feedback Duramed was receiving noted above, an equally plausible explanation is that Duramed's marketing efforts were not succeeding as well as had been expected. Leitzinger does not address this possibility.

Keith Leffler, expert for CVS and RiteAid, relies on the same facts about Wyeth's PBM contracts to conclude that "Imposition and enforcement of such contractual provisions by a dominant seller with market power are clearly anticompetitive regardless of whether they are disguised as competitive responses or discounts." (Leffler Report at P42) But beyond this characterization of conduct, Leffler does not discuss or account for any of the other potential factors that could affect the marketplace success of a competing drug, or the specific factors that may have affected Cenestin's market share. He assumes, as does Leitzinger, that Wyeth's PBM contracts caused the Cenestin market share.

But, assuming for [\*57] the moment that the cause-and-effect relationship between the PBM contracts and Cenestin's market presence is accepted, the Leitzinger and Leffler opinions on the second part of the antitrust injury analysis - that Wyeth's price increases were the result of its PBM contracts' unlawful exclusionary effects - are fatally flawed. Leffler quotes from an internal Wyeth document which states: "As market share leader in estrogen replacement therapy, Premarin . . . price increases should be aggressive to cover increasing costs and to maximize profits." (Leffler report P48, n. 72) From 1991 to 1998, Wyeth's average list price increase for Premarin was 6.7% per year. After 1998, the average price increase was 15.8% per year. Since Wyeth's costs were not increasing (at least at that rate), Leffler concludes that the price increases were implemented only to "maximize profits." But once again, profit maximization, even at the expense of a competitor, does not run afoul of the antitrust statutes.

But both experts opine that Wyeth "crossed the line" between legal profit maximization and illegal supracompetitive pricing. They both rely on economic theory to support this opinion. According to Leffler, [\*58] basic economic theory teaches that "a seller's profit maximizing price decreases when it faces more competition." (Leffler Report, P47) Wyeth's price behavior doesn't fit the theory, so he concludes that it was Wyeth's monopolistic behavior that permitted it to raise its prices in the face of competition from Cenestin.

Leitzinger also relies on "basic economic theory" that a dominant seller will lower its product price in response to market entry of competitors. This economic theory, of course, in itself contains assumptions about the relevant market - in particular, cross-elastic products and equally efficient competitors. While the record is replete with references to the uniqueness of the pharmaceutical marketplace in the United States, both Leitzinger and Leffler assume without substantive discussion that these basic pricing theories apply largely across-the-board to this unique market. There is a significant body of evidence that brand name drug prices actually rise in response to generic competition. This pricing behavior is noted in [Geneva v. Barr, 386 F.3d 485, 496-500 \(2d Cir. 2004\)](#), and in [In re Ciprofloxacin Hydrochloride Antitrust Lit., 363 F.Supp.2d 514, 521-22 \(E.D.N.Y. 2005\)](#). [\*59] The Cipro court cites a July 1998 Congressional Budget Office Study concluding that prices for brand-name drugs continue to rise

faster than inflation even after generic competition begins.<sup>9</sup> Despite this, Leitzinger and Leffler simply assume that Wyeth's pricing "should have" followed their basic theory. This Court need not accept an expert's assumption that is supported only by the "ipse dixit" of the expert. See, e.g., [General Electric v. Joiner, 522 U.S. 136, 146, 139 L. Ed. 2d 508, 118 S. Ct. 512 \(1997\)](#): "But nothing in either *Daubert* or the Federal Rules of Evidence requires a district court to admit opinion evidence which is connected to existing data only by the *ipse dixit* of the expert. A court may conclude that there is simply too great an analytical gap between the data and the opinion proffered."

Apart [\*60] from economic theory, the **factual** support for their opinions cited by both Leitzinger and Leffler consists of Wyeth's Premarin price projections. Their primary source document (Plaintiffs Exhibit 171, WYE180544 - 180553) is entitled "Strategic Options Summary" and is dated July 8, 1999. Its author (Wyeth marketing employee Steve Strickland) describes it as a "summary of each of the three year financial options for the Premarin Franchise. Each summary contains detailed assumptions and the net effect on sales." The summary contains a base case, an "upside - preferred" case, and a "downside" case. Each of the three options contains net sales return projections based on levels and qualities of marketing investment; several assumptions about the demographics of oral ERT use; Wyeth's ability to launch additional products in the ERT/HRT market and the timing of those product entries; and assumptions about various potential competitors, only one of which is Cenestin. (There can be no doubt that manufacturers keep close watch on competitors, and that product pricing decisions are based in part upon competitive market conditions. This is as true for pharmaceuticals as it is for Scotch [\*61] tape!)

From this document, Leitzinger and Leffler conclude that the alternate assumptions about Premarin price increases are **directly** linked to the alternate assumptions about Cenestin's market performance. Thus, they both conclude that once Wyeth "knew" that it was successful in limiting Cenestin's market share through its PBM contracts, it raised Premarin list price in line with the "best case" scenario of the 1999 marketing budget projections. This is a highly questionable leap of logic. There is nothing in the document stating that the alternate scenario price increases are tied to or dependent upon Wyeth's PBM contracts. Indeed, Leitzinger admitted that nothing in the document actually says what he believes it says, that the market share projections for Cenestin were tied to the stated price increase projections. Rather Leitzinger says he is **inferring** that "the difference in Cenestin's penetration was an important consideration distinguishing the pricing recommendations under the two cases." He also rejected the idea that **any** of the other critical assumptions contained in the document, such as quality and quantity of marketing, demographic changes, or introduction [\*62] of new Wyeth products, could also affect Premarin pricing. (Leitzinger Deposition, p. 192) His refusal to recognize that distinct possibility, and his failure to attempt to control for the possibility that those other factors may have played an important role in Wyeth's price increases, makes his inference untenable.

The Court finds that Plaintiffs have not established a "but-for" causative link between Wyeth's PBM contracts and Wyeth's price increases. Therefore, Plaintiffs have not shown the existence of a triable issue of fact on whether they suffered an "antitrust injury." (The same fatal flaw exists for Plaintiffs' "but-for" damages model, which the Court need not discuss at length. Absent proof of a causative link between the alleged monopolistic conduct and the alleged supracompetitive price, the "but-for" Premarin prices offered by Leitzinger and Leffler are untenable.)

## CONCLUSION

For all of the foregoing reasons, the Court will grant Wyeth's motion for summary judgment (Doc. 135) against Class Plaintiffs and intervenors CVS and Rite Aid. The motions for leave to file supplemental briefs are denied.

DATED: June 13, 2005

Sandra S. Beckwith, Chief Judge

United [\*63] States District Court

<sup>9</sup>CBO, "How Increased Competition from Generic Drugs Has Affected Prices and Returns in the Pharmaceutical Industry" (July 1998). A portion of this report is contained in Wyeth's Exhibit B-10, Doc. 135.

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## MacArthur v. San Juan County

United States District Court for the District of Utah, Central Division

June 13, 2005, Decided ; June 13, 2005, Filed

Civil No. 2:00-CV-584J

### **Reporter**

416 F. Supp. 2d 1098 \*; 2005 U.S. Dist. LEXIS 25235 \*\*; 2005-1 Trade Cas. (CCH) P74,869

DR. STEVEN MACARTHUR, et al., Plaintiffs, vs. SAN JUAN COUNTY, et al., Defendants.

**Subsequent History:** [\*\*1] Later proceeding at *MacArthur v. San Juan County*, 416 F. Supp. 2d 1098, 416 F. Supp. 2d 1098, 2005 U.S. Dist. LEXIS 43695 (D. Utah, 2005)

**Prior History:** [\*Macarthur v. San Juan County\*, 309 F.3d 1216, 2002 U.S. App. LEXIS 20987 \(10th Cir. Utah, 2002\)](#)

## **Core Terms**

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privileges, Plaintiffs', patients, proposed amended complaint, pretrial order, medical staff, pretrial conference, allegations, supervision, rights, facilities, staff privileges, clinic, staff, emergency room, anti trust law, deprivation, pretrial, fair dealing, cards, damages, pleaded, constitutional right, defamation, motion to dismiss, summary judgment, antitrust, member of the board, parties, cause of action

## **LexisNexis® Headnotes**

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Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### **HN1 [down arrow] Conferences, Pretrial Conferences**

At a pretrial conference, consideration may be given, and the court may take appropriate action, with respect to the formulation and simplification of the issues, including the elimination of frivolous claims or defenses. [Fed. R. Civ. P. 16\(c\)\(1\)](#).

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### **HN2 [down arrow] Conferences, Pretrial Conferences**

The reference in [Fed. R. Civ. P. 16\(c\)\(1\)](#) to "formulation" is intended to clarify and confirm the court's power to identify the litigable issues. It has been added in the hope of promoting efficiency and conserving judicial resources by identifying the real issues prior to trial, thereby saving time and expense for everyone. The notion is emphasized by expressly authorizing the elimination of frivolous claims or defenses at a pretrial conference. There is no reason to require that this await a formal motion for summary judgment. Nor is there any reason for the court to wait for the parties to initiate the process called for in [Rule 16\(c\)\(1\)](#). [Fed. R. Civ. P. 16](#), advisory committee's notes. The court at

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the pretrial conference, thus, is directed to define the issues, facts, and theories actually in contention, which means that extraneous issues should be weeded out.

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### [HN3](#) [] Conferences, Pretrial Conferences

As a case takes shape and the court struggles to narrow and pinpoint the issues, the parties have an unflagging obligation to spell out squarely and distinctly those claims they desire to advance at the trial proper. Good-faith compliance with [Fed. R. Civ. P. 16](#) plays an important role in this process. [Rule 16\(c\)\(1\)](#) places upon counsel a substantial responsibility for assisting the court in identifying the factual issues worthy of trial. [Fed. R. Civ. P. 16](#), advisory committee's notes. Attorneys at a pre-trial conference must make a full and fair disclosure of their views as to what the real issues of the trial will be. D. Utah Civ. R. 7-l(d).

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### [HN4](#) [] Conferences, Pretrial Conferences

[Fed. R. Civ. P. 16\(c\)](#) confirms the court's power to identify the litigable issues and to eliminate frivolous claims or defenses without awaiting the making of a summary judgment or other motion by the parties. But at the same time, counsel bear a substantial responsibility in formulating the triable issues in that they must identify these issues for the court or they waive the right to have them tried.

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### [HN5](#) [] Conferences, Pretrial Conferences

See D. Utah Civ. R. 16(c).

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

### [HN6](#) [] Conferences, Pretrial Conferences

Local rules of the United States District Court for the District of Utah anticipate that trial counsel will be fully prepared to participate in the pretrial examination of the issues contemplated by [Fed. R. Civ. P. 16\(c\)](#).

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

### [HN7](#) [] Motions to Dismiss, Failure to State Claim

A grievance involving a governmental unit is still a grievance, but a grievance may or may not be a claim upon which relief can be granted in a judicial proceeding. [Fed. R. Civ. P. 12\(b\)\(6\)](#).

Governments > Local Governments > Administrative Boards

**HN8** [blue download icon] Local Governments, Administrative Boards

San Juan County is organized as a political subdivision of the State of Utah under the Utah Constitution and [Utah Code Ann. § 17-50-101 et seq.](#) (2001). The San Juan Health Services District (SJHSD) is organized as a special service district under the Utah Code Ann. § 17A-2-1301 et seq. (2004), and is funded in part through tax revenues. San Juan County appoints the members of the SJHSD governance board. Utah Code Ann. § 17A-2-1326 (2001).

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

**HN9** [blue download icon] Complaints, Requirements for Complaint

Generally, a pleading must contain a short and plain statement of the claim showing that the pleader is entitled to relief. [Fed. R. Civ. P. 8\(a\)\(2\)](#). Accordingly, a pleading must give fair notice and state the elements of the claim plainly and succinctly. To give such notice, a pleading must set forth specific facts as the basis for the plaintiffs' claims, not merely legal conclusions. Without specific facts, claims are little more than conclusory allegations, which are insufficient to state a claim for relief.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Judgments > Summary Judgment > General Overview

Civil Procedure > Pretrial Matters > Conferences > Pretrial Conferences

**HN10** [blue download icon] Motions to Dismiss, Failure to State Claim

The parties may test the legal sufficiency of claims by motion under [Fed. R. Civ. P. 12\(b\)\(6\)](#) or [56](#), and [Fed. R. Civ. P. 16](#) empowers district courts to weed out frivolous claims. There is no reason to require that the elimination of frivolous claims await a formal motion for summary judgment, [Fed. R. Civ. P. 16\(c\)\(1\)](#), advisory committee's notes, and it certainly is not inconsistent with the general purpose of [Rule 16](#) to use this rule to determine whether there are any issues remaining in the case that justify proceeding to a full trial on the merits.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

**HN11** [blue download icon] Racketeer Influenced & Corrupt Organizations, Claims

In order to state a civil Racketeer Influenced Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), claim, a plaintiff must allege that he or she suffered (1) an injury to his or her business or property because the defendant(s), (2) while involved in one or more enumerated relationships with an "enterprise," (3) engaged in a pattern of racketeering activity or collected an unlawful debt. [18 U.S.C.S. §§ 1961-1968](#).

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

**HN12** [blue download icon] Racketeer Influenced & Corrupt Organizations, Claims

Among the essential elements required to establish civil liability under the Racketeer Influenced Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), statute, plaintiffs must show that the defendants have conducted the affairs of an identifiable "enterprise" through a "pattern of racketeering activity," that is, that the defendants have committed a continuous series of related criminal acts in violation of one or more of the statutes

listed in [18 U.S.C.S. § 1961\(1\)](#). [18 U.S.C.S. § 1962](#). Defendants need not engage in the stereotypical mobster behavior to come within the bounds of civil RICO, but they must nevertheless be shown to have participated in continuing criminal violations constituting an identifiable "pattern of racketeering activity." The various acts of racketeering activity described in the statute are often referred to as "predicate acts" because they form the basis for liability under RICO.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > Fraud

Criminal Law & Procedure > ... > Fraud Against the Government > Mail Fraud > General Overview

#### [\*\*HN13\*\*](#) [ ] **Claims, Fraud**

See [18 U.S.C.S. § 1341](#).

Criminal Law & Procedure > ... > Fraud Against the Government > Mail Fraud > Elements

#### [\*\*HN14\*\*](#) [ ] **Mail Fraud, Elements**

In order to prove the offense defined in [18 U.S.C.S. § 1341](#) in a criminal proceeding, the government must prove the following essential elements: (1) that the defendant knowingly devised or knowingly participated in a scheme or artifice for obtaining money or property by means of false or fraudulent pretenses, representations, or promises; (2) that the pretenses, representations or promises were material, that is, they would reasonably influence a person to part with money or property; (3) that the defendant did so with the intent to defraud; and (4) that in advancing, or furthering, or carrying out this scheme to obtain money or property by means of false or fraudulent pretenses, representations, or promises, the defendant used the mail, or any private or commercial interstate carrier, or caused the same to be used by someone else.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > Fraud

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

#### [\*\*HN15\*\*](#) [ ] **Claims, Fraud**

To establish mail fraud as a predicate act of racketeering activity for the purposes of a civil Racketeer Influenced Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), claim, plaintiffs must plead and prove facts establishing each of these essential elements as to each occurrence, as to each predicate act alleged as part of the requisite "pattern of racketeering activity." [Fed. R. Civ. P. 9\(b\)](#) requires that allegations of mail fraud be pleaded with particularity.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > Fraud

Criminal Law & Procedure > ... > Fraud Against the Government > Mail Fraud > Elements

#### [\*\*HN16\*\*](#) [ ] **Claims, Fraud**

Mail fraud is not committed simply by sending false statements through the mail; the mails must have been used to further a scheme to defraud or obtain money or property through false pretenses.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > Fraud

Criminal Law & Procedure > ... > Fraud Against the Government > Mail Fraud > Elements

#### **HN17** [ ] **Claims, Fraud**

The essential elements of mail fraud are a scheme or artifice to defraud, namely, to obtain money or property by means of false or fraudulent pretenses, representations, or promises, and the use of the mails in furtherance of the scheme.

Criminal Law & Procedure > ... > Obstruction of Administration of Justice > Witness Tampering > Elements

#### **HN18** [ ] **Witness Tampering, Elements**

The language of 18 U.S.C.S. § 1512 prohibits specific conduct, including physical force, threats of physical force, or intimidation, threatening, "corrupt" or "misleading" persuasion or harassment, that is intended to "influence, delay or prevent" a witness from attending or testifying in an official proceeding, or intended to cause testimony, records, documents, or other objects to be withheld, concealed, altered or destroyed in order to impair their availability for use in an official proceeding. [18 U.S.C.S. § 1512\(a\), \(b\), \(c\), \(d\)](#). [Section 1512](#) prohibits only the coercive conduct specifically described in its subsections; the legislative history reflects Congress' rejection of broadly inclusive language in favor of the specific conduct narrowly described in the final version of the statute.

Criminal Law & Procedure > ... > Obstruction of Administration of Justice > Witness Tampering > Elements

#### **HN19** [ ] **Witness Tampering, Elements**

Prospective fact witnesses may indeed feel fearful, anxious or apprehensive about how their testimony may be responded to by those against whom it may be offered. In some cases, potential witnesses may fear for their very lives, and with good reason. Federal law affords such witnesses some degree of protection. [18 U.S.C.S. § 1513](#) (retaliation against witness); [18 U.S.C.S. §§ 3521-3528](#) (federal witness protection program). But fear, anxiety and apprehension on the part of a prospective witness as to a future loss of employment, denial of services, or other adverse personal consequences do not equate with the culpable criminal conduct on the part of a defendant that violates [18 U.S.C.S. § 1512](#). A defendant must do something--use physical force, threats of physical force, or intimidation, threatening, corrupt or misleading persuasion or harassment--that is intended to "influence, delay or prevent" a witness from attending or testifying in an official proceeding, or intended to cause testimony, records, documents, or other objects to be withheld, concealed, altered or destroyed in order to impair their availability for use in an official proceeding, in order to run afoul of the witness tampering statute. [18 U.S.C.S. § 1512\(a\)-\(d\)](#).

Criminal Law & Procedure > ... > Obstruction of Administration of Justice > Witness Tampering > Elements

#### **HN20** [ ] **Witness Tampering, Elements**

The provisions of [18 U.S.C.S. § 1512](#) address specific affirmative, coercive, or misleading conduct intended to inhibit or influence future witness testimony or the availability of evidence yet to be offered in a pending or future federal proceeding.

Criminal Law & Procedure > ... > Obstruction of Administration of Justice > Witness Tampering > Elements

## [\*\*HN21\*\*](#) [blue download icon] **Witness Tampering, Elements**

The provisions of [18 U.S.C.S. § 1513](#) prohibit violent retaliation, for example, killing, attempting to kill, causing bodily injury, or damaging tangible property, against any person for attending or furnishing testimony or evidence in a federal proceeding or providing information to a law enforcement officer relating to the commission or possible commission of a federal offense. [18 U.S.C.S. § 1513\(a\), \(b\)](#).

Criminal Law & Procedure > ... > Extortion > Hobbs Act > Elements

## [\*\*HN22\*\*](#) [blue download icon] **Hobbs Act, Elements**

The Anti-Racketeering Act of 1934, [18 U.S.C.S. § 1951](#), makes it a federal offense to commit robbery or extortion that in any way or degree obstructs commerce. To prove guilt, the government must prove that a defendant committed extortion or robbery, and that such conduct interfered with interstate commerce.

Criminal Law & Procedure > ... > Extortion > Hobbs Act > Elements

## [\*\*HN23\*\*](#) [blue download icon] **Hobbs Act, Elements**

The Hobbs Act's definition of "extortion" as the obtaining of property from another, with his consent, induced by wrongful use of actual or threatened force, violence, or fear, or under color of official right, [18 U.S.C.S. § 1951\(b\)\(2\)](#), is read to require that a person must "obtain" property from another party to commit extortion, that is, that there must be not only the deprivation but also the acquisition of property.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

## [\*\*HN24\*\*](#) [blue download icon] **Racketeer Influenced & Corrupt Organizations, Claims**

A private civil action under the federal Racketeer Influenced Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), statute remains available as a means for those persons who have been injured in their business or property by reason of a violation of RICO's criminal provisions to seek legal and equitable remedies for their injuries from those whose ongoing criminal conduct has caused them harm. [18 U.S.C.S. § 1964](#). However, civil RICO liability does not serve merely as a device to multiply the money damages available to parties embroiled in more commonplace civil litigation, or as a means to vilify civil litigants by labeling them as "racketeers," gangsters, extortionists and criminals.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## [\*\*HN25\*\*](#) [blue download icon] **Racketeer Influenced & Corrupt Organizations, Claims**

Where a plaintiff's complaint fails to allege specific facts stating the elements essential to her federal claim under the Racketeer Influenced Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), dismissal with prejudice is warranted.

Civil Rights Law > Criminal Interference With Civil Rights > Access to Clinics

Healthcare Law > ... > Reproductive Services > Reproductive Technology > Access to Services

#### **HN26** [blue icon] **Criminal Interference With Civil Rights, Access to Clinics**

The Freedom of Access to Clinic Entrances Act of 1994, [18 U.S.C.S. §§ 241, 248](#), addresses the conduct of anyone who by force or threat of force or by physical obstruction, intentionally injures, intimidates or interferes with or attempts to injure, intimidate or interfere with any person because that person is or has been, or in order to intimidate such person or any other person or any class of persons from, obtaining or providing reproductive health services, or that person is exercising or seeking to exercise the [First Amendment](#) right of religious freedom at a place of religious worship. Though it is primarily a criminal statute, [18 U.S.C.S. § 248\(c\)\(1\)](#) provides that any person aggrieved by reason of the conduct prohibited by [§ 248\(a\)](#) may commence a civil action seeking temporary, preliminary or permanent injunctive relief and compensatory and punitive damages, as well as the costs of suit and reasonable fees for attorneys and expert witnesses, or as an alternative to compensatory damages, an award of statutory damages in the amount of \$ 5,000 per violation. [18 U.S.C.S. § 248\(c\)\(1\)\(A\), \(b\)](#).

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

#### **HN27** [blue icon] **Governmental & Nonprofit Liability, Health Care Quality Improvement Act**

Title IV, § 412 of the Health Care Quality Improvement Act, [42 U.S.C.S. §§ 11101-11152](#), specifically [42 U.S.C.S. § 11112](#), does set standards for professional review actions affecting a health practitioner's practice privileges, but it does so in the context of a statutory scheme that shields the review participants from civil liability arising from the review action if that action satisfies [42 U.S.C.S. § 11112](#)'s procedural criteria. [42 U.S.C.S. § 11111](#).

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

#### **HN28** [blue icon] **Governmental & Nonprofit Liability, Health Care Quality Improvement Act**

See [42 U.S.C.S. § 11112\(a\)](#).

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

#### **HN29** [blue icon] **Governmental & Nonprofit Liability, Health Care Quality Improvement Act**

See [42 U.S.C.S. § 11111\(1\)](#).

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

#### **HN30** [blue icon] **Governmental & Nonprofit Liability, Health Care Quality Improvement Act**

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The Health Care Quality Improvement Act, [42 U.S.C.S. §§ 1101-1112](#), specifically [42 U.S.C.S. § 1111](#) makes an express exception as to liability under any law of the United States or any state relating to the civil rights of any person or persons, including the Civil Rights Act of 1964, [42 U.S.C.S. § 2000e et seq.](#), and the Civil Rights Acts, 42 U.S.C.S. § 1981 et seq., and for actions by the Attorney General under the federal antitrust laws.

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

#### [\*\*HN31\*\*](#) [blue icon] **Governmental & Nonprofit Liability, Health Care Quality Improvement Act**

The Health Care Quality Improvement Act (HCQIA), [42 U.S.C.S. §§ 1101-1112](#), does not create a private civil cause of action in favor of plaintiffs whose staff privileges at a medical facility have been adversely affected by a professional or peer review action. Therefore, in the context of a grievance by a health care professional whose staff privileges have been limited or denied by a peer review process, the question posed by the HCQIA is not whether the participants in the review process are liable under the HCQIA, but whether the HCQIA operates to immunize those participants from private civil liability based upon other legal theories.

Healthcare Law > Medical Treatment > Failures & Refusals to Treat > Patient Anti-Dumping Act

#### [\*\*HN32\*\*](#) [blue icon] **Failures & Refusals to Treat, Patient Anti-Dumping Act**

The Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C.S. § 1395dd](#), places obligations of screening and stabilization upon hospitals and emergency rooms that receive patients suffering from an "emergency medical condition." Among other provisions, EMTALA requires the emergency departments of hospitals participating in the federal Medicare program to provide appropriate medical screening and stabilizing treatment for all persons who present themselves at the emergency room and request care.

Healthcare Law > Medical Treatment > Failures & Refusals to Treat > Patient Anti-Dumping Act

#### [\*\*HN33\*\*](#) [blue icon] **Failures & Refusals to Treat, Patient Anti-Dumping Act**

See [42 U.S.C.S. § 1395dd\(a\), \(b\)](#).

Healthcare Law > Medical Treatment > Failures & Refusals to Treat > Patient Anti-Dumping Act

Healthcare Law > ... > Actions Against Facilities > Emergency Care Negligence > Patient Anti-Dumping Act

#### [\*\*HN34\*\*](#) [blue icon] **Failures & Refusals to Treat, Patient Anti-Dumping Act**

The Emergency Medical Treatment and Active Labor Act, [42 U.S.C.S. § 1395dd\(c\)](#), sets standards governing the transfer of emergency room patients to other health care facilities, and [§ 1395dd\(d\)](#) provides for the enforcement of [§ 1395dd](#)'s requirements through civil monetary penalties collected by the Secretary of Health and Human Services and through private civil actions by any individual who suffers personal harm as a direct result of a participating hospital's violation of a requirement of this section. [42 U.S.C.S. § 1395dd\(d\)\(2\)](#). The statute is construed as imposing strict liability on hospitals for violations of its screening and stabilization requirements.

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Healthcare Law > Medical Treatment > Failures & Refusals to Treat > Patient Anti-Dumping Act

Healthcare Law > ... > Actions Against Facilities > Emergency Care Negligence > Patient Anti-Dumping Act

### **HN35** [blue icon] Failures & Refusals to Treat, Patient Anti-Dumping Act

See [42 U.S.C.S. § 1395dd\(d\)\(2\)](#).

Healthcare Law > Medical Treatment > Failures & Refusals to Treat > Patient Anti-Dumping Act

### **HN36** [blue icon] Failures & Refusals to Treat, Patient Anti-Dumping Act

A hospital's duty to provide the required emergency medical screening and stabilizing treatment to persons requesting such care cannot be delayed by any inquiry as to that person's "method of payment or insurance status." [42 U.S.C.S. § 1395dd\(h\)](#). Nor is the participating hospital's duty to provide emergency screening and treatment under the Emergency Medical Treatment and Active Labor Act, [42 U.S.C.S. § 1395dd\(a\)](#) and [\(b\)](#), limited to those persons who are regularly in the care of physicians or health care providers having current staff privileges or practice privileges at that hospital.

Public Health & Welfare Law > ... > Medicare > Providers > General Overview

### **HN37** [blue icon] Medicare, Providers

See [42 U.S.C.S. § 1395a\(a\)](#).

Public Health & Welfare Law > ... > Medicare > Providers > General Overview

### **HN38** [blue icon] Medicare, Providers

Section 1802 of Title XVIII of the Social Security Act, [42 U.S.C.S. § 1395a](#), the so-called Medicare "freedom of choice provision," reflects one of the fundamental principles upon which the Medicare program was founded, and guarantees Medicare beneficiaries the freedom to choose health care providers, who would then be paid by Medicare at the program's prescribed rates. [Section 1395a\(a\)](#) bars interference by the Secretary of Health and Human Services or his subordinates in the administration of the Medicare program with a beneficiary's selection of a physician.

Civil Rights Law > ... > Contractual Relations & Housing > Equal Rights Under the Law (sec. 1981) > General Overview

### **HN39** [blue icon] Contractual Relations & Housing, Equal Rights Under the Law (sec. 1981)

See [42 U.S.C.S. § 1981](#).

Civil Rights Law > ... > Contractual Relations & Housing > Equal Rights Under the Law (sec. 1981) > Proof of Discrimination

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#### **[HN40](#)[] Equal Rights Under the Law (sec. 1981), Proof of Discrimination**

The provisions of [42 U.S.C.S. § 1981](#) address intentional racial discrimination in the making and enforcement of contracts: A [§ 1981](#) plaintiff must prove by a preponderance of the evidence that the defendant intentionally discriminated against him or her on the basis of race.

Civil Rights Law > ... > Contractual Relations & Housing > Equal Rights Under the Law (sec. 1981) > Protected Classes

#### **[HN41](#)[] Equal Rights Under the Law (sec. 1981), Protected Classes**

The United States Supreme Court construes the language of [42 U.S.C.S. § 1981](#) that secures to all the same contracting rights as "white citizens" to refer only to the racial, as opposed to, say, gender-based or religious, character of the prohibited discrimination. Whites as well as blacks may assert contract denial claims under [§ 1981](#) on the basis of race. "Ancestry" as "race," as a prohibited basis for discrimination for purposes of [§ 1981](#), does not embrace national origin, religion, or status as an alien.

Civil Rights Law > ... > Contractual Relations & Housing > Equal Rights Under the Law (sec. 1981) > Proof of Discrimination

#### **[HN42](#)[] Equal Rights Under the Law (sec. 1981), Proof of Discrimination**

To state a claim under [42 U.S.C.S. § 1981](#), the plaintiffs must show that (1) they are members of an identifiable racial or ancestral group; (2) the defendant had an intent to discriminate on the basis of their race or ancestry; and (3) the discrimination concerned one or more of the activities enumerated in the statute, namely, the making and enforcing of a contract. A [§ 1981](#) claim for interference with the right to make and enforce a contract must allege the actual loss of a contract interest, not merely the possible loss of future contract opportunities.

Civil Rights Law > ... > Contractual Relations & Housing > Equal Rights Under the Law (sec. 1981) > Protected Classes

#### **[HN43](#)[] Equal Rights Under the Law (sec. 1981), Protected Classes**

Prudential limitations on standing ordinarily require that an action under [42 U.S.C.S. § 1981](#) be brought by the direct victims of the alleged discrimination because they are best situated to assert the individual rights in question.

Civil Rights Law > Protection of Rights > Conspiracy Against Rights > General Overview

#### **[HN44](#)[] Protection of Rights, Conspiracy Against Rights**

See [42 U.S.C.S. § 1985\(3\)](#).

Civil Rights Law > Protection of Rights > Conspiracy Against Rights > Elements

#### **[HN45](#)[] Conspiracy Against Rights, Elements**

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To state a claim under [42 U.S.C.S. § 1985](#), there must be some racial, or perhaps otherwise class-based, invidiously discriminatory animus behind the conspirators' action. A plaintiff who fails to allege racial or class-based discrimination cannot state a claim under [§ 1985\(3\)](#).

Civil Rights Law > Protection of Rights > Section 1983 Actions > General Overview

## [HN46](#) [+] Protection of Rights, Section 1983 Actions

See [42 U.S.C.S. § 1983](#).

Civil Rights Law > ... > Section 1983 Actions > Elements > General Overview

## [HN47](#) [+] Section 1983 Actions, Elements

The language of 42 U.S.C.S. § 1983 provides an enforcement remedy for one who is deprived under color of state law of any rights, privileges, or immunities secured by the Constitution. There are two elements to a § 1983 claim: (1) the conduct complained of must have been under color of state law, and (2) the conduct must have subjected the plaintiff to a deprivation of constitutional rights, or rights protected by federal law.

Civil Rights Law > ... > Section 1983 Actions > Elements > Causal Relationship

## [HN48](#) [+] Elements, Causal Relationship

The language of [42 U.S.C.S. § 1983](#) does not specify the state of mind on the part of someone who "subjects, or causes to be subjected" a person to a deprivation of civil rights which a plaintiff must allege and prove to establish liability under the statute; the question is did the defendant violate the plaintiff's [Fourteenth Amendment](#) rights? The defendant's state of mind is relevant only to the existence of the claimed [Fourteenth Amendment](#) violation. Although [§ 1983](#) does not require a specific state of mind for actionability, a court must examine closely the nature of the constitutional right asserted to determine whether a deprivation of that right requires any particular state of mind. For instance, deprivations of equal protection require proof of discriminatory intent on the part of the state actor, while deprivations under the [Eighth Amendment](#) require a showing of deliberate indifference. Moreover, some deprivations of [First Amendment](#) rights require proof that the state's action was intended to repress an individual's protected speech or association.

Civil Rights Law > ... > Section 1983 Actions > Elements > Protected Rights

## [HN49](#) [+] Elements, Protected Rights

In order to state a claim under [42 U.S.C.S. § 1983](#), a complaint must assert a right to recover under the Constitution or other federal laws and not be wholly insubstantial and frivolous. Conclusionary allegations, unsupported by facts, will be rejected as insufficient to state a claim under the Civil Rights Act. The plaintiff must allege with at least some degree of particularity overt acts which defendants engaged in that support the plaintiff's claim.

Civil Rights Law > ... > Section 1983 Actions > Elements > General Overview

## [HN50](#) [+] Section 1983 Actions, Elements

In order to prevail on a claim for a [42 U.S.C.S. § 1983](#) conspiracy, a plaintiff must plead and prove not only a conspiracy, but also an actual deprivation of rights; pleading and proof of one without the other will be insufficient. In pleading conspiracy, a plaintiff must allege specific facts showing agreement and concerted action among the alleged co-conspirators. Conclusory allegations of conspiracy are insufficient to state a valid [§ 1983](#) claim. Thus, a plaintiff fails to state a claim for conspiracy absent specific facts showing a "meeting of the minds" among the alleged co-conspirators.

Civil Rights Law > ... > Immunity From Liability > Local Officials > Direct Causal Links

#### [HN51](#) [] Local Officials, Direct Causal Links

A local government may be liable under [42 U.S.C.S. § 1983](#) if the action that is alleged to be unconstitutional implements or executes a policy, statement, ordinance, regulation, or decision officially adopted and promulgated by that body's officers. Causation presents a threshold question: the first inquiry in any case alleging local governmental liability under [§ 1983](#) is the question whether there is a direct causal link between a local governmental policy or custom and the alleged constitutional deprivation, because it is only when the execution of the government's policy or custom inflicts the injury that a local government entity may be held liable under [42 U.S.C.S. § 1983](#).

Civil Rights Law > ... > Immunity From Liability > Local Officials > Deliberate Indifference

#### [HN52](#) [] Local Officials, Deliberate Indifference

Assuming that causation may be shown, to subject a governmental entity to liability under [42 U.S.C.S. § 1983](#), a municipal policy must be a policy statement, ordinance, regulation, or decision officially adopted and promulgated by a municipality's officers. Absent such an official policy, a municipality may also be held liable if the discriminatory practice is so permanent and well settled as to constitute a "custom or usage" with the force of law. Thus, acts that do not rise to the level of official policy may nonetheless create liability if they are sufficiently widespread and pervasive so as to constitute a custom. However, conduct directed solely at a plaintiff may not demonstrate a custom or policy of the entity to be deliberately indifferent to that conduct as a general matter.

Civil Rights Law > ... > Immunity From Liability > Local Officials > Deliberate Indifference

Civil Rights Law > ... > Immunity From Liability > Local Officials > Direct Causal Links

#### [HN53](#) [] Local Officials, Deliberate Indifference

The deliberate indifference standard may be satisfied when the municipality has actual or constructive notice that its action or failure is substantially certain to result in a constitutional violation, and it consciously and deliberately chooses to disregard the risk of harm. Although a single incident generally will not give rise to liability, deliberate indifference may be found absent a pattern of unconstitutional behavior if a violation of federal rights is a "highly predictable" or "plainly obvious" consequence of a municipality's action. The official position must operate as the "moving force" behind the violation, and the plaintiff must demonstrate a "direct causal link" between the action and the right violation.

Civil Rights Law > ... > Immunity From Liability > Local Officials > Direct Causal Links

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#### **HN54** [blue document icon] Local Officials, Direct Causal Links

The policy "causation" question presupposes that a deprivation of constitutional rights has occurred by a municipality; if there was no deprivation, the policy or custom is immaterial.

Civil Rights Law > ... > Immunity From Liability > Local Officials > Customs & Policies

Civil Rights Law > Protection of Rights > Immunity From Liability > Respondeat Superior Distinguished

#### **HN55** [blue document icon] Local Officials, Customs & Policies

The doctrine of respondeat superior is not applicable to render a supervisor or other superior liable under [42 U.S.C.S. § 1983](#) for the unconstitutional conduct of his subordinates. Vicarious liability under the doctrine of respondeat superior cannot be applied either to superiors or to local government entities under [§ 1983](#), under any circumstances. Instead, local governmental entities are suable persons under [§ 1983](#) and can be held liable for their unconstitutional policies, practices, and customs.

Civil Rights Law > Protection of Rights > Immunity From Liability > Respondeat Superior Distinguished

#### **HN56** [blue document icon] Immunity From Liability, Respondeat Superior Distinguished

The superior does not and should not invariably have a [42 U.S.C.S. § 1983](#) duty, solely by reason of position, to compensate a person whose constitutional rights have been violated by subordinates. What is currently required in order for the superior to have such a duty is that the superior personally either acted unconstitutionally or with deliberate indifference. That is, the superior must have possessed either the state of mind for the particular constitutional violation or deliberate indifference, and must also have played a causal role in plaintiff's constitutional deprivation.

Civil Rights Law > Protection of Rights > Immunity From Liability > Respondeat Superior Distinguished

#### **HN57** [blue document icon] Immunity From Liability, Respondeat Superior Distinguished

The language of [42 U.S.C.S. § 1983](#) addresses conduct which subjects, or causes to be subjected, the plaintiff to a deprivation of civil rights, requiring pleading and proof of a causal connection between a defendant's conduct and the constitutional deprivation suffered by the plaintiff. Thus, theories of vicarious liability are not available to [§ 1983](#) plaintiffs. Only the direct acts or omissions of government officials, not the acts of subordinates, will give rise to individual liability under [§ 1983](#). Where an official becomes aware of a constitutional violation only after the fact, he or she cannot be held liable for the violation under [§ 1983](#) because the violation has already occurred and the official played no causal role in it. Thus, some personal involvement of the supervisory official in the subordinate's unconstitutional conduct, analogous to the official policy or custom requirement for local government liability, must be shown for [§ 1983](#) liability.

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### **HN58** [blue document icon] Immunity From Liability, Defenses

Government officials performing discretionary functions generally are shielded from liability from civil damages insofar as their conduct does not violate clearly established statutory or constitutional rights of which a reasonable

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person would have known. Although courts have derived from this statement a variety of multi-part tests, the essential inquiry is would an objectively reasonable official have known that his conduct was unlawful?

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### [HN59](#) [+] **Immunity From Liability, Defenses**

In the Tenth Circuit, courts employ a three-step qualified immunity inquiry. First, a court asks whether the plaintiffs allegations, if true, establish a constitutional violation. If not, the suit is dismissed; if so, the court moves to the second step: whether the law was clearly established at the time the alleged violations occurred. This step gives the official an opportunity to show that he neither knew nor should have known of the relevant legal standard because the law was not clearly established at the time he acted. Where the law is not clearly established, courts do not require officials to anticipate its future developments, and qualified immunity is therefore appropriate. If the law was clearly established, the court reaches the third step of the inquiry: whether, in spite of the fact that the law was clearly established, "extraordinary circumstances," such as reliance on the advice of counsel or on a statute, so prevented the official from knowing that his actions were unconstitutional that he should not be imputed with knowledge of a clearly established right. This occurs only "rarely."

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### [HN60](#) [+] **Immunity From Liability, Defenses**

Whether an official is protected by qualified immunity turns upon the objective legal reasonableness of the action, in light of legal rules clearly established at the time the action was taken. The contours of the right allegedly violated must be sufficiently clear so that a reasonable official would understand that what he or she is doing violates that right. This is not to say that an official action is protected by qualified immunity unless the very action in question has previously been held unlawful, but it is to say that in light of pre-existing law that unlawfulness must be apparent. Thus, if prior case law provides "fair warning" that an officer's conduct would violate the plaintiff's constitutional rights, officials can still be on notice that their conduct violates established law even in novel factual circumstances.

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

Evidence > Burdens of Proof > Burden Shifting

#### [HN61](#) [+] **Immunity From Liability, Defenses**

Once a defendant raises the defense of qualified immunity, the burden shifts to the plaintiff to satisfy a heavy two-part burden to demonstrate that the defendant violated a constitutional or statutory right and that the right at issue was clearly established at the time of the defendant's unlawful conduct. If the plaintiff cannot make both showings, the defendant is entitled to qualified immunity; if he can, the burden shifts to the defendant to prove that there are no genuine issues of material fact and that he or she is entitled to judgment as a matter of law.

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### [HN62](#) [+] **Immunity From Liability, Defenses**

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Qualified immunity is governed by an objective reasonableness standard, and evidence concerning the defendant's subjective intent is simply irrelevant to that defense.

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### **HN63** [blue icon] **Immunity From Liability, Defenses**

In order for the law to be clearly established there must have been a United States Supreme Court or other Tenth Circuit decision on point so that the contours of the right were sufficiently clear that a reasonable official would understand that what he is doing violates that right.

Civil Rights Law > Protection of Rights > Immunity From Liability > Defenses

#### **HN64** [blue icon] **Immunity From Liability, Defenses**

Qualified immunity establishes a right not to be tried. The entitlement to qualified immunity is an immunity from suit rather than a mere defense to liability, and like an absolute immunity, it is effectively lost if a case is erroneously permitted to go to trial.

Constitutional Law > Substantive Due Process > Deprivation of Economic Interests

#### **HN65** [blue icon] **Substantive Due Process, Deprivation of Economic Interests**

The Fourteenth Amendment's "liberty" guarantee includes an individual's right to engage in any of the common occupations of life. Liberty denotes not merely freedom from bodily restraint but also the right of the individual to contract, to engage in any of the common occupations of life, to acquire useful knowledge, to marry, establish a home and bring up children, to worship God according to the dictates of his own conscience, and generally to enjoy those privileges long recognized as essential to the orderly pursuit of happiness by free men. In a Constitution for a free people, there can be no doubt that the meaning of "liberty" must be broad indeed.

Constitutional Law > Substantive Due Process > Deprivation of Economic Interests

#### **HN66** [blue icon] **Substantive Due Process, Deprivation of Economic Interests**

The Due Process Clause of the Fourteenth Amendment protects an individual's liberty interest which is viewed as including an individual's freedom to work and earn a living and to establish a home and position in one's community. It requires no argument to show that the right to work for a living in the common occupations of the community is of the very essence of the personal freedom and opportunity that it was the purpose of the Fourteenth Amendment to secure.

Constitutional Law > Substantive Due Process > Deprivation of Economic Interests

Healthcare Law > Business Administration & Organization > Hospital Privileges > General Overview

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

## **HN67** [blue icon] **Substantive Due Process, Deprivation of Economic Interests**

A physician's "liberty" interest in pursuing his or her professional practice and establishing a home and position in a particular community does not per se entitle the physician to exercise plenary staff privileges at public hospitals or medical facilities. A doctor has no constitutional right to the staff privileges of a hospital merely because he is licensed to practice medicine. Generally, a physician is limited to assertion of a substantive due process right not to be excluded from staff privileges except for reasons related to the operation of the hospital which are not arbitrary or capricious, and a right to procedural due process sufficient to ensure that the physician has an opportunity to demonstrate that the exclusion is not justified.

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Healthcare Law > Business Administration & Organization > Hospital Privileges > General Overview

## **HN68** [blue icon] **Procedural Due Process, Scope of Protection**

A physician's liberty interest in pursuing a professional practice raises procedural due process concerns with respect to the grant or denial of staff privileges at a public hospital or medical facility once a request for such privileges has been made.

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

## **HN69** [blue icon] **Procedural Due Process, Scope of Protection**

The essence of Fourteenth Amendment due process analysis is the implication of a liberty or property interest. Under the Fourteenth Amendment, procedural due process requires notice and a pre-deprivation hearing before property interests are negatively affected by governmental actors. Health care professionals have been held to have a property interest in their professional licenses.

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Healthcare Law > Business Administration & Organization > Hospital Privileges > General Overview

## **HN70** [blue icon] **Procedural Due Process, Scope of Protection**

To pursue a due process claim in the courts based upon a denial of hospital staff privileges, those privileges must in fact be denied before the claim may be pursued in the courts.

Healthcare Law > Business Administration & Organization > Facility & Personnel Licensing > Personnel Licensing

## **HN71** [blue icon] **Facility & Personnel Licensing, Personnel Licensing**

See Utah Code Ann. § 58-70a-501(1) (2002).

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Healthcare Law > Business Administration & Organization > Facility & Personnel Licensing > Personnel Licensing

## [\*\*HN72\*\*](#) [+] Facility & Personnel Licensing, Personnel Licensing

See Utah Admin. Code r. 156-70a-501 (2004).

Healthcare Law > Business Administration & Organization > Facility & Personnel Licensing > Personnel Licensing

## [\*\*HN73\*\*](#) [+] Facility & Personnel Licensing, Personnel Licensing

While it is true that under [\*Utah Code Ann. § 58-70a-501\(1\)\*](#) (2002) and Utah Admin. Code r. 156-70a-501 (2004), a physician assistant may provide "any medical services" not specifically prohibited that are within the range of her skills and scope of competence and the skills and scope of practice of her supervising physician, she cannot lawfully exercise the identical degree of independent professional judgment and discretion that a physician could exercise, and logically she could not be entitled as a matter of constitutional right to exercise practice privileges at hospitals, clinics, and similar facilities identical to those that physicians may enjoy.

Constitutional Law > Substantive Due Process > Deprivation of Economic Interests

Healthcare Law > Business Administration & Organization > Facility & Personnel Licensing > Personnel Licensing

## [\*\*HN74\*\*](#) [+] Substantive Due Process, Deprivation of Economic Interests

Limiting a physician assistant's practice privileges to take into account the statutory and regulatory requirement of direct supervision and review by a physician cannot operate to deprive the physician assistant of "liberty" or "property" otherwise guaranteed by the [\*Fourteenth Amendment\*](#). Nor is it arbitrary or unreasonable for a health care facility to require that physician assistants exercise staff privileges under the supervision of a physician who currently has staff privileges at the same facility.

Contracts Law > Contract Interpretation > Good Faith & Fair Dealing

## [\*\*HN75\*\*](#) [+] Contract Interpretation, Good Faith & Fair Dealing

To determine the legal duty a contractual party has under the covenant of good faith and fair dealing, a court will assess whether a party's actions are consistent with the agreed common purpose and the justified expectations of the other party. The court determines the "purpose, intentions, and expectations" by considering the contract language and the course of dealings between and conduct of the parties.

Contracts Law > Contract Interpretation > Good Faith & Fair Dealing

## [\*\*HN76\*\*](#) [+] Contract Interpretation, Good Faith & Fair Dealing

Under Utah law, some general principles limit the scope of the covenant of good faith and fair dealing, including the following: First, this covenant cannot be read to establish new, independent rights or duties to which the parties did not agree ex ante. Second, this covenant cannot create rights and duties inconsistent with express contractual

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terms. Third, this covenant cannot compel a contractual party to exercise a contractual right to its own detriment for the purpose of benefitting another party to the contract. Finally, courts will not use this covenant to achieve an outcome in harmony with the court's sense of justice but inconsistent with the express terms of the applicable contract.

Contracts Law > Contract Interpretation > Good Faith & Fair Dealing

**HN77** [+] **Contract Interpretation, Good Faith & Fair Dealing**

Generally, the degree to which a party to a contract may invoke the protections of the covenant of good faith and fair dealing turns on the extent to which the contracting parties have defined their expectations and imposed limitations on contract terms. In all instances, however, the reach of the implied covenant of good faith and fair dealing extends no further than the purposes and express terms of the contract.

Contracts Law > Contract Interpretation > Good Faith & Fair Dealing

**HN78** [+] **Contract Interpretation, Good Faith & Fair Dealing**

The Utah Supreme Court takes the position that the ability of a plaintiff to recover in tort for breach of the implied covenant of good faith and fair dealing in a contract has the potential for distorting well-established principles of contract law and will not be permitted. Utah law thus does not recognize an independent tort cause of action based upon good faith and fair dealing apart from the purposes and terms of an existing contract, and in contrast to equitable doctrines such as unconscionability, the implied covenant cannot serve as a basis for invalidating a contract.

Healthcare Law > Medical Treatment > Patient Confidentiality > General Overview

**HN79** [+] **Medical Treatment, Patient Confidentiality**

In Utah, the maintenance and protection of the confidentiality of medical records involves the application of both legal and ethical standards.

Healthcare Law > Medical Treatment > Patient Confidentiality > General Overview

**HN80** [+] **Medical Treatment, Patient Confidentiality**

See Utah Admin. Code r. 156-67-602 (2005).

Healthcare Law > Medical Treatment > Patient Confidentiality > General Overview

**HN81** [+] **Medical Treatment, Patient Confidentiality**

See [Utah Code Ann. § 58-67-803\(1\)](#) (2002).

Torts > Intentional Torts > Intentional Infliction of Emotional Distress > Elements

## [\*\*HN82\*\*](#) [blue icon] **Intentional Infliction of Emotional Distress, Elements**

An action for severe emotional distress, though not accompanied by bodily impact or physical injury, may lie where the defendant intentionally engaged in some conduct toward the plaintiff, (a) with the purpose of inflicting emotional distress, or (b) where any reasonable person would have known that such would result; and his actions are of such a nature as to be considered outrageous and intolerable in that they offend against the generally accepted standards of decency and morality.

Torts > Intentional Torts > Intentional Infliction of Emotional Distress > Elements

## [\*\*HN83\*\*](#) [blue icon] **Intentional Infliction of Emotional Distress, Elements**

To prevail on her claim of intentional infliction of emotional distress, a plaintiff must prove that the defendants either intentionally or recklessly engaged in intolerable and outrageous conduct that caused her severe emotional distress.

Torts > Intentional Torts > Intentional Infliction of Emotional Distress > Elements

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > Elements

## [\*\*HN84\*\*](#) [blue icon] **Intentional Infliction of Emotional Distress, Elements**

Intentional infliction of emotional distress, in contrast to negligent infliction of emotional distress, does not require that plaintiff actually be at risk of bodily harm.

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > Potential Plaintiffs

## [\*\*HN85\*\*](#) [blue icon] **Negligent Infliction of Emotional Distress, Potential Plaintiffs**

The Utah Supreme Court expressly recognizes a cause of action for negligent infliction of emotional distress. It adopts the zone of danger approach, allows recovery to plaintiffs who suffer emotional distress because of another's negligence, though they do not suffer any physical impact, only if the plaintiffs are placed in actual physical peril and fear for their own safety. Therefore, this does not provide recovery to plaintiffs who are not within the zone of danger created by a defendant's negligence. The rule does not give protection to mental and emotional tranquility in itself. One who unintentionally but negligently subjects another to such emotional distress does not take the risk of any exceptional physical sensitiveness to emotion which the other may have unless the circumstances known to the actor should apprise him of it.

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > Potential Plaintiffs

## [\*\*HN86\*\*](#) [blue icon] **Negligent Infliction of Emotional Distress, Potential Plaintiffs**

One restriction that provides a check on feigned disturbances, thereby ensuring the genuineness of claims is the requirement that plaintiffs who claim to be the direct victim of negligent infliction of emotional distress must allege resulting illness or bodily harm, including clinically identifiable mental illness.

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > Potential Plaintiffs

### **HN87** Negligent Infliction of Emotional Distress, Potential Plaintiffs

If the actor unintentionally causes emotional distress to another, he is subject to liability to the other for resulting illness or bodily harm if the actor (a) should have realized that his conduct involved an unreasonable risk of causing the distress, otherwise than by knowledge of the harm or peril of a third person, and (b) from facts known to him should have realized that the distress, if it were caused, might result in illness or bodily harm. This rule has no application to illness or bodily harm of another which is caused by emotional distress arising solely from harm or peril to a third person, unless the negligence of the actor has otherwise created an unreasonable risk of bodily harm to the other.

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > Elements

### **HN88** Negligent Infliction of Emotional Distress, Elements

To sustain a claim of negligent infliction of emotional distress, the emotional distress suffered must be severe; it must be such that a reasonable person, normally constituted, would be unable to adequately cope with the mental stress engendered by the circumstances of the case.

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

Evidence > Burdens of Proof > Clear & Convincing Proof

Torts > Business Torts > Fraud & Misrepresentation > General Overview

### **HN89** Heightened Pleading Requirements, Fraud Claims

In order to prevail on a claim of fraud or misrepresentation, all the elements of fraud must be established by clear and convincing evidence. Under [Fed. R. Civ. P. 9\(b\)](#), those missing elements of reasonable reliance, causation, and injury are among the circumstances constituting fraud that must be pleaded with particularity. Absent such pleading, plaintiffs' fraud claim remains vulnerable to dismissal pursuant to [Fed. R. Civ. P. 9\(b\)](#), independent of a motion under [Fed. R. Civ. P. 12\(b\)\(6\)](#) or [56](#).

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

### **HN90** Heightened Pleading Requirements, Fraud Claims

In applying Utah's parallel civil rule, the mere recitation by a plaintiff of the elements of fraud in a complaint does not satisfy the particularity requirement. Rather, Utah R. Civ. P. 9(b) requires a complaint to recite the relevant surrounding facts with sufficient particularity to show what facts are claimed to constitute the fraud charges. [Rule 9\(b\)](#) also imposes a much more basic and fundamental requirement: a requirement of clarity and conciseness.

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > Fraud Claims

### **HN91** Heightened Pleading Requirements, Fraud Claims

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Pleading a fraud claim without specifying the facts upon which it is based essentially dumps upon the trial court the burden of sifting through the hundreds of paragraphs of alleged facts to ascertain whether plaintiffs have alleged facts necessary to make all their elements of fraud. Such an approach is unacceptable. It is plaintiffs' responsibility, not the courts, to set forth the relevant surrounding facts in such a manner that it is evident what facts are claimed to constitute the fraud charges.

Civil Procedure > Pretrial Matters > Conferences > Final Pretrial Conferences

### [HN92](#) [blue download icon] Conferences, Final Pretrial Conferences

See D. Utah Civ. R. 7-1(d).

Healthcare Law > Business Administration & Organization > General Overview

Healthcare Law > ... > Actions Against Facilities > Standards of Care > Hospitals

### [HN93](#) [blue download icon] Healthcare Law, Business Administration & Organization

Because the hospital bylaws constitute a contract between the hospital and the physician, the hospital must comply with those bylaws when taking actions which effect its staff. The weight of authority grants deference to hospital officials' professional judgment. Under this authority, courts require that a hospital only "substantially comply" with its bylaws. Substantial compliance with the bylaws adequately serves their primary purpose, which is to ensure fair procedures for staffing decisions.

Civil Procedure > Judgments > Entry of Judgments > General Overview

### [HN94](#) [blue download icon] Judgments, Entry of Judgments

See D. Utah Civ. R. 54-1.

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

### [HN95](#) [blue download icon] Complaints, Requirements for Complaint

The Federal Rules of Civil Procedure encourage litigants to plead only a simple statement, in sequence, of the events which have transpired, coupled with a direct claim by way of demand for judgment.

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Conforming Pleadings to Evidence

### [HN96](#) [blue download icon] Amendment of Pleadings, Conforming Pleadings to Evidence

While generally, motions to amend a complaint to conform to the evidence are made at trial or in the immediate aftermath of trial, the express language of [Fed. R. Civ. P. 15\(b\)](#) does not limit such motions to that context.

Civil Procedure > Judgments > Relief From Judgments > Altering & Amending Judgments

## [HN97](#) [blue icon] Relief From Judgments, Altering & Amending Judgments

Except to the extent that a motion under [Fed. R. Civ. P. 60\(b\)](#) or [Fed. R. Civ. P. 59\(e\)](#) is deemed a "motion for reconsideration," the Federal Rules do not expressly provide for such motions. Nevertheless, in the Tenth Circuit, a "motion for reconsideration" may be made on one or more specific grounds: Grounds warranting a motion to reconsider include (1) an intervening change in the controlling law, (2) new evidence previously unavailable, and (3) the need to correct clear error or prevent manifest injustice. Thus, a motion for reconsideration is appropriate where the court has misapprehended the facts, a party's position, or the controlling law.

Civil Procedure > ... > Relief From Judgments > Grounds for Relief from Final Judgment, Order or Proceeding > Extraordinary Circumstances

## [HN98](#) [blue icon] Grounds for Relief from Final Judgment, Order or Proceeding, Extraordinary Circumstances

Relief under [Fed. R. Civ. P. 60\(b\)](#) is extraordinary and may only be granted in exceptional circumstances.

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For Bradley Eddie, Terra Talker, Plaintiffs: Susan Rose, SANDY, UT.

**Judges:** BRUCE S. JENKINS, United States Senior District Judge.

**Opinion by:** BRUCE S. JENKINS

## **Opinion**

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**[\*1109] MEMORANDUM DECISION & ORDER**

**THE FINAL PRETRIAL CONFERENCE ([Fed. R. Civ. P. 16\(c\)](#))**

[Fed. R. Civ. P. 16\(c\)\(1\)](#)

### **THE PART I PLAINTIFFS**

**Dr. Steven MacArthur, M.D**

**Ms. Michele Lyman, P.A.**

**Ms. Helen Valdez**

### **THE PART I PLAINTIFFS' ALLEGATIONS AGAINST THE INDIVIDUAL DEFENDANTS**

**The County Commissioners**

**County Attorney Craig Halls**

**SJHSD Board Members: Atcity, Lewis, Housekeeper, Adams, Shumway & Holliday**

**The SJHSD Administrators: Wood, Bailey & Bradford**

**Laurie Schafer (a/k/a Laurie Shafer)**

**Marilee Bailey, R.N.**

**Ora Lee Black**

**Carla Grimshaw**

**Gloria Yanito**

**Julie Bronson**

**Lori Wallace, R.N. a/k/a Laurie Walker**

**Dr. Lloyd Val Jones, M.D.**

**Dr. Manfred Nelson, M.D.**

**Dr. James Redd, M.D.**

#### **THE PART I PLAINTIFFS' THEORIES OF LIABILITY**

**(1) Plaintiffs' Civil RICO Claims ([18 U.S.C. §§ 1961 et seq.](#))**

**Predicate Acts of "Racketeering Activity" ([18 U.S.C. § 1961\(1\)](#))**

**(a) [18 U.S.C. § 1341](#) - Mail Fraud**

**(b) [18 U.S.C. § 1512](#) - Witness Tampering**

**(c) [18 U.S.C. § 1951](#) - Interference with Commerce by Threats**

**(2) Freedom of Access to Clinic Entrances Act of 1994 ([18 U.S.C. § 248](#)) [\*\*5]**

**(3) Health Care Quality Improvement Act, [42 U.S.C. § 11112 \(2000\)](#)**

**(4) Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C. § 1395dd \(2000\)](#)**

**(5) "Medicare Patient [Bill of Rights](#)" ([42 U.S.C. § 1395a](#))**

**(6) [42 U.S.C. § 1981](#)**

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(7) [42 U.S.C. § 1985\(3\)](#)

(8) [42 U.S.C. § 1983](#)

[§ 1983 Conspiracy](#)

**Liability of the SJHSD & San Juan County**

**Plaintiffs' [§ 1983](#) Claims Against the County Commissioners & SJHSD Board Members**

**Vicarious Liability, Respondeat Superior & [§ 1983](#)**

**The SJHSD Board & the SJHSD Medical Staff's "Policy" re: Physician Assistants**

[\*1110] **Qualified Immunity & Plaintiffs' [§ 1983](#) Claims**

**Dr. MacArthur's [§ 1983](#) Claim**

**Dr. MacArthur's "Right" to Practice at SJHSD Facilities**

**Dr. MacArthur's Request for Privileges & Procedural Due Process**

**Ms. Lyman's [§ 1983](#) Claim**

**Substantive Due Process**

**Misogyny & "Hostile Environment" under [§ 1983](#)**

**Qualified Immunity & Ms. Lyman's [§ 1983](#) Claim**

**Ms. Helen Valdez' [§ 1983](#) Claim**

**(9) Federal Antitrust Laws ([15 U.S.C. §§ 1 et seq.](#))**

**The Local Government Antitrust Act ([15 U.S.C. §§ 34-36](#))**

**Dr. MacArthur's Federal [Antitrust Law](#) Claim**

**Ms. Lyman's Federal [Antitrust Law](#) Claim**

**(10) [Utah Constitution, art. I, §§ 1, 7, 25, 26, 27](#)**

**(11) Utah Unfair Practices Act ([Utah Code Ann. §§ 13-5-1 et seq.](#) [\*\*6] (2001))**

**(12) Utah Civil Rights Act ([Utah Code Ann. §§ 13-7-1 et seq.](#) (2001))**

**(13) Interference with Contract and with Prospective Business Relations**

**(14) "state common law defamation (also a U. S. Constitutional right to reputation as guaranteed by the [Ninth Amendment](#))"**

**(a) Utah Law of Defamation**

**(b) Defamation & the Ninth Amendment**

**(15) "Federal common law and Utah contract common law and statutory provisions that prohibit contracts of adhesion, bad faith, and lack of fair dealing. Utah Code Ann. 78-12-25(1) (1996)," including the Implied Covenant of Good Faith and Fair Dealing**

**(a) Contracts of Adhesion**

**(b) Implied Covenant of Good Faith and Fair Dealing**

**(16) "privacy rights and statutory entitlements to have their credential files and patient files accurately kept by the district under Medicaid and Utah Health Department statutes and regulations"**

**(17) Negligent and Intentional Infliction of Emotional Distress**

**(a) Intentional Infliction of Emotional Distress**

**(b) Negligent Infliction of Emotional Distress**

**(c) The Part I Plaintiffs' Emotional Distress Claims**

**(18) Fraud**

**Summary re: the Part I Plaintiffs' Causes of Action**

**Pretrial Determination of the Part I Plaintiffs' Claims**

**Claims [\*\*7] Against San Juan County and the SJHSD**

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**Summary re: the Final Pretrial Conference**

**PLAINTIFFS' MOTION FOR LEAVE TO FILE AN AMENDED COMPLAINT**

**THE PART I PLAINTIFFS' MOTIONS FOR RECONSIDERATION**

**CONCLUSION**

This case involves a potpourri of individual claims with individual histories and individual times and contexts, held together, if at all, by a common defendant, or common defendants. It has an erratic procedural history, complicated

by prolix pleadings and appendices, evolving arguments, and motions to reconsider matters already decided. In an effort to deal with this matter as completely as we can--extended though it may be--the court in the context of pretrial has considered in detail each of the plaintiffs' legal theories, and the factual allegations advanced as the basis for those theories, all in an effort to [\*1111] identify any genuine issues that would require a trial.

The original complaint filed in this action asserted claims by fifteen individual plaintiffs against San Juan County, the San Juan Health Services District, and various individual defendants. Some of those claims [\*\*8] were decided upon motion, and some have been resolved by agreement; several of the original plaintiffs and defendants are no longer parties to this case. ( See Order on Motions Heard on July 2, 2002, filed August 22, 2002 (dkt. no. 417); Order on Motion of Defendant San Juan Foundation to Dismiss, filed June 5, 2002 (dkt. no. 366); Order of Dismissal with Prejudice, filed March 28, 2002 (dkt. no. 309); Order of Dismissal with Prejudice, filed March 25, 2002 (dkt. no. 306); Order of Dismissal with Prejudice, filed March 11, 2002 (dkt. no. 298); Order, filed February 12, 2002 (dkt. no. 272); Order, filed November 29, 2001 (dkt. no. 234); see also Order, filed February 15, 2002 (dkt. no. 279).) Some of the questions decided by the district judge initially assigned this case became the subject of an interlocutory appeal, and are now back before this court on remand. See [MacArthur v. San Juan County, 309 F.3d 1216 \(10th Cir. 2002\)](#).

By the time of the Final Pretrial Conference on November 14-15, 2002, there remained six named plaintiffs, whose claims fall into two discrete groups: plaintiffs Donna Singer, Fred Riggs and Al Dickson, who seek enforcement of a judgment against several of the [\*\*9] defendants previously obtained in Navajo Tribal Court--the matter now before this court on remand from the court of appeals--and plaintiffs Dr. Steven MacArthur, Michelle Lyman and Helen Valdez, who assert individual claims against the defendants arising from various events and alleged acts of one or more of the defendants. The claims of these six remaining plaintiffs were detailed in a proposed Amended Complaint submitted by counsel a few days before the Final Pretrial Conference. ( See "Amended Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," annexed to "Plaintiffs' Rule 15 Motion to Amend and Supplement Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," and "Memorandum of Fact and Law in Support," filed November 6, 2002 (dkt. no. 438) (hereinafter "Proposed Amended Complaint").)<sup>1</sup> "Part I" of the Proposed Amended Complaint sets forth the claims of MacArthur, Lyman and Valdez (*id.* at 2-98 PP1-254); "Part II" of the same pleading spells out the relief sought by Singer, Riggs and Dickson. (*Id.* at 98-120.)

The claims and defenses involving the "Part I Plaintiffs," MacArthur, Lyman and Valdez, were also delineated in an agreed form of proposed Pretrial Order submitted six days later as contemplated by the court's local rules, see [DUCivR 16-I\(e\)](#), and by the schedule previously established by the court in this case.<sup>2</sup> ( See Proposed [\*1112] Pretrial Order, received November 12, 2002.<sup>3</sup> ) On the eve of pretrial, the San Juan Health District defendants filed motions to dismiss those plaintiffs' RICO, Health Care Quality Improvement Act and EMTALA claims (dkt. nos. 443, 445, 447), followed the next day by motions to dismiss those plaintiffs' claims of interference with commerce by threats, mail fraud, witness tampering and federal **antitrust law** violations (dkt. nos. 450, 452, 456, 454).

#### THE FINAL PRETRIAL CONFERENCE ([Fed. R. Civ. P. 16\(c\)](#))

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<sup>1</sup> As noted in a November 8, 2002 remark on the docket, the Proposed Amended Complaint was accompanied by a separate addendum [\*\*10] of "Pertinent Parts of the Navajo Court Record as Attachment to the Amended Complaint," received by the Clerk of the Court on November 8, 2002 and lodged in the case file.

<sup>2</sup> ( See Minute Entry, dated October 8, 2002 (dkt. no. 427).) At the request of plaintiffs' counsel, the dates for submission of the draft Pretrial Order (11/1/2002) and the Final Pretrial Conference (11/5/2002) were reset by amended notice of hearing, [\*\*11] with the conference to commence on November 12, then November 14. ( See Motion for a Short Extension of Time to Submit the Final Pretrial Order for Medical Reasons, filed October 28, 2002 (dkt. no. 434); Notice of Hearing, filed October 31, 2002 (dkt. no. 435); Motion to Extend Time for Pretrial Proceedings, filed November 8, 2002 (dkt. no. 439); Amended Notice of Hearing, filed November 12, 2002 (dkt. no. 441).)

<sup>3</sup> The Proposed Pretrial Order ultimately was neither signed by the court nor docketed and filed in this case. To ensure a complete record of the Final Pretrial Conference in this action, a copy of the Proposed Pretrial Order in .pdf file format is annexed to this Memorandum Decision & Order as an Appendix.

At the Final Pretrial Conference, court and counsel explored in some detail the factual footing and legal theories underlying the claims of the Part I plaintiffs, engaging in an extended colloquy that sought to identify, formulate and simplify the issues, and to pinpoint any genuine issues of material fact issues requiring a trial. [Fed. R. Civ. P. 16\(c\)\(1\)](#)

**HN1**[<sup>↑</sup>] At a pretrial conference, "consideration may be given, and the court [\*\*12] may take appropriate action, with respect to (1) the formulation and simplification of the issues, including the elimination of frivolous claims or defenses; . . ." [Fed. R. Civ. P. 16\(c\)\(1\)](#). **HN2**[<sup>↑</sup>]

The reference in [Rule 16\(c\)\(1\)](#) to "formulation" is intended to clarify and confirm the court's power to identify the litigable issues. It has been added in the hope of promoting efficiency and conserving judicial resources by identifying the real issues prior to trial, thereby saving time and expense for everyone.... The notion is emphasized by expressly authorizing the elimination of frivolous claims or defenses at a pretrial conference. There is no reason to require that this await a formal motion for summary judgment. Nor is there any reason for the court to wait for the parties to initiate the process called for in [Rule 16\(c\)\(1\)](#).

[Fed. R. Civ. P. 16](#) advisory committee note to 1983 amendment (citation omitted). "The court thus is directed to define the issues, facts, and theories actually in contention, which means that extraneous issues should be weeded out ...." 6A Charles A. Wright, Arthur R. Miller & Mary K. Kane, *Federal Practice and Procedure* § 1525, at 242 (2d ed. 1990) (footnotes omitted). [\*\*13] As the court of appeals explained some years ago: "The salutary, indeed the desirable and efficacious, purpose of a pretrial conference is to sift the discovered and discoverable facts to determine the triable issues, both factual and legal, and to chart the course of the lawsuit accordingly." [Lynch v. Call, 261 F.2d 130, 132 \(10th Cir. 1958\)](#).

It follows that **HN3**[<sup>↑</sup>] "as a case takes shape and the court struggles to narrow and pinpoint the issues, the parties have an unflagging obligation to spell out squarely and distinctly those claims they desire to advance at the trial proper. Good-faith compliance with Civil [Rule 16](#) plays an important role in this process." [Veranda Beach Club Limited Partnership v. Western Surety Co., 936 F.2d 1364, 1371 \(1st Cir. 1991\)](#) (citation omitted). [Rule 16\(c\)\(1\)](#) places upon counsel "a substantial responsibility for assisting the court in identifying the factual issues worthy of trial." [Fed. R. Civ. P. 16](#) advisory committee note to 1983 amendment; cf. [Erff v. MarkHon Industries, Inc., 781 F.2d 613, 617 \(7th Cir. 1986\)](#) [\*1113] ("Attorneys at a pre-trial conference must make a full and fair disclosure of their views as to what the real issues of the trial will be."); see [\\*\\*14](#) also [DUCivR 7-1\(d\)](#).<sup>4</sup>

**HN4**[<sup>↑</sup>] [Rule 16\(c\)](#) has confirmed the court's power to identify the litigable issues, and to eliminate frivolous claims or defenses without awaiting the making of a summary judgment or other motion by the parties. But at the same time, counsel bear a substantial responsibility in formulating the triable issues in that they must these issues for the court or they waive the right to have them tried.

3 James W. Moore, et al.; *Moore's Federal Practice* P16.11, at 16-49 (2d ed. Rev. 1994) (footnotes omitted).

Both the Proposed Amended Complaint (Part [\\*\\*15](#) I) and the Proposed Pretrial Order recite an extended litany of grievances against San Juan County, the San Juan Health Services District ("SJHSD") and various individual defendants, ranging from allegations of nepotism in the administration of the SJHSD and San Juan County

<sup>4</sup> [DUCivR 7-1\(d\)](#) reads:

(d) **HN5**[<sup>↑</sup>] **Final Pretrial Conference.** Trial counsel must attend the final pretrial conference with the court. Preparation for this final pretrial conference should proceed pursuant to [Fed. R. Civ. P. 16](#) and should include (i) preparation by plaintiffs counsel of a recommended pretrial order that is submitted to other counsel at least five (5) days prior to the final pretrial date, and (ii) preparation for resolution of unresolved issues in the case.

**HN6**[<sup>↑</sup>] Our local rules thus anticipate that trial counsel will be fully prepared to participate in the pretrial examination of the issues contemplated by [Fed. R. Civ. P. 16\(c\)](#).

government to an individual physician's ill-tempered use of derogatory language in referring to medical support staff and patients and his unavailability for specific patient emergencies. ( See Proposed Amended Complaint at 35 P58, 35 PP50-52, <sup>5</sup> 60 P146, 63 PP156-58, 64 P159, 66-67 PP163-164, 67-68 PP165-166; Proposed Pretrial Order at 21 P58, 21 PP 51-52, 43P146, 44-45 PP156-59, 46 PP163-164, 47-48 PP165-166.) Even so, the Proposed Amended Complaint represented a significant narrowing of the scope of plaintiffs' claims from that of the original complaint--a pleading that alleged a wide range of grievances involving the operation of San Juan County government and the SJHSD, <sup>6</sup> and sought the entry of sweeping declaratory judgments and writs of mandamus requiring, *inter alia*, a GAO <sup>7</sup> audit of federal funds expended in the county in [\*1114] the previous ten years, an IRS audit of payroll tax withholding, the convening of [\*\*16] a federal grand jury investigation, and the immediate seizure or sequestration of the defendant entities' financial records by the U.S. Marshal pending that investigation and the GAO and IRS audits. ( See Complaint, filed July 25, 2000 (dkt. no. 1), at 156 PP3, 5 (Prayer for Relief).)

**HN7** A grievance involving a governmental unit is still a grievance,<sup>8</sup> but a grievance may or may not be "a claim upon which relief can be granted" in a judicial proceeding. *Fed. R. Civ. P. 12(b)(6)*. In attempting to identify and define genuine issues for trial, court and counsel at pretrial undertook to parse the Part I Plaintiffs' allegations in search of viable legal claims. (See Transcript of Hearing, dated November 14, 2002 ("Tr. 11/14/02"), *passim*; Transcript of Hearing, dated November 15, 2002 ("Tr. 11/15/02"), *passim*.)

## THE PART I PLAINTIFFS

### [\*1115] Dr. Steven MacArthur, M.D.

Dr. Steven MacArthur, M.D. is a licensed physician specializing in obstetrics and gynecology. By 1999, he had been in practice in his specialty for about eighteen years (though not in active practice for at least the prior year <sup>9</sup> ). On or about December 9, 1999, Dr. MacArthur requested full provisional one-year privileges to practice medicine at health care facilities operated by the SJHSD, including the Blanding Urgent Care Center, Blanding Birthing Center, Monument Valley Clinic, Monticello Clinic and San Juan Hospital, the only hospital facility located in San Juan

<sup>5</sup> Part I of the Proposed Amended Complaint includes two series of paragraphs numbered 50 through 58 at pages 34 and 35, and a second sequence of paragraphs 125-168 at pages 54-69; the Proposed Pretrial Order incorporates two similar sequences at pages 20-21 and 38-48, reflective of the fact that counsel simply reiterated almost all of the allegations of Part I of the Proposed Amended Complaint as "Plaintiffs' Statement of Contested Issues of Fact" in Section 5 of the Proposed Pretrial Order.

In this Memorandum Decision & Order, for the sake of clarity, any citations to these numbered paragraphs in either document refer to both the page and paragraph number(s) of the reference.

<sup>6</sup> ( See, e.g., Complaint (Verified), filed July 25, 2000 (dkt. no. 1), at 141 P472 ("County Commissioners have laughed at Taxpayers who sought to have San Juan County Commissioners account for what they are spending [and] notice budget [\*\*17] items prior to meetings by at least 24 hours."); *id.* at 150-151 P 514 ("San Juan County has treated the taxpayers with disdain and disrespect and laughed at those taxpayers bringing to the County Commission's attention the statutory provisions the taxpayers believed the County was violating.").

<sup>7</sup> Apparently referring to the General Accounting Office (now the Government Accountability Office). See *What is GAO?*, at <http://www.gao.gov/about/what.html>.

<sup>8</sup> Cf. *U.S. Const., Amend. I* ("Congress shall make no law. . . abridging . . . the right of the people peaceably to assemble, and to petition the Government for a redress of grievances."). "The *First Amendment* . . . guarantees the [\*\*18] right to petition the Government for a redress of grievances." *White v. Lee*, 227 F.3d 1214, 1227 (9th Cir. 2000) (internal quotation marks omitted).

<sup>9</sup> Tr. 11/14/02, at 6:16-18 (Ms. Rose.).

County.<sup>10</sup> The SJHSD did not grant Dr. MacArthur full provisional one-year privileges within thirty days after his request, as contemplated by the SJHSD medical staff bylaws. Nor did it deny them.

Instead, SJHSD administrators (defendants Bradford and Dr. James Redd) granted him two-week "temporary" practice privileges allowing him to treat at least a limited number of patients at SJHSD facilities, and these "temporary" privileges were extended twice, through February 2, 2000.<sup>11</sup>

Dr. MacArthur exercised his "temporary" privileges in providing care to several patients at SJHSD facilities; he also participated with another physician in a delivery by caesarian section in November or December of 1999. In doing so, Dr. MacArthur alleges that he encountered problems involving the availability, quality and sterility of medical instruments and equipment, and some resistance--even antagonism--on the part of SJHSD nurses and support staff in treating his patients. He was further troubled by rumors that cast doubt upon his background, professional integrity and expertise, and a local newspaper report that his privileges had been "lifted" by the SJHSD, when in fact no formal determination of his request had yet been made.

On or about February 2, 2000, the SJHSD did not **[\*\*21]** further extend his "temporary" privileges, and had not yet acted on his requests for full provisional privileges. At that point, the delay as to full provisional privileges was explained on the basis that required documentation was missing from his application packet (*viz.*, a copy of his medical license and DEA dispensing license), documentation which he believed had been furnished and in any event was readily available and easily verified.

By February of 2000, Dr. MacArthur had become apprehensive that his request for full provisional privileges may ultimately be denied, albeit for questionable, perhaps even pretextual reasons, and that his "temporary" privileges would soon expire and might not be further extended. He did not press the privileges issue with the SJHSD on or after February 2, 2000. Dr. MacArthur decided to move his medical practice to Ely, Nevada, and did not further pursue his request for full provisional practice privileges at the SJHSD facilities. ( See Proposed Pretrial Order at 37 P199.)

Dr. MacArthur now contends that his requests for full provisional one-year privileges were deferred in violation of his constitutional right as a licensed physician to pursue **[\*\*22]** his profession through use of publicly-sponsored medical facilities, and for pretextual reasons (*viz.*, "missing" documents), the real reasons being (1) discriminatory intent based upon his age (over 40), his associations with Ms. Lyman (gender), and Jewish and Mexican-American physicians (Drs. Penn and Mena), and his reporting of remarks concerning Dr. Penn; and (2) the intent to limit his competition with other SJHSD medical staff and contract physicians, none of whom are OB/GYN specialists, in serving the needs of women patients in San Juan County. He seeks an award of "damages in excess of \$ 3.5 million dollars and attorney fees" to compensate him for the loss of income anticipated from an estimated ten years' practice in the San Juan County market, resulting from the failure of the SJHSD defendants to grant him full provisional privileges as he requested, and the conduct of those individuals who propagated rumors spreading

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<sup>10</sup> The next nearest hospital facility to San Juan Hospital in Monticello, Utah is about 65 miles away to the north (Moab) or the east (Cortez, Colorado), and about 85 miles from Blanding. Shiprock **[\*\*19]** Hospital in Shiprock, New Mexico, is between 65 to 85 miles from southern San Juan County. ( SeeProposed Pretrial Order at 19 P39.)

<sup>11</sup> On December 23, 1999, Dr. MacArthur was informed by Cleal Bradford of the SJHSD that he had been granted "temporary" privileges, which would last from December 23 through January 5, 2000, while his request for full provisional privileges was being considered. According to the defendants, when Dr. MacArthur first discussed his "temporary" privileges with Mr. Bradford, Bradford asked Dr. MacArthur to specify the number of patients that Dr. MacArthur thought he would treat during the temporary privilege period. When Dr. MacArthur indicated that it would be difficult to estimate exactly, Bradford told MacArthur to increase his estimate to cover any potential but unplanned patients. Defendants insist that Dr. MacArthur's "temporary privileges" did not carry any limitation **[\*\*20]** on the actual number of patients that Dr. MacArthur could see during the "temporary" privileges period--but the same may not be true of the number of patients he could treat at SJHSD facilities. On January 10, 2000, Dr. MacArthur's "temporary" privileges were extended from January 5, 2000, through January 25, 2000. On January 26, 2000, Dr. MacArthur was again granted an extension through February 2, 2000.

defamatory falsehoods concerning his background, integrity or professionalism. (Proposed Amended Complaint at 94-95.)

### **Ms. Michele Lyman, P.A.**

Plaintiff Michele Lyman resides in Blanding, Utah, and has been practicing as a licensed Physician's Assistant since [\*\*23] 1996. She initially worked for the SJHSD at Montezuma Creek in 1995, completing her preceptorship under the supervision of Dr. Lloyd Val Jones, M.D. in 1996. She then became employed by and practiced under the supervision of Dr. James Redd, M.D., who was in private practice in Blanding; [\*1116] she continued to be supervised by Dr. Jones as a "back-up" as well. While working for Dr. Redd, Ms. Lyman regularly covered Dr. Redd's clinic, and providing some coverage for the Blanding nursing home, the Blanding Birthing Center, the San Juan Hospital emergency room, and the Blanding Urgent Care Center, a SJHSD facility where she alleges she enjoyed full SJHSD medical staff privileges,<sup>12</sup> and was paid by the District for her "on-call" services. ( See Proposed Pretrial Order at 29 P132; Tr. 11/15/02, at 3:4-5:13 (Ms. Rose).) Ms. Lyman ceased working under Dr. Redd's supervision on or about October 7, 1998, but continued providing coverage for the SJHSD through November, 1998. She alleges that she was effectively denied her staff privileges at the Blanding Urgent Care Center within three days after leaving Dr. Redd, and thereafter experienced considerable difficulty in exercising her privileges at [\*\*24] SJHSD facilities, even though she was working in Monticello under the supervision of two other Monticello physicians having SJHSD staff privileges, *viz.*, Dr. Nathaniel Penn, M.D. from November 1998 until July 1999 (when Dr. Penn had moved his practice to Moab),<sup>13</sup> and Dr. Robert Mena, M.D., from July to November 1999 (when Dr. Mena's SJHSD privileges expired). In early 1999, Ms. Lyman and Dr. Penn opened a Blanding Family Practice clinic; Ms. Lyman eventually purchased that clinic from Dr. Penn and operated as a "state-approved off-site

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<sup>12</sup> While working under the supervision of Drs. Redd and Jones at the Blanding Urgent Care Center, plaintiffs allege that "Mrs. Lyman did the following patient procedures:

- a) Took care of acute head trauma's; and,
  - b) Put in chest tubes; and,
  - c) Delivered a couple of babies; and,
  - d) Sutured cuts; and,
  - e) Dealt with heart attacks; and,
  - f) Informed families of tragedies; and,
  - g) Ordered tests; and,
  - h) Prescribed medications and shots; and,
  - i) Prescribed tests to be run on the patients; and,
  - j) Admitted and discharged patients; and,
  - k) Consulted [\*\*25] other specialists by phone; and,
  - l) Treated patients with infectious diseases; and,
  - m) Referred patients to the San Juan Hospital and to the other district facilities,
- all without a Dr. at her side and without on site supervision, and with no Dr. even in town available for assistance.

(Proposed Amended Complaint at 55-57 P129.) However, plaintiffs then allege that "Mrs. Lyman and Dr. Key, before he left, informed Dr. Redd and Dr. Jones that this practice of leaving Mrs. Lyman without either Dr. on call was wrong, and that the practice should be changed," (*id.* at 57 P130), and now characterize that practice as a "Violation of Medical ByLaws and State laws and regs." ( *Id.* at 57.)

<sup>13</sup> ( SeeProposed Amended Complaint at 76 P203 (In "April, 1999, after working in Monticello under Dr. Penn, Ms. Lyman began a new practice *in Blanding*under the off-site direction of Dr. Nathaniel Penn."); Proposed Pretrial Order at 52 P203 (same).)

"independent rural clinic" for three years, until she in turn sold her practice. (Proposed Amended Complaint at 14, 96.)

In December 1999, Ms. Lyman requested a renewal of her SJHSD staff privileges (to be exercised under supervision by Dr. MacArthur), which request was delayed, purportedly because of "missing" documentation in her personnel file, e.g., CPR certification cards, that [\*\*26] Ms. Lyman is certain had been properly issued and were current through at least December of 1999. She furnished copies of the missing cards, but alleges that the dates on those cards had been altered.

By the end of March, 2000, formal administrative action on her request for privileges was still being deferred by the SJHSD until the CPR certification card issue was resolved. According to the [\*1117] pleadings, from November 1999 until sometime in 2001, Ms. Lyman may not have had a supervising physician practicing in San Juan County who had staff privileges with the SJHSD, except for the brief period between December 23, 1999 and February 2, 2000, when Dr. MacArthur exercised "temporary" SJHSD privileges.<sup>14</sup> At the time of pretrial, she was again being supervised by Dr. Jones. ( See Tr. 11/15/02, at 24:9-25, 26:7-11 (Ms. Rose).)

According to the plaintiffs,

The District employees as a pattern sought to restrain competition, there was inadequate impartiality in 'peer review' or in issuing privileges since the people issuing the privileges are usually in economic competition with those they are giving privileges. Privileges for Mrs. Lyman were de facto denied by nursing personnel and medical staff without any action by the District governance board.

(Proposed Pretrial Order at 14.) As Ms. Lyman's counsel explained at pretrial,

She's complaining that she could not get the privileges at the hospital when she was working under physicians that had privileges. Her patients she would send over to the clinic, they would not get shots. At one point she was told she couldn't order labs or x-rays. At one point she was told she couldn't set foot in the facility.

(Tr. 11/15/02, at 14-19 (Ms. Rose).)

In addition to the alleged interference with her practice privileges at SJHSD facilities after October 1998, Ms. Lyman alleges harassment and intimidation of, and denial of health care services to her patients by Dr. Redd and other SJHSD support staff, which [\*\*28] she contends was intended to inhibit competition by her with the SJHSD medical staff and contract providers. She also alleges a deliberate campaign of harassment conducted against her by Dr. Redd since she ceased working for him in October of 1998, intended to hinder and frustrate her professional practice, and cause her severe emotional distress. She contends that Dr. Redd created a misogynistic "hostile environment" in his own medical office in Blanding during the time that she worked under his supervision, and that her personal and professional reputation has suffered as a consequence of defamatory rumors, insinuations and accusations published to her patients and others by one or more of the defendants.

Ms. Lyman seeks an award of "damages in excess of Six (6) Million Dollars" as compensation for "unfair practices" interfering with the exercise of her practice privileges and he relationship with her patients, the harassment and intimidation of her patients, "the terrorism of her children, and herself, and the spreading of rumors that equate to nothing less than criminal defamation for both Michele Lyman and Dr. MacArthur." (Proposed Amended Complaint at 96-98.) She also seeks injunctive [\*\*29] relief "to protect patients of Mrs. Lyman and her supervising physician, and give Mrs. Lyman's patients uniform and considerate care with District staff sensitive to the unique needs of the patient," and allowing Ms. Lyman "to minimally go into any facility to at least speak [\*1118] and associate with her patient, regardless of whether she has privileges at the District." According to plaintiff, "ordering the [SJHSD] governance board to make physicians and chiefs of staff accountable for patient complaints and treat all medical providers and physician's equally and uniformly is not contradictory to good public policy." ( *Id.* at 93-94.)

<sup>14</sup> At pretrial, however, counsel insisted Drs. Penn and Mena continued to supervise Ms. Lyman at a distance even after Dr. MacArthur left for Nevada--concededly doing do at that point without SJHSD privileges--and that when Drs. Penn and Mena no longer supervised her, Ms. Lyman "went to work under Dr. Jones," and therefore "there was never a time that she wasn't without [\*\*27] a supervising physician." (Tr. 11/15/02, at 25:1-26:11 (Ms. Rose).)

**Ms. Helen Valdez**

The claims of plaintiff Helen Valdez arise out of a single event that took place on April 14, 1999. On that date, Ms. Valdez, accompanied by her sister-in-law, Charlene Gonzales, went to the San Juan Hospital emergency room at about 8:08 a.m. At that time, she was suffering from what was subsequently diagnosed as acute diverticulitis; she was experiencing symptoms including vomiting, cramping, diarrhea and pain, and felt very weak and tired. Ms. Valdez told the emergency room personnel "that she'd been sick, [and] needed to see a doctor." <sup>15</sup> **\*\*30** She assisted in filling out a typed patient admittance form, furnishing identification and health insurance information to an emergency room clerk named Judy Kascheaiveaz. She signed the form, as did the clerk. At that point, Ms. Valdez had not described her symptoms to the clerk. <sup>16</sup> Ms. Valdez became ill and went to the lavatory, and when she returned, she observed a nurse in the emergency room, Lori Wallace, R.N., tell the clerk that "she could set both her patients up in the emergency room for the physician," referring to Ms. Valdez and Michael Bailey, another individual who had come to the emergency room with an injured foot. <sup>17</sup>

While Ms. Valdez went to the lavatory a second time, her sister-in-law, Ms. Gonzales, says that she overheard the nurse, Ms. Wallace, tell the clerk to "tell Helen [Ms. Valdez] to go to the doctor's **\*\*31** office. Dr. Penn's office would open at 9:00." <sup>18</sup> Ms. Gonzales did not hear Ms. Wallace say anything else, and did not converse directly with Ms. Wallace about what she had overheard. <sup>19</sup>

Ms. Gonzalez related the overheard conversation to Ms. Valdez upon her return from the lavatory, and without any further conversation with Ms. Wallace, Ms. Kascheaiveaz, or other emergency room employees, Ms. Valdez left the emergency room, again accompanied by Ms. Gonzales. Instead of going to see her doctor at his office, Ms. Valdez went home. <sup>20</sup> At the time she left the emergency room, Ms. Valdez had not discussed her symptoms with Ms. Wallace or Ms. Kascheaiveaz, whom she had seen in the emergency room, <sup>21</sup> and had not yet seen or been examined by a physician.

**[\*1119]** Her symptoms subsided for a day but then intensified, and three days later, Ms. Valdez went to the Blanding Urgent Care Clinic, where she was examined by Dr. James Redd, M.D. Dr. Redd diagnosed her condition as acute diverticulitis, for which he prescribed oral antibiotics and a strict liquid diet. <sup>22</sup>

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<sup>15</sup> (Deposition of Charleen Gonzales, dated January 7, 2002, at 12:22-25.)

<sup>16</sup> (Deposition of Helen Valdez, dated December 6, 2001, at 18:11-22.)

<sup>17</sup> (*Id.* at 17:3-18:10.) At that point, according to Ms. Valdez, she had not spoken with Ms. Wallace and did not know whether or not the nurse "knew anything about [her] symptoms or what was wrong." (*Id.* at 18:11-22.)

<sup>18</sup> (Deposition of Charlene Gonzales, dated January 7, 2002, at 14:7-17, 20:13-24.)

<sup>19</sup> (*Id.*)

<sup>20</sup> Ms. Valdez testified in deposition that she believes Dr. Penn was already at the San Juan Hospital on the morning of April 14th, and that Mr. Bailey, the other emergency room patient at that time, subsequently told her he was examined by Dr. Penn in the emergency room about five minutes after Ms. Valdez had left. (Deposition of Helen Valdez, dated December **\*\*32** 6, 2001, at 19:15-20:18.)

<sup>21</sup> Ms. Valdez telephoned the emergency room before going there on the morning of April 14th, and briefly discussed her symptoms with a nurse, someone other than Ms. Wallace. (*Id.* at 18:14-17.)

<sup>22</sup> After leaving the San Juan Hospital emergency room on April 14th, Ms. Valdez did not attempt to contact her physician, Dr. Penn, because she believed he was out of town that weekend. (*Id.* at 26:15-22.) Nor did she try to contact Dr. Penn when her symptoms worsened after seeing Dr. Redd because she did not want to be admitted to San Juan Hospital for treatment. She chose to go to Cortez, Colorado instead. (*Id.* at 35:4-21.)

Ms. Valdez' condition did not improve significantly, and two days later she went to Cortez, Colorado, where she was hospitalized and placed on IV fluids and antibiotics. After receiving treatment in the Cortez hospital for several days, Ms. Valdez **[\*\*33]** returned home. Within a few days, she became ill again, and this time was admitted to the University of Utah Hospital, where she was diagnosed as having an obstruction requiring immediate surgery. She underwent surgery, which apparently was successful.

To compensate for "the badge of inferiority she was made to wear as she left the facility she had sought help from, not being able to see the provider of her choice, [and] not being able to feel as though she could return to a facility in Monticello for fear of Laurie Wallace," Ms. Valdez seeks an award of "damages of \$ 350,000 and attorneys fees." (Proposed Amended Complaint at 92-93.)

## **THE PART I PLAINTIFFS' ALLEGATIONS AGAINST THE INDIVIDUAL DEFENDANTS**

Besides the SJHSD and its parent entity, San Juan County,<sup>23</sup> the Part I Plaintiffs have named several individual defendants, originally and in the Proposed Amended Complaint: Commissioner Tyron Lewis, Commissioner Bill Redd, Craig Halls, Reid Wood, Cleal Bradford, Roger Atcity, John Lewis, John Housekeeper, Karen Adams, Patsy Shumway, Dr. James Redd, Dr. Lloyd Val Jones, Dr. Manfred Nelson, Richard Bailey, Marilee Bailey, Ora Lee Black, Gary Holliday, Laurie Schafer a/k/a "Laurie Shafer," **[\*\*34]**<sup>24</sup> Lori Wallace a/k/a "Laurie Walker,"<sup>25</sup> Carla Grimshaw, Gloria Yanito, and Julie Bronson.

### **[\*1120] The County Commissioners**

By the time of pretrial, two San Juan County Commissioners remained as defendants in this action in their individual capacities: Bill Redd and Ty Lewis. Both apparently were also named as defendants for their conduct as SJHSD Board members.<sup>26</sup> Plaintiffs allege very few specific facts concerning Commissioners Redd or Lewis individually;<sup>27</sup> instead, their allegations are pleaded against the *Commission* or the *County*:

<sup>23</sup> [HN8](#) San Juan County is organized as a political subdivision of the State of Utah under the Utah Constitution and [Utah Code Ann. §§ 17-50-101 et seq.](#) (2001). The SJHSD is organized as a special service district under the Utah Code Ann. § 17A-2-1301 et seq. (2004), and is funded in part through tax revenues. San Juan County appoints the members of the SJHSD governance board. See Utah Code Ann. § 17A-2-1326 (2001).

<sup>24</sup> Ms. Schafer was omitted from the caption of the original Complaint and apparently was added by a document entitled "Amendments to the Complaint Corrections of Errors," filed August 1, 2000 (dkt. no. 3). See [Fed. R. Civ. P. 15\(a\)](#) ("A party may amend the party's pleading once as a matter of course at any time before a responsive pleading is served ...."). She was again omitted from the captions of both the Proposed Amended Complaint and the Proposed Pretrial Order, in each instance without explanation. Nevertheless, she appears to have been included among the defendants represented by Mr. Harrison in preparation of the Proposed Pretrial Order.

<sup>25</sup> The captions of the original Complaint, the **[\*\*35]** Proposed Amended Complaint and the Proposed Pretrial Order refer to a defendant named "Laurie Walker"--in reality, Lori Wallace, R.N., a former SJHSD employee who was working in the San Juan Hospital emergency room on April 14, 1999 when plaintiff Helen Valdez was there seeking treatment. ( See Answer to Complaint by Laurie Walker (Lori Wallace), filed September 25, 2000 (dkt. no. 46) (name correction noted on docket).)

<sup>26</sup> Commissioner Redd was a member of the SJHSD Board for a brief period in late 1998 and early 1999, and Commissioner Lewis was a member from late 1998 to mid-1999. (Proposed Pretrial Order at 67 P2.)

<sup>27</sup> "County Commissioner Ty Lewis made the statement and determination in a public meeting that the County would drive out qualified private competitors," (Proposed Pretrial Order at 29 P135); "in **[\*\*37]** areas of health care, Commissioner Ty Lewis is against a private entity that would or will compete with the District." ( *Id.* at 20 P50; Proposed Amended Complaint at 34 P50 (same)).

106. The County Commission and District Board, by not policing and supervising the medical staff and leaving carte blanche decisions on who gets on staff and does not get on staff, contributes directly to the private use of the staff's use of the governmental processes.

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110. The lack of the District Board or County Commission [\*\*36] in taking action to supercede medical staff and head of medical staff privilege-granting decisions, and deliberate indifference to investigating complaints, holding hearings, and exercising their government authority to foster economic competition as mandated by statutes, falls outside any 'political' action, and directly is intended to control the business processes of competitors of District employee physicians and P.A.s and those medical staff physicians directly contracting with the District.

(Proposed Amended Complaint at 42-43 PP106, 110; Proposed Pretrial Order at 31 PP146, 150 (same). See Proposed Amended Complaint at 34 P52 ("The County and District had a de facto policy of deliberate indifference to those who complained of suffering from Dr. Redd and other District staff members.").)

### **County Attorney Craig Halls**

As to San Juan County Attorney Craig Halls, the Part I Plaintiffs note that he "is the brother in law of Rick Bailey, District CEO and County Commission administrator." (Proposed Pretrial Order at 21 § 51.)<sup>28</sup> With respect to certain administrative problems at the San Juan Hospital identified by the Utah Department of Health at or about the time of the event complained of by Ms. Valdez, plaintiffs state that "the Health District and County Commissioners were informed of these problems in a Board meeting, with an executive session attended by Commissioner Bill Redd and County Attorney Craig Halls." (*Id.* at 60 P236; Proposed Amended Complaint at 87 P236 (same).) More generally, the Part I Plaintiffs allege that the County Commissioners, County Administrator and County Attorney "behaved in a deliberately indifferent manner, failed to adequately investigate the problems Mrs. Lyman and Dr. MacArthur identified in the District, did not hold hearings [\*1121] on the matters, did not enforce, [\*\*38] or take any actions to rectify the situations identified by Mrs. Lyman and Dr. MacArthur." (Proposed Amended Complaint at 16-17.) "A pattern of deliberated indifference as a policy was exhibited by the County Commission, County Attorney, Health District board, administrators and medical staff." (*Id.* at 17.)

### **SJHSD Board Members: Atcity, Lewis, Housekeeper, Adams, Shumway & Holliday**

Defendants Roger Atcity, John Lewis, John Housekeeper, Karen Adams, Patsy Shumway and Gary Holliday are or at relevant times were members of the Board of Trustees of the San Juan Health Services District. (Proposed Pretrial Order at 67 P3.) Defendant Cleal Bradford was also a member of the SJHSD Board from approximately February 1999 until June 1999, and from approximately June 22, 1999 until April 2001, Bradford served as executive director of the SJHSD. (*Id.*)

In the Proposed Amended Complaint, the Part [\*\*39] I Plaintiffs plead very few factual allegations involving specific SJHSD Board members.<sup>29</sup> The Proposed Amended Complaint alleges nothing regarding intentionally

<sup>28</sup> Plaintiffs assert that "Cleat Bradford and James Redd had access to District board members and County Commissioners and the County Attorney as relatives and close friends, in a highly rural and isolated area," whereas plaintiffs MacArthur and Lyman did not. (Proposed Pretrial Order at 32 PP151-152.)

<sup>29</sup> Plaintiffs allege that

223. [On] December 21, 1999 Ms. Lyman Attended San Juan Health Care Services board Meeting to discuss and attempt to resolve her problems with SJHSD staff with the SJHSD board. She requested to have a public meeting so the public could fully understand the issues involved in the health care system their tax dollars support.

224. SJHSD governance board chairman Roger Atcity stated that he and SJHSD Patsy Shumway and SJHSD Karen Adams had discussed the situation before the official meeting and had decided that the grievance meeting with SJHSD

discriminatory acts or other culpable individual conduct of defendants Atcity, Shumway, Housekeeper,<sup>30</sup> John Lewis, and Adams. Other than noting his status as a SJHSD Board member, the Proposed Amended Complaint says nothing at all about defendant Gary Holliday.

Rather than addressing alleged conduct of individual Board members, the Plaintiffs appear to be complaining of alleged *inaction* by the Board as a *Board*: "The governance [\*1122] board displayed a pattern of not holding doctors or others accountable for interfering in doctor/patient relations. The County was aware of the problems and did nothing to investigate, hold hearings, or resolve the provider and patients' and public's concerns as evidenced in petitions with hundreds of signatures." (Proposed Pretrial Order at 14; see *id.* at 31 P149 ("District Board members and CEOs stated they entrusted medical staff privileging to the medical staff or head of medical staff.").) In plaintiffs' view:

The District has illegally operated the district by having County Commissioners as board members, by not holding doctors accountable for violations of the law, by not following their own medical by-laws, by not applying policies [\*\*42] equally across the board to all persons, by not overriding letters or memos of doctors that set policy, without board approval, while stifling economic competition in the area.

(*Id.* at 74.)

### **The SJHSD Administrators: Wood, Bailey & Bradford**

Like their allegations against the SJHSD Board members, plaintiffs' claims against SJHSD administrators Wood, Bailey and Bradford are largely footed upon allegations of *inaction* in response to plaintiffs' grievances:

- 109. Reid Wood and Rick Bailey did nothing to assist Mrs. Lyman in exercising privileges with the District that the District Board never officially and formally terminated.
- 110. Reid Wood, Cleal Bradford, and Rick Bailey as CEOs never held the medical Staff chiefs accountable for policies effecting services of P.A.s, whether written or de facto.
- 111. Reid Wood, Cleal Bradford, and Rick Bailey as CEOs never contradicted the medical Staff chiefs for policies effecting services of Michele Lyman, whether written or de facto.

governance board would be private. Such a decision being made before the meeting and without public input appears to be in violation of Utah's Open Meeting law. (cmplt. # 162-168).

(Proposed Amended Complaint [\*\*40] at 83-84 PP223-224; see Proposed Pretrial Order at 57 P223-224 (same).)

John Housekeeper did do some investigation for Mrs. Lyman, but labeled Dr. MacArthur a troublemaker because Dr. MacArthur was perceived by him to be associated with his current counsel in a lawyer/client relationship when Dr. MacArthur appeared at the District Board meeting in December, 1999.

(*Id.* at 22.)

Mrs. Valdez, Dr. MacArthur, Mrs. Lyman informed the District of their problems and to no avail. Dr. MacArthur and others reporting problems to Board member Patsy Shumway and John Housekeeper were labeled either troublemakers or Dr. Redd detractors.

(Proposed Pretrial Order at 14.)

The Defendant community leaders Rick Bailey, Ty Lewis, John Lewis, Karen Adams, Cleal Bradford, with the power and authority over the entire district, did nothing to investigate, find and hold accountable the responsible parties, and carried out a state identified de facto policy that diminished the standard of care for the patients.

(*Id.* at 27 P112(b).)

<sup>30</sup> Concerning Mr. Housekeeper, the Proposed Amended Complaint alleges that Ms. Lyman "suffered from Dr. Redd driving by her home honking his horn," and relates that "the horn honking [\*\*41] subsided notably when John Housekeeper was notified as board member that it was going on and was asked to tell Dr. Redd to stop the honking." (Proposed Amended Complaint at 17, 22-23.) Plainly this scenario would not serve as a basis for any liability on the part of Mr. Housekeeper.

112. ....

b. The Defendant community leaders Rick Bailey, Ty Lewis, John Lewis, Karen Adams, Cleal Bradford, with the power and authority over the entire district, did nothing to investigate, find and hold accountable the [\*\*43] responsible parties, and carried out a state identified de facto policy that diminished the standard of care for the patients.

\*\*\*\*

126. CEO's Cleal Bradford, Reid Wood, and Rick Bailey did nothing to help these doctors [MacArthur, Penn & Mena] have improved working conditions within the district, or renew their licenses or privileges. All three doctors were not employees of the District when supervising Mrs. Lyman.

\*\*\*\*

188. Reid Wood and all other CEO'S in this complaint, ignored Mrs. Lyman's attempts to rectify her situation, or exacerbated it.

\*\*\*\*

190. December 10, 1998 - Mrs. Lyman called SJHSD administrator Reid Wood twice to see if she could resolve some of the issues she was having with the nurses at the hospital since joining Dr. Penn and to resolve some of the problems with the clinic. Reid Wood did not return her calls. The third Mrs. Lyman called she was told by Carla Grimshaw that he was out of the office.

(Proposed Pretrial Order at 26-28 PP109-111, 112(b), 126; *id.* at 49 P188, 50 P190; see Proposed Amended Complaint at 71-72 PP188, 190 (same).)

[\*1123] As for Mr. Bradford, the plaintiffs describe the process by which he granted temporary practice privileges to Dr. MacArthur, [\*\*44] (Proposed Pretrial Order at 25-26 PP98-101, 104-105), and then assert that "CEO Cleal Bradford made the determination in granting Dr. MacArthur limited temporary privileges that it was best for the District if referrals to the District facilities came from District doctors. Dr. MacArthur was not employed by the District." ( *Id.* at 29 P134.)<sup>31</sup> Finally, plaintiffs assert:

151. Cleal Bradford and James Redd had access to District board members and County Commissioners and the County Attorney as relatives and close friends, in a highly rural and isolated area.

152. Dr. MacArthur and Michele Lyman did not have this familial and close friend relationship with Commissioners and District Board members.

153. Cleal Bradford who signed off on privileges as the District CEO lobbied the Board and County Commission, and medical staff, in meetings with a plurality of the decision-making body, without Mrs. Lyman or Dr. MacArthur being present.

( *Id.* at 32 PP151-153; see Proposed Amended Complaint at 44 PP111-113 (same).)

What conceivable cause of action the latter allegations would pertain to is not readily apparent. The balance of the allegations against Wood, Bailey and Bradford assert a failure to take affirmative steps to investigate and remedy plaintiffs' grievances involving members of the SJHSD medical and support staff, similar to plaintiffs' claim against the individual SJHSD Board members.

#### **Laurie Schafer (a/k/a Laurie Shafer)**

Laurie Schafer served at relevant times as Patient Care Director for the SJHSD. Plaintiffs allege: (1) that "Dr. MacArthur had an incident report allegedly filed against him by Marilee Bailey, Julie, Bronson, Laurie Shafer, Cleal Bradford that was never discussed with him or placed in his District file, and is a report that he considers to be untrue." (Proposed Pretrial Order at 25 P96); (2) that "Mrs. Shafer noticed the dates [on Ms. Lyman's CPR cards]

<sup>31</sup> Plaintiffs also allege that "Dr. MacArthur had an incident report allegedly filed against him by Marilee Bailey, Julie Bronson, Laurie Shafer, Cleal Bradford that was never discussed [\*\*45] with him or placed in his District file, and is a report that he considers to be untrue." (Proposed Amended Complaint at 39 P88; Proposed Pretrial Order at 25 P96 (same).)

were in error in medical staff meeting," that "the Medical staff and Cleal Bradford and Laurie Shafer discussed Mrs. Lyman's CPR card problems of wrong [\*\*46] dates without Mrs. Lyman being present," that "Mrs. Lyman's CPR cards were reviewed and found to be appropriate on more than one occasion by Carla Grimshaw and Laurie Shafer," and that "the medical staff and Cleal Bradford and Laurie Shafer unanimously decided to publish the altered cards to the American Heart Association by vote of the medical staff, who was considering privileges for Mrs. Lyman, without Mrs. Lyman being present." ( *Id.* at 32 P164-165, 34 P174); (3) "The medical staff, Cleal Bradford, Laurie Shafer, Carla Grimshaw failed to notify Dr. MacArthur of any missing documents in his application packet." ( *Id.* at 35 P182); (4) "After, Dr. MacArthur missed this February 2000 meeting, Cleal Bradford, Laurie Shafer, Dr. Redd met with San Juan Record editor Bill Boyle and discussed Dr. MacArthur's privileges with Mr. Boyle. Dr. MacArthur's privileges was private information." ( *Id.* at 36 P195); (5) "Mrs. Lyman was told that her friendship with Laurie Shafer would be over as she knew it if Mrs. Lyman associated herself with Dr. Penn." ( *Id.* at 47 P137; and (5) on one recent occasion when Ms. Lyman was treating a patient at the Blanding Birthing Center under Dr. Jones' supervision, [\*\*47] Ms. Shafer allegedly told "Mrs. Lyman and another nurse of Dr. Jones that they would have to leave. Mrs. Lyman and the nurse finished caring for the patient." ( *Id.* at 63 P254). Further, they allege that on December 16, 1998, Ms. Lyman was told she did not have SJHSD privileges and that SJHSD staff were not to take orders from her. "Ms. Lyman asked Ms. Yanito who gave her this order and she stated that Laurie Schafer and Dr. Redd," ( *id.* at 48-49 P 170), and that "Laurie Schafer called later in the day and stated that Ms. Lyman could use the lab and xray *only during Dr. Penn's office hours*, otherwise Ms. Lyman did not have privileges." ( *Id.* at 49 P186 (emphasis in original). See Proposed Amended Complaint at 39 P88; 46-49PP 132-133, 138, 142, 150; 51 P163; 59 P137; 69-71 PP170, 186; 91-92 P254 (same).)

### **Marilee Bailey, R.N.**

At relevant times, defendant Marilee Bailey, R.N., worked as a nurse on the SJHSD support staff. Plaintiffs allege that Ms. Bailey is the wife of defendant Richard Bailey, and that like Laurie Schafer, "Dr. MacArthur had an incident report allegedly filed against him by Marilee Bailey, Julie Bronson, Laurie Shafer, Cleal Bradford that was never discussed with him [\*\*48] or placed in his District file, and is a report that he considers to be untrue." (Proposed Pretrial Order at 25 P96; see Proposed Amended Complaint at 39 P88 (same).)

### **Ora Lee Black**

Plaintiffs allege that "Ora Lee Black, as manager of Blanding clinic and birthing center, posted a paper on the walls within site of the patients stating that Mrs. Lyman had no privileges at SJHSD. Later the limited privileges of lab and exray [sic] were extended to her for her patients as required by State law," and that SJHSD "Staff had previously voted for her privileges and then the County, Board, and medical staff did nothing while District staff Ora Lee Black, Dr. Redd, Gloria Yanito denied her the same. Some privileges as to labs and exrays [sic] were eventually restored." (Proposed Pretrial Order at 49 P18733 54 P 209; see Proposed Amended Complaint at 71 P187 (same).) Further,

September 16, 1999 -Etta (Ms. Lyman's secretary) was told by Ora Lee Black that Ms. Lyman would not be allowed to order labs until Ms. Lyman sent a letter to Dr. Redd stating who her supervising physician was. (Ms. Lyman had already sent a letter to administration stating that the State DOPL had approved Dr. Penn in Moab as [\*\*49] her supervising physician and Dr. Robert Dr. Mena in Monticello as her back up supervising physician as he was closer than Dr. Penn and could back up any emergencies for admits for Ms. Lyman at the San Juan Hospital). By then, Dr. Dr. Mena had quit the San Juan Health Care Services as an employee and had started a private practice. (cmplt. # 149).

( *Id.* at 55 P213; see Proposed Amended Complaint at 79-80 P213 (same).)

### **Carla Grimshaw**

Carla Grimshaw is a SJHSD employee. Plaintiffs allege that "less than 24 hours prior to the February 2, 2000 medical staff meeting, Carla Grimshaw called Mrs. Lyman's office to invite Mrs. Lyman and Dr. [\*1125] MacArthur to that meeting";<sup>32</sup> that "Carla Grimshaw delivered copies of Mrs. Lyman's file to her," and that "Mrs. Lyman and Carla Grimshaw, custodian for the records, acknowledge the CPR cards were missing from Mrs. Lyman's credentialing files while in the District's custody"; that "Mrs. Lyman's CPR cards were reviewed and found to be appropriate on more than one occasion by Carla Grimshaw and Laurie Shafer"; that "Carla Grimshaw, records custodian, stated that [Dr. MacArthur's] medical license and DEA license was missing," and "allegedly wrote a note to [\*\*50] Mr. Bradford saying Dr. MacArthur was missing only his DEA license and State of Utah Medical License," but that "the medical staff, Cleal Bradford, Laurie Shafer, Carla Grimshaw failed to notify Dr. MacArthur of any missing documents in his application packet." (Proposed Pretrial Order at 26 P102, 32 P156, 33 P161, 34 P170, 35 P182, 184, 36 P191; see also Proposed Amended Complaint at 44-50 PP114-159 ("Credentialing Document Problems").) Plaintiffs also recount that on May 5, 1999,

Andrea Bianchini (Ms. Lyman's secretary) faxed Ms. Lyman's ACLS, PALS and BLS heart resuscitation American Heart Association certification cards to Judy at the hospital at the administration's request. Dr. Penn and Ms. Lyman have been requesting her privileges be restored through Reid Wood. Andrea also called Carla Grimshaw to make sure that the certifications have reached her. Grimshaw stated that the faxed cards have arrived and that Medical staff reviewed the certifications, found them in order, and the packet has been placed in her personnel file.

( *Id.* at 53 P207; see Proposed Amended Complaint at 77 P207.)

### **Gloria Yanito**

Plaintiffs allege that on

December 16, 1998 - On this day, Ms. Lyman attempted to send a patient to the E.R. in Blanding for treatment. As soon as the patient got to Blanding, Christine Singer (who began working for Dr. Penn in December 1998) took a call from Gloria Yanito, RN at the Blanding Urgent Care. Ms. Yanito stated that Ms. Lyman did not have privileges and that Ms. Lyman "can not give orders of any kind or use any of the county facilities". Ms. Singer then told Ms. Lyman, with several witnesses sitting in the office. Ms. Lyman immediately called Ms. Yanito back and asked Yanito to repeat the Message. Yanito repeated, "you do not have privileges. We are not supposed to take any orders from you and you are not allowed to set foot in any of the county facilities". Ms. Lyman asked Ms. Yanito who gave her this order and she stated that Laurie Schafer and Dr. Redd. Ms. Lyman then attempted to call Laurie Schafer and [\*\*52] was told she was not in. Ms. Lyman spoke with Carla Grimshaw and told her she wanted this order in writing, Grimshaw stated that she would let Laurie know. Ms. Lyman also attempted to call Reid Wood, he was not in. (Cmplt. # 130)

( Proposed Pretrial Order at 48-49 P184; Proposed Amended Complaint at 69-70 P170 (same).) They further allege that Ms. Lyman had been granted SJHSD privileges, but "then the County, Board, [\*1126] and medical staff did nothing while District staff Ora Lee Black, Dr. Redd, Gloria Yanito denied her the same," (*id.* at 54 P209), apparently referring to the December 16, 1998 conversation with respect to Ms. Yanito.

### **Julie Bronson**

Plaintiffs allege that Julie Bronson, a nurse employed by the SJHSD, circulated a false rumor that Dr. MacArthur, *inter alia*, had previously lost practice privileges due to a felony conviction:

<sup>32</sup> On "February 1, 2000 Carla Grimshaw calls Ms. Lyman's office to say that Ms. Lyman and Dr. [\*51] MacArthur need to be at Medical staff Meeting in the a.m. at 0800. Ms. Grimshaw states nothing about their privileges being an agenda item, or that medical staff would making any decisions about those privileges." (Proposed Pretrial Order at 58-59 P229.)

January 31, 2000- Louisa Lyman, of the Utah State Public Health system calls Ms. Lyman's office and states that nurse Julie Bronson has said that Dr. MacArthur lost his privileges to perform, epidurals due to a felony conviction, that during a delivery the nurse came to Dr. MacArthur in the Dr's lounge and told him that the OB was ready to push and he [\*\*53] purportedly said, "I'm going to have an orgasm", and that Dr. MacArthur spent time in prison for tax evasion- All of which is totally untrue and without any foundation whatsoever. Louisa called her office and first spoke to Christine. Ms. Lyman called back and Louisa Lyman repeated this story. Ms. Lyman stated the story was untrue.

(Proposed Amended Complaint at 84-85 P228; see Proposed Pretrial Order at 58 P228 (same).) They also allege, as noted above, that "Dr. MacArthur had an incident report allegedly filed against him by Marilee Bailey, Julie Bronson, Laurie Shafer, Cleal Bradford that was never discussed with him or placed in his District file, and is a report that he considers to be untrue." ( *Id.* at 39 P88; see Proposed Pretrial Order at 25 P96 (same).)

#### **Lori Wallace, R.N. a/k/a Laurie Walker**

As summarized above, Plaintiffs allege that on April 14, 1999, plaintiff Helen Valdez (accompanied by her sister-in-law, Charleen Gonzales) came to the San Juan Hospital emergency room, seeking medical care for an illness later diagnosed as acute diverticulitis. At that time, SJHSD employee Lori Wallace, R.N., was working in the emergency room. While Ms. Valdez was in the hospital lavatory, [\*\*54] she alleges that Ms. Gonzales overheard Lori Wallace tell the emergency room clerk "to go to Dr. Penn's clinic." (Proposed Amended Complaint at 23; Proposed Pretrial Order at 13;*id.* at 23 P81 ("Mrs. Valdez was told by Mrs. Gonzales that Nurse Wallace had told the receptionist that Dr. Penn's clinic was open and Mrs. Valdez should go to the clinic.")) Without any direct conversation with Lori Wallace, Ms. Valdez decided to leave the emergency room, again accompanied by Ms. Gonzales, and return home. Plaintiffs allege that Ms. Valdez "was turned away, when accompanied by her Mexican-American appearing sister-in-law, by nurse Laurie Wallace"; at the same time, plaintiffs allege that "the white young male with no insurance in the ER waiting area was seen by Dr. Penn almost immediately after Mrs. Valdez left." (Proposed Amended Complaint at 86 P232-233; see Proposed Pretrial Order at 22 P66 ("Mrs. Valdez' neighbor who was a white young male and had no insurance was seen immediately.")) Plaintiffs pleaded no other factual allegations against Ms. Wallace.

#### **Dr. Lloyd Val Jones, M.D.**

Dr. Lloyd Val Jones, M.D., is a licensed physician practicing in Blanding, Utah, who at relevant times has [\*\*55] provided services under contract with the SJHSD. Plaintiffs allege that "For Mrs. Lyman's claims, at times the [SJHSD] medical staff consisted of Dr. Penn, Dr. Mena, Dr. Jones, Dr. Nelson, Dr. Cook, Dr. Redd." (Proposed Amended Complaint at 30-31 [\*1127] P28; see Proposed Pretrial Order at 18 P28 (same).<sup>33</sup>) According to plaintiffs,

- 32. Dr. Redd and Dr. Jones and Dr. Cook and Dr. Nelson did not approve Mrs. Lyman having privileges unless her doctor was a medical staff member and then only if the physician was in the same town as she.
- 33. While the policy for P.A.s appears neutral, it effected only Michele Lyman in how it was applied, monitored, and carried out.
- 34. Mrs. Lyman had no other place to apply for hospital privileges.
- 35. Mrs. Lyman's patients at times stopped going to her as they needed to use the District emergency facilities for ailments and were told they could not.

(*Id.* at 31 PP32-35.) Plaintiff Lyman alleged that her privileges were "severely limited by Dr. Redd and Dr. Jones with no action by the board of directors," recounting a single conversation in mid-1999:

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<sup>33</sup> According to plaintiffs, With the exceptions of Dr. Jones and a Monument Valley clinic doctor, all other physicians and P.A.'s within San Juan District are employees of San Juan District." (Proposed Pretrial Order at 20 P43.)

209. Dr. Penn and Ms. Lyman attended the Medical staff Meeting for June, 1999. Dr. Penn and Ms. Lyman requested [\*\*56] full privileges be restored and Dr. Redd and Jones both stated that only if Dr. Penn was willing to sit in Blanding with Ms. Lyman while Ms. Lyman took ER call and they would not supervise me. Mr. Bryant as a P.A. working under Dr. Jones while Dr. Jones was not in Blanding, had no such restraints. Mrs. Lyman pointed out that she covered the ER (Blanding urgent care clinic) in Blanding by herself on many occasions. There was no response. (Cmplt. 137-145) Staff had previously voted for her privileges and then the County, Board, and medical staff did nothing while District staff Ora Lee Black, Dr. Redd, Gloria Yanito denied her the same. Some privileges as to labs and xrays [sic] were eventually restored.

210. Dr. Penn then suggested to medical staff that the only reason that Dr. Redd was against Ms. Lyman's privileges was because Dr. Redd was mad at Ms. Lyman for quitting Dr. Redd and Dr. Redd couldn't take it. To this Dr. Redd responded, "So what!" Dr. Jones then made the comment that Ms. Lyman had a rather large following of patients and that when he was taking ER call he didn't want Ms. Lyman to be able to see her patients at will and thus "dip into his ER money". They left with [\*\*57] the staff's edict that Ms. Lyman could call into the ER (Blanding Urgent Care) for shots. However, Ms. Lyman tried on several occasions to call in injections to the ER (Blanding Urgent Care Clinic) and was denied every time. Ms. Lyman always had to call Dr. Penn's office and have him call the order in. (Cmplt. 146)

(*Id.* at 78-79 PP209-210; see Proposed Pretrial Order PP209-210 (same).)

Circumstances change, and by the time of pretrial, Ms. Lyman was working for Utah Navajo Health Systems, once again *under Dr. Jones' supervision*, ( see Tr. 11/15/02, at 24:9-25 (Ms. Rose)); she points to two recent incidents involving patients in Dr. Jones' and her care:

253. Within the last 14 or so days, a patient of Dr. Jones and Michele Lyman's was told, when she called the Birthing Center in labor, that the Birthing Center was shut and she would just have to travel to Monticello. Dr. Jones' staff verified that indeed the BCC was claiming they were SHUT. The patient presented [\*\*58] at Blanding Family Clinic, [\*1128] now owned by Utah Navajo Health Systems, and was found to be too far progressed to travel anywhere. Time was of the essence. Mrs. Lyman's supervising physician was denied patient care by the District he has full privileges with. The lady delivered in the Blanding Family Clinic and was then transported to Monticello for observation. The Blanding Family Clinic is taxpayer supported. There is no record of this type of patient of a Dr. Redd being told the Birthing Center was shut.

254. In another instance, a woman in labor was bleeding to death and she and the baby were in a very dangerous situation. Dr. Jones and Mrs. Lyman transported the woman to the Birthing Center and did an immediate c section on the unconscious or nearly unconscious mother. Both mom and baby were saved. As Dr. Jones was cleaning up, Dr. Fisher and Laurie Shafer were telling Mrs. Lyman and another nurse of Dr. Jones that they would have to leave. Mrs. Lyman and the nurse finished caring for the patient. This incident occurred prior to the Clinic being 'shut' when Michele's next patient was in labor and delivered in a clinic.

(Proposed Amended Complaint at 91-92 PP253-254; see Proposed Pretrial [\*\*59] Order at 62-63 PP253-254 (same).)

#### **Dr. Manfred Nelson, M.D.**

Dr. Manfred Nelson, M.D., is a licensed physician practicing in San Juan County and at relevant times was a member of the SJHSD medical staff. Plaintiffs' allegations against Dr. Nelson--few as they are--essentially parallel those pleaded against Dr. Jones concerning restriction of Ms. Lyman's privileges in mid-1999, with the addition of the assertion that "Dr. Nelson sent a letter severely criticizing Mrs. Lyman and he is on Medical Staff and has never met her, spoken to her, or worked with her. His writings are the best evidence of the types of rumors he was being told, and the damages the medical staff were seeking to inflict upon Mrs. Lyman." (Proposed Pretrial Order at 61 P248.)

**Dr. James Redd, M.D.**

As noted above, Dr. James Redd, M.D., a Blanding, Utah physician, maintained a private medical practice in Blanding until he became a SJHSD employee in early 1999; at relevant times thereafter, Dr. Redd served as District medical staff director. Early in her career, plaintiff Lyman worked as a Physician Assistant under Dr. Redd's and Dr. Jones' supervision. She ended that arrangement in October 1998, and sought supervision **[\*\*60]** by other physicians practicing in the area.

From a review of plaintiff Lyman's allegations at the time of pretrial, it becomes plainly apparent that Dr. Redd is the primary focus of those allegations. Plaintiffs plead a litany of factual allegations against Dr. Redd, recounting a series of incidents involving the making of derogatory remarks or infliction of other verbal abuse, interference with Ms. Lyman's exercise of SJHSD staff privileges from and after the time she left his supervision in October 1998, and harassment and intimidation of patients who had some relationship with Ms. Lyman and/or her supervising physicians (Drs. Penn, Mena, MacArthur and now, Jones). (See Proposed Pretrial Order at 41-45 PP133(D)-(F), 138, 144-150, 153, 156-159; *id.* at 45-48 PP162-163, 165-166; *id.* at 48-50 PP167-186, 193; *id.* at 62-63 PP253-254 (quoted *supra*); see also Proposed Amended Complaint at 58-76 PP133(D)-(F), 138, 143-150, 153, 156-195, 199-205; *id.* at 77-78 PP208 (emergency room patient "was told by Dr. Redd that she must choose between Ms. Lyman/Dr. Penn and **[\*1129]** Dr. Redd as a health care provider," and that "if the patient chose Ms. Lyman, the patient could never use the E.R. again.").) Plaintiffs **[\*\*61]** assert that "the District medical staff director, Dr. Redd has a long standing policy of animus toward women both as employees and as patients," (*id.* at 20 P51), borne out in the incidents recounted in their pleadings, and that Dr. Redd demeaned and disparaged the other physicians with whom Ms. Lyman had associated. (*Id.* at 56 PP215-216.) They also allege a pattern of personal harassment and annoyance directed against Ms. Lyman by Dr. Redd:

196. Dr. Redd was witnessed by others as driving by Mrs. Lyman's home, frequently honking.

197. Mrs. Lyman reports that Dr. Redd followed Mrs. Lyman's about 10 year old daughter in his car for a period of time, frightening the daughter.

198. Mrs. Lyman and her nurse Christine Singer, experienced numerous flat tires over a two week or so period, with no foreign items found in the tires. These flat tires occurred at the office and at their homes.

(*Id.* at 51 PP196-198; see Proposed Amended Complaint at 73-74 PP196-198 (same).)

**THE PART I PLAINTIFFS' THEORIES OF LIABILITY**

As summarized in the Proposed Pretrial Order, Part I of the Proposed Amended Complaint asserts an array of causes of action arising under federal and Utah state law, including:

- (1) **[\*\*62]** Racketeer Influenced Corrupt Organizations Act, [18 U.S.C. §§ 1961 et seq. \(2000\)](#);
- (2) Freedom of Access to Clinic Entrances Act of 1994, [18 U.S.C. § 248 \(2000\)](#)(3) Health Care Quality Improvement Act, [42 U.S.C. § 11112 \(2000\)](#);
- (4) Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C. § 1395dd\(2000\)](#);
- (5) "Medicare Patient Bill of Rights," [42 U.S.C. § 1395a \(2000\)](#); (6) [42 U.S.C. § 1981 \(2000\)](#);
- (7) [42 U.S.C. § 1985\(3\) \(2000\)](#);
- (8) [42 U.S.C. § 1983\(2000\)](#);

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(9) § 4 of the Clayton Act, [15 U.S.C. § 15 \(2000\)](#) and § 1 of the Sherman Anti-Trust Act, [15 U.S.C. § 1 \(2000\)](#);  
<sup>34</sup>

(10) [Utah Constitution, art. I, §§ 1, 7, 25, 26, 27](#);

(11) Utah Unfair Practices Act, [Utah Code Ann. §§ 13-5-1 et seq.](#) (2001);

(12) Utah Civil Rights Act, [Utah Code Ann. §§ 13-7-1 et seq.](#) (2001);

(13) interference with contract and with prospective business relations;

(14) "state common law defamation (also a U.S. Constitutional right to reputation as guaranteed by the [Ninth Amendment](#)";<sup>35</sup>

(15) "Federal common law and Utah contract common law and statutory provisions that prohibit contracts of adhesion, bad faith, and lack of fair dealing. Utah Code Ann. 78-12-25(1) (1996)," including [\*1130] the implied covenant of [\*\*\*63] good faith and fair dealing;<sup>36</sup>

(16) "privacy rights and statutory entitlements to have their credential files and patient files accurately kept by the district under Medicaid and Utah Health Department statutes and regulations";

(17) negligent and intentional infliction of emotional distress; and

(18) fraud.

(See Proposed Pretrial Order at 3-6.)

**HN9** Generally, a pleading must contain [\*\*\*64] "a short and plain statement of the claim showing that the pleader is entitled to relief." [Fed.R.Civ.P. 8\(a\)\(2\)](#). "Accordingly, a pleading must 'give[ ] fair notice and state[ ] the elements of the claim plainly and succinctly.'" [Jones v. Community Redevelopment Agency, 733 F.2d 646, 649 \(9th Cir. 1984\)](#) (quoting 2A J. Moore & J. Lucas, *Moore's Federal Practice* P8.13 at 8-111 (2d ed.1983)). To give such notice, a pleading must set forth specific facts as the basis for the plaintiffs' claims, not merely legal conclusions. Without specific facts, "claims are little more than conclusory allegations, which are insufficient to state a claim for relief." [Swoboda v. Dubach, 992 F.2d 286, 289-290 \(10th Cir. 1993\)](#) (citing [Hall v. Bellmon, 935 F.2d 1106, 1110 \(10 th Cir. 1991\)](#)).

**HN10** The parties may test the legal sufficiency of claims by motion under [Fed. R. Civ. P. 12\(b\)\(6\)](#) or [56](#), and as explained above, "[Rule 16](#) empowers district courts to weed out frivolous claims." [Smith v. Gulf Oil Co., 995 F.2d 638, 644 \(6th Cir. 1993\)](#). "There is no reason to require that [the elimination of frivolous claims] await a formal motion for summary judgment," [Fed. R. Civ. P. 16\(c\)\(1\)](#), advisory committee note to 1983 [\*\*\*65] amendment, and it certainly "is not inconsistent with the general purpose of [Rule 16](#) to use this rule 'to determine whether there are any issues remaining in the case that justify proceeding to a full trial on the merits.'" [Chavez v. Illinois State Police, 251 F.3d 612, 654 \(7th Cir. 2001\)](#) (quoting 6A Charles A. Wright, et al., *Federal Practice & Procedure* § 1529, at 301 (2d ed.1990)).

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<sup>34</sup> More recently, plaintiffs' counsel has invoked the Utah Antitrust Act, Utah Code Ann. §§ 76-10-911 through 76-10-926 (2003), in addition to the federal antitrust statutes. (Memorandum in Support of Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross- Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), at 4.)

<sup>35</sup> Plaintiffs' counsel now refers to "civil and criminal defamation with malice," apparently invoking [Utah Code Ann. § 76-9-404](#) (2003) in addition to the common law theories. (*Id.*)

<sup>36</sup> Plaintiffs' counsel would now extend this theory to reach interference with a plaintiff's "right to pursue his profession and business affairs by lack of good faith and fair dealing inherent and mandated in all Utah business relations." (*Id.*)

In evaluating whether the plaintiffs' claims are maintainable or are frivolous, court and counsel must examine them within the framework of their various legal theories; the facts alleged as the basis for these claims must be considered in terms of the essential elements of each cause of action.

### (1) Plaintiffs' Civil RICO Claims ([18 U.S.C. §§ 1961 et seq.](#))

**HN11** [↑] In order to state a civil RICO claim, a plaintiff must allege that he or she suffered (1) an injury to his or her business or property because the defendant(s), (2) while involved in one or more enumerated relationships with an "enterprise," (3) engaged in a pattern of racketeering activity or collected an unlawful debt. See [18 U.S.C. §§ 1961-1968\(2000\)](#).

#### Predicate Acts of "Racketeering Activity" ([18 U.S.C. § 1961\(1\)](#))

**HN12** [↑] Among the essential elements required [\*\*66] to establish civil liability under the RICO statute, plaintiffs must show, *inter alia*, that the defendants have conducted the affairs of an identifiable "enterprise" through a "pattern of racketeering activity," that is, that the defendants have committed a continuous series of related criminal acts in violation of one or more of the [\*1131] statutes listed in [18 U.S.C. § 1961\(1\)](#) ("racketeering activity" defined). [18 U.S.C. § 1962](#). See, e.g., [BancOklahoma Mortgage Corp. v. Capital Title Co., 194 F.3d 1089, 1100 \(10th Cir. 1999\)](#) ("To establish a civil RICO claim under [18 U.S.C. § 1962\(c\)](#), [plaintiff] must show that the [defendants] '(1) participated in the conduct (2) of an enterprise (3) through a pattern (4) of racketeering activity.' [Resolution Trust Corp. v. Stone, 998 F.2d 1534, 1541 \(10th Cir. 1993\)](#) (citing [Phelps v. Wichita Eagle-Beacon, 886 F.2d 1262, 1273 \(10th Cir. 1989\)](#)).") Defendants "need not engage in the stereotypical mobster behavior to come within the bounds of civil RICO," [Smith v. Our Lady of the Lake Hosp., Inc., 960 F.2d 439, 447 \(5th Cir. 1992\)](#) (citing [United States v. Turkette, 452 U.S. 576, 580-81, 591, 69 L. Ed. 2d 246, 101 S. Ct. 2524\(1981\)](#)), but they must nevertheless [\*\*67] be shown to have participated in continuing criminal violations constituting an identifiable "pattern of racketeering activity." See [H.J. Inc. v. Northwestern Bell Tel. Co., 492 U.S. 229, 239, 106 L. Ed. 2d 195, 109 S. Ct. 2893 \(1989\)](#).<sup>37</sup>

The Proposed Amended Complaint points to mail fraud ([18 U.S.C. § 1341](#)), witness tampering ([18 U.S.C. § 1512](#)) and interference with commerce by threats ([18 U.S.C. § 1951](#)) as the predicate acts of racketeering activity pertinent to plaintiffs' claims asserted in this case.<sup>38</sup> (Proposed Amended Complaint at 12.)

##### (a) [18 U.S.C. § 1341](#) - Mail Fraud

[18 U.S.C. § 1341 \(2000\)](#) reads:

**HN13** [↑] Whoever, having devised or intending to devise any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, or to sell, dispose of, loan, exchange, alter, give away, distribute, supply, or furnish or procure for unlawful use any counterfeit or spurious coin, obligation, security, or other article, or anything represented to be or intimated or held out to be

<sup>37</sup> The statute of limitations applicable to civil RICO actions is the four-year limitations period governing civil enforcement actions under the Clayton Act, [15 U.S.C. § 15b](#). See, e.g., [Agency Holding Corp. v. Malley-Duff & Assocs., Inc., 483 U.S. 143, 156, 107 S. Ct. 2759, 97 L. Ed. 2d 121 \(1987\)](#); [Phelps v. Wichita Eagle-Beacon, 886 F.2d 1262, 1273 n. 12 \(10th Cir. 1989\)](#).

<sup>38</sup> "The various acts of racketeering activity described in the statute are often referred to as 'predicate acts' because they form the basis for liability under RICO." [BancOklahoma Mortgage Corp., 194 F.3d at 1102](#) (citing [Bacchus Industr., Inc. v. Arvin Industr., Inc., 939 F.2d 887, 891 \(10th Cir. 1991\)](#)). [\*\*68]

Plaintiffs' counsel also refers to "(d) illegal destruction or tampering with confidential documents in a federally contracted facility;" and "(e) intimidation of witnesses for monetary gain," (Proposed Pretrial Order at 3 P(5)), but these are not found among the offenses enumerated in the statute's definition of "racketeering activity" and thus cannot serve as RICO predicate acts. [18 U.S.C. § 1961\(1\)](#) ("racketeering activity" defined).

such counterfeit or spurious article, for the purpose of executing such scheme or artifice or attempting so to do, places in any" post office or authorized depository for mail matter, any matter or thing whatever to be sent or delivered by the Postal Service, [\*\*69] or deposits or causes to be deposited any matter or thing whatever to be sent or delivered by any private or commercial interstate carrier, or takes or receives therefrom, any such matter or thing, or knowingly causes to be delivered by mail or such carrier according to the direction thereon, or at the place at which it is directed to be delivered by the person to whom it is addressed, any such matter or thing, shall be fined under this title or imprisoned not more than 20 years, or both. [\*1132] If the violation affects a financial institution, such person shall be fined not more than \$ 1,000,000 or imprisoned not more than 30 years, or both.

**HN14** [↑] In order to prove the offense defined in [§ 1341](#) in a criminal proceeding, the government must prove the following essential elements: (1) that the defendant knowingly devised or knowingly participated in a scheme or artifice for obtaining money or property by means of false or fraudulent pretenses, representations, or promises; (2) that the pretenses, representations or promises were material, that is, they would reasonably influence a person to part with money or property; (3) that the defendant did so with the intent to defraud; and (4) that in advancing, [\*\*70] or furthering, or carrying out this scheme to obtain money or property by means of false or fraudulent pretenses, representations, or promises, the defendant used the mail, or any private or commercial interstate carrier, or caused the same to be used by someone else.

**HN15** [↑] To establish mail fraud as a predicate act of racketeering activity for the purposes of a civil RICO claim, plaintiffs must plead and prove facts establishing each of these essential elements as to each occurrence, as to each predicate act alleged as part of the requisite "pattern of racketeering activity." [Rule 9\(b\) of the Federal Rules of Civil Procedure](#) require that allegations of mail fraud be pleaded with particularity. See, e.g., [Farlow v. Peat, Marwick, Mitchell & Co., 956 F.2d 982, 989-90 \(10th Cir. 1992\)](#) (predicate acts of mail fraud require heightened pleading pursuant to [Rule 9\(b\)](#)); [Cayman Exploration Corp. v. United Gas Pipe Line Co., 873 F.2d 1357, 1362 \(10th Cir. 1989\)](#) ([Rule 9\(b\)](#) requires particularity in pleading the RICO predicate acts of mail fraud).

Plaintiff Lyman alleges that her CPR certification cards, "a necessary component of her ability to obtain privileges were altered purposefully," that "she [\*\*71] was not notified immediately that her cards were in some way in error," that "the cards were stolen from her file at least on two if not three occasions," that "*the forged documents were mailed to the American Heart Association,*" and that "the doctors would have profited from Mrs. Lyman not being able to work . . . ." (Proposed Pretrial Order at 63 P255 (emphasis added); see *id.* at 14 ("forged documents were sent in the US mail to harm her reputation with the American Heart Association who oversees the cpr classification certification programs Mrs. Lyman is obligated to pass")); *id.* at 29 PP129-131 ("The U.S. mail was used to mail the cards while the local doctors and medical providers could profit from limiting Mrs. Lyman's competition and reputation with the American Heart Association"); *id.* at 34 PP174-175.)

Plaintiff Lyman thus complains that her CPR cards were altered and/or forged, and alleges "the use of the mail system to send fraudulent cards" to the American Heart Association. (*Id.* at 66.) Yet **HN16** [↑] mail fraud is not committed simply by sending false statements through the mail; the mails must have been used to further a scheme to defraud or obtain money or property through false [\*\*72] pretenses. See [BancOklahoma Mortgage Corp., 194 F.3d at 1102](#). Here, Ms. Lyman's CPR cards, even if altered or forged, and thereby becoming false or "fraudulent" representations in one sense, are not themselves alleged to be the means of obtaining money or property, and are not such as to "reasonably influence a person to part with money or property" as required to prove a violation of [§ 1341](#). Plaintiffs allege that "the local doctors and medical providers could profit from limiting Mrs. Lyman's competition and reputation with the American Heart Association," (Proposed Pretrial Order at 29 P131), but do not claim that any of the defendants obtained or schemed to obtain money or property by means of the altered or forged CPR cards.

Here, the Part I Plaintiffs have failed to plead facts establishing **HN17** [↑] the essential elements of mail fraud (a scheme or artifice to defraud, *viz.*, to obtain money or property by means of false or fraudulent pretenses, representations, or promises, and the use of the mails in furtherance of the scheme) as against any of the named defendants.

(b) **18 U.S.C. § 1512** - Witness Tampering

**HN18**[<sup>↑</sup>] Section 1512 of Title 18, United States Code prohibits specific conduct, including [\*\*73] physical force, threats of physical force, or intimidation, threatening, "corrupt" or "misleading" persuasion or harassment, that is intended to "influence, delay or prevent" a witness from attending or testifying in an official proceeding, or intended to cause testimony, records, documents, or other objects to be withheld, concealed, altered or destroyed in order to impair their availability for use in an official proceeding. 18 U.S.C. § 1512(a), (b), (c), (d) (2000). Section 1512 prohibits only the coercive conduct specifically described in its subsections; the legislative history reflects Congress' rejection of broadly inclusive language in favor of "the specific conduct narrowly described in the final version of the statute." United States v. Dawlett, 787 F.2d 771, 774-775 (1st Cir. 1986) (citing United States v. Lester, 749 F.2d 1288, 1295-1297 (9th Cir. 1984)); cf. McAndrew v. Lockheed Martin Corp., 206 F.3d 1031, 1039-1040 (11th Cir. 2000) (assertion that defendants attempted to deter plaintiff by force, intimidation, or threat from testifying before a federal grand jury about employer's activities by threatening him with job-related sanctions alleged a violation under the federal [\*\*74] witness tampering statute).

The Part I Plaintiffs assert that defendant "Dr. Redd informed the head of the local nursing home that the nursing home patients would no longer see Dr. Cook as a result of making a witness statement," that "witnesses have requested that they not be used to give testimony due to fear of retaliation and loss of jobs," and that one witness has stated she is petrified her relatives will not stay employed or her children will not be seen at District facilities if she testifies." (Proposed Pretrial Order at 61 PP244-246; Proposed Amended Complaint at 88-89 PP244-246.) None of these allegations set forth facts evidencing conduct by any named defendant that falls within the scope of the statute.

**HN19**[<sup>↑</sup>] Prospective fact witnesses may indeed feel fearful, anxious or apprehensive about how their testimony may be responded to by those against whom it may be offered. In some cases, potential witnesses may fear for their very lives, and with good reason. Federal law affords such witnesses some degree of protection. See generally 18 U.S.C. § 1513 (retaliation against witness); 18 U.S.C. §§ 3521-3528 (2000) (federal witness protection program). But fear, anxiety and apprehension [\*\*75] on the part of a prospective witness as to a future loss of employment, denial of services, or other adverse personal consequences do not equate with the culpable criminal conduct on the part of a defendant that violates § 1512. A defendant must do *something* -- use physical force, threats of physical force, or intimidation, threatening, corrupt or misleading persuasion or harassment -- that is intended to "influence, delay or prevent" a witness from attending or testifying in an official proceeding, or intended to cause testimony, records, documents, or other objects to [\*\*1134] be withheld, concealed, altered or destroyed in order to impair their availability for use in an official proceeding, in order to run afoul of the witness tampering statute. 18 U.S.C. § 1512(a)-(d).<sup>39</sup> The Proposed Amended Complaint alleges nothing of that kind.<sup>40</sup>

<sup>39</sup> **HN20**[<sup>↑</sup>] Section 1512 addresses specific affirmative coercive or misleading conduct intended to inhibit or influence *future* witness testimony or the availability of evidence yet to be offered in a pending or future federal proceeding. See United States v. Rose, 362 F.3d 1059, 1067-1068 (8th Cir. 2004); United States v. Davis, 357 F.3d 726, 728-729 (8th Cir. 2004), [\*\*76] vacated on other grounds, 543 U.S. 1099, 125 S. Ct. 1049, 160 L. Ed. 2d 993 (2005) (mem.); United States v. Romero, 54 F.3d 56, 62 (2d Cir. 1995) ("knowing interference with a potential communication between an individual who might become a witness and federal law enforcement officials falls within the ambit of Section 1512. We have thus previously noted that the statute covers 'potential' witnesses. United States v. Hernandez, 730 F.2d 895, 898 (2d Cir. 1984) ('[section] 1512 explicitly covers "potential" witnesses>'); United States v. Maggitt, 784 F.2d 590, 593 (5th Cir. 1986) ("18 U.S.C. § 1512 punishes only those threats made with the intent to cause the witness to withhold future testimony").

<sup>40</sup> More recently, plaintiffs' counsel has asserted that Dr. MacArthur and Ms. Lyman suffered retaliation in violation of 18 U.S.C. § 1513 for having informed the SJHSD's governance board of remarks made by SJHSD administration and staff concerning Dr. Nathaniel Penn being a "little New York Jew." (See Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), at [\*\*77] 17; Memorandum in Support of Plaintiff Lyman's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' [sic] Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed December 28, 2004 (dkt. no. 696), at 24.) **HN21**[<sup>↑</sup>] Section 1513 prohibits violent retaliation (e.g., killing, attempting to kill, causing bodily injury, damaging tangible property)

(c) [18 U.S.C. § 1951](#) - Interference with Commerce by Threats

**HN22** [+] The Anti-Racketeering Act of 1934, Act of June 18, 1934, ch. 569, 48 Stat. 979, codified at [18 U.S.C. § 1951 \(2000\)](#), makes it a federal offense to commit robbery or extortion that in any way or degree obstructs commerce. To prove guilt, the government must prove that a defendant committed extortion or robbery, and that such conduct interfered with interstate commerce. Though [§ 1951](#) is often referred to as the "Hobbs Act," the Hobbs Act ([Act of July 3, 1946, ch. 537, 60 Stat. 420](#)) itself amended the 1934 Anti-Racketeering Act to include extortionate conduct by labor unions, which had been held to be exempt under the statute's original language. See [United States v. Local 807, Teamsters Union, 118 F.2d 684, 687-88 \(2d Cir. 1941\)](#), aff'd, [315 U.S. 521, 539, 86 L. Ed. 1004, 62 S. Ct. 642 \(1942\)](#).

The courts read the legislative history of the 1934 Act to indicate that Congress enacted the 1934 legislation to eliminate racketeering by organized gangs, which was found to have a substantial effect on interstate commerce, particularly the interstate transportation industry. See [\*1135] [United States v. Local 807, Teamsters Union, 315 U.S. 521, 528-530, 86 L. Ed. 1004, 62 S. Ct. 642 \(1942\)](#) [\*\*\*79] (citing H. Rep. No. 1833, 73d Cong. 2d Sess. (1934)). The 1934 Act was first introduced in the Senate in response to a Senate Committee on Interstate Commerce investigation of "rackets" and "racketeering," which the Committee defined as "an organized conspiracy to commit the crimes of extortion or coercion, or attempts to commit extortion or coercion," as defined by "the penal law of the State of New York and other jurisdictions." S. Rep. No. 75-1189, 75th Cong., 1st Sess., at 3 (1935). The Committee reported that many businesses were being coerced to pay "dues" for "protection" from gangsters -- most of whom were actually affiliated with those offering the "protection" -- who would engage in the "hijacking" of trucks used to transport merchandise in interstate commerce, as well as price-fixing and other coercive conduct harmful to commerce. *Id.* at 9, 21-23; [Local 807, Teamsters Union, 315 U.S. at 529-30](#) (citing H.R. Rep. No. 73-1833, "at 2 (1934) (the 1934 Act was intended to make unlawful racketeering "in connection with price fixing and economic extortion directed by professional gangsters.")). According to the 1934 bill's sponsor, Senator Copeland, the legislation was intended [\*\*\*80] to "render more difficult the activities of predatory criminal gangs." S. Rep. No. 73-1440, at 1 (1934). The same was true of the 1946 legislation:

In arguing for the adoption of the Hobbs Act, Congressman Hobbs, the sponsor of the Act, emphasized that the 1934 Act was being amended to address highway robbery by organized labor unions and was intended to protect individuals and goods in interstate commerce. Additional testimony during the debate in the House of Representatives clearly establishes that the Hobbs Act was passed to protect individuals "trying to deliver food into the various big cities in our nation" and those "who feel they have a right to drive down ... public highways and streets ..." According to Mr. Hobbs, the "sole and simple purpose" of the Hobbs Act is to protect interstate commerce and "free the highways and streets of this country of robbers." Thus, the Hobbs Act was originally a subject matter specific statute that applied only to actions of organized gangs, and, like other subject matter specific statutes, was passed by Congress only after findings that the specific type of crime so addressed presented a national problem. This interpretation of the Hobbs Act is [\*\*\*81] further supported by the initial and long held position of the Justice Department that the robbery provision of the Act was to be utilized only in instances "involving organized crime, gang activity, or wide-ranging criminal activity."

Michael McGrail, *The Hobbs Act after Lopez*, [41 B.C.L. Rev. 949, 956-57 \(2000\)](#) (footnotes omitted). Since its 1946 re-enactment in the Hobbs Act, the Court has read [§ 1951](#) to "manifest ... a purpose to use all the constitutional power Congress has to punish interference with interstate commerce by extortion, robbery or physical violence."

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against any person for attending or furnishing testimony or evidence in a federal proceeding or providing information to a law enforcement officer "relating to the commission or possible commission of a Federal offense. ..." [18 U.S.C. § 1513\(a\), \(b\)](#). Plaintiffs have alleged no federal proceeding, no reporting of a federal offense, and no violent retaliation. Even [§ 1513\(e\)](#), which prohibits "interference with the lawful employment or livelihood of any person for providing to a law enforcement officer any truthful information relating to the commission or possible commission of any Federal offense," simply cannot be read to reach the reporting of ethnic remarks to a local hospital's governance board.

Counsel's assertion that [§ 1513](#) was violated by conduct so plainly outside the clear language of the statute raises [\*\*\*78] serious concerns under [Fed. R. Civ. P. 11](#).

United States v. Culbert, 435 U.S. 371, 373, 55 L. Ed. 2d 349, 98 S. Ct. 1112 (1978) (quoting Stirone v. United States, 361 U.S. 212, 215, 4 L. Ed. 2d 252, 80 S. Ct. 270 (1960)).

In Scheidler v. National Organization for Women, Inc., 537 U.S. 393, 154 L. Ed. 2d 991, 123 S. Ct. 1057 (2003), however, the Court read HN23<sup>41</sup> the Hobbs Act's definition of "extortion" as "the obtaining of property from another, with his consent, induced by wrongful use of actual or threatened force, violence, or fear, or under color of official [\*1136] right," 18 U.S.C. § 1951(b)(2), to require "that a person must 'obtain' property from another party to [\*\*82] commit extortion," that is, that there must be "not only the deprivation but also the acquisition of property." 537 U.S. at 404. The anti-abortion protestors in *Scheidler* did not violate § 1951 for purposes of civil RICO liability because in physically obstructing the operation of clinics performing abortions, they "neither pursued nor received 'something of value from' respondents that they could exercise, transfer or sell"; thus, under § 1951, "merely interfering with or depriving someone of property" was not "sufficient to constitute extortion." Id. at 405.

Even if taken as true in their entirety, none of the factual allegations of Part I of the Proposed Amended Complaint identify any property 'obtained' or acquired from the plaintiffs by San Juan County, the SJHSD, or any of the named individual defendants with plaintiffs' consent "induced by wrongful use of actual or threatened force, violence, or fear, or under color of official right." <sup>41</sup> Nor do any of the additional factual assertions set forth more recently in the Part I Plaintiffs' combined motions for reconsideration and summary judgment identify any property or thing of value obtained and acquired by the defendants from [\*\*83] these plaintiffs through extortionate means. (See Plaintiff Valdez's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 664); Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670); Plaintiff Lyman's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed December 28, 2004 (dkt. no. 695).) These plaintiffs are not engaged in the interstate transportation of goods, or in the sale of merchandise flowing through interstate commerce. Nor, for that matter, do any of plaintiffs' allegations describe conduct of the kind of "organized crime, gang activity, or wide-ranging criminal activity" on the part of the named defendants that Congress had in mind in enacting the statute.

HN24<sup>42</sup> A private civil action under the federal RICO statute remains available as a means for those persons who have been "injured in [their] business or property" by reason of a violation of RICO's criminal provisions to seek legal and equitable remedies for their injuries from those whose ongoing criminal conduct has caused them harm. See 18 U.S.C. § 1964. However, civil RICO liability does not serve merely as a device to multiply the money damages available to parties embroiled in more commonplace civil litigation,<sup>43</sup> or as a [\*1137] means to vilify civil litigants by labeling them as "racketeers," gangsters, extortionists and criminals. See Sedima, S.P.R.L. v. Imrex Co., Inc., 473 U.S. 479, 496, 87 L. Ed. 2d 346, 105 S. Ct. 3275 (1985) ((a civil RICO plaintiff only has standing if "he has been injured in his business [\*\*85] or property by the conduct constituting the violation").

HN25<sup>44</sup> Where a plaintiff's amended complaint fails to allege specific facts stating the elements essential to her federal claim under RICO, dismissal with prejudice is warranted. See, e.g., Martinez v. Martinez, 207 F.Supp.2d

<sup>41</sup> Plaintiffs assert that Ms. Lyman's patients "were told that even in an emergency they would not be seen by the District if they continued to visit Mrs. Lyman [\*\*84] for health care. Mrs. Lyman believes threatening patients that emergency care will be denied in an emergency is extortion of the lowest kind." (Proposed Pretrial Order at 63 P255.) A threat of denial of emergency medical care by a public facility may be found to be improper for a number of reasons, but such a threat does not constitute "extortion" within the meaning of the Hobbs Act.

<sup>42</sup> The potential for abuse of the civil RICO remedy was recognized some years ago: "Given the resulting proliferation of civil RICO claims and the potential for frivolous suits in search of treble damages, greater responsibility will be placed on the bar to inquire into the factual and legal bases of potential claims or defenses prior to bringing such suit or risk sanctions for failing to do so." Chapman & Cole v. Itel Container Int'l, 865 F.2d 676, 685 (5th Cir.), cert. denied, 493 U.S. 872, 110 S. Ct. 201, 107 L. Ed. 2d 155 (1989) (quoting Black & Magenheim, *Using the RICO Act in Civil Cases*, Houston Law. , Oct. 1984, at 20, 24-25 (Oct. 1984)).

1303, 1305-09 (D.N.M. 2002) ("no reasonable or competent counsel who had read any Tenth Circuit cases concerning civil RICO complaints, and the requisites thereof, could believe that the amended complaint filed in this case stated a viable RICO claim."), *aff'd in part, [\*86] vacated and remanded in part on other grounds, 62 Fed.Appx. 309, 2003 WL 1904807 (10th Cir. 2003); Condict v. Condict, 826 F.2d 923, 929 (10th Cir. 1987)* (affirming dismissal of civil RICO claim; "this is but an unsuccessful effort to dress a garden-variety fraud and deceit case in RICO clothing").

## (2) Freedom of Access to Clinic Entrances Act of 1994 ([18 U.S.C. § 248](#))

**HN26** [+] The Freedom of Access to Clinic Entrances Act of 1994, Pub. L. No. 103-259, 108 U.S.C. 694, *codified at 18 U.S.C. §§ 241, 248 (2000)*, addresses the conduct of anyone who "by force or threat of force or by physical obstruction, intentionally injures, intimidates or interferes with or attempts to injure, intimidate or interfere with any person because that person is or has been, or in order to intimidate such person or any other person or any class of persons from, obtaining or providing reproductive health services," or that person is "exercising or seeking to exercise the [First Amendment](#) right of religious freedom at a place of religious worship[.]<sup>43</sup> Though it is primarily a criminal statute, [§ 248\(c\)\(1\)](#) provides that "any [\*87] person aggrieved by reason of the conduct prohibited by subsection (a) may commence a civil action" seeking "temporary, preliminary or permanent injunctive relief and compensatory and punitive damages, as well as the costs of suit and reasonable fees for attorneys and expert witnesses," or as an alternative to compensatory damages, "an award of statutory damages in the amount of \$ 5,000 per violation." [18 U.S.C. § 248\(c\)\(1\)\(A\), \(b\)](#).

There appears little doubt that patient access to a hospital, clinic, birthing center, or physician's office in San Juan County that offers "medical, surgical, counseling or referral services relating to ... pregnancy" comes within the scope of protection afforded by this statute. [18 U.S.C. § 248\(e\)\(1\), \(5\)](#). The plaintiffs in this case, however, have not alleged that the defendants engaged in the specific offense conduct prohibited by the statute, that is, the [\*88] use of "force or threat of force or ... physical obstruction" to "intentionally injure[], intimidate[] or interfere[] with" patient access to reproductive health care facilities and services. Part I of the Proposed Amended Complaint makes no allegation of facts showing that any defendant has used physical force or obstruction to obstruct or intimidate anyone seeking to obtain or provide reproductive health services.

## [\*1138] (3) Health Care Quality Improvement Act, [42 U.S.C. § 11112 \(2000\)](#)

Following the Pretrial Conference, the Part I Plaintiffs apparently moved to dismiss their claims under the Health Care Quality Improvement Act (HCQIA), [42 U.S.C. § 11101-11152 \(2000\)](#), and the Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C. § 1395dd \(2000\)](#), on grounds of mootness. (See Plaintiffs' Motion to Dismiss, filed November 25, 2002 (dkt. no. 463).) At the hearing on January 7, 2003, the court granted plaintiffs' motion. (See Minute Entry, dated January 7, 2003 (dkt. no. 480).)<sup>44</sup>

<sup>43</sup> [Section 248\(a\)\(3\)](#) also prohibits conduct which "intentionally damages or destroys the property of a facility, or attempts to do so, because such facility provides reproductive health services, or intentionally damages or destroys the property of a place of religious worship." [18 U.S.C. § 248\(a\)\(3\)](#).

<sup>44</sup> As the case proceeded, Ms. Valdez' EMTALA and HCQIA claims were specifically dismissed on motion by her own counsel. (See Plaintiffs' Motion to Dismiss, filed November 25, 2002 (dkt. no. 463).) As written, [\*89] that motion moved "for an order dismissing the defendants' motions to dismiss EMTALA and Health Care Quality Improvement Act claims, due to mootness" -- apparently making what amounted to a motion to strike the defendants' moving papers. (*Id.* (emphasis added); see Defendants' Motion to Dismiss Plaintiffs' EMTALA Claims, filed November 13, 2002 (dkt. no. 447).) The Plaintiffs' Motion to Dismiss was not accompanied by an explanatory memorandum.

However, as docketed, calendared and heard, the Plaintiffs' Motion to Dismiss was treated as a motion to dismiss *Ms. Valdez' EMTALA and HCQIA claims* as moot:

THE COURT: ... Many of the items that we dealt with before have heretofore been resolved. I do note that plaintiff's motion to dismiss the EMTALA and Health Care Quality Improvement Act Claims, docket number 463, filed November 25th are

Apart from the question of mootness and the effect of plaintiffs' own motion, it appears in any event that the Part I Plaintiffs' claim would fail to state a legally cognizable claim. [HN27](#)[] Title IV, § 412 of the HCQIA, [42 U.S.C. § 11112](#), the provision cited by plaintiffs, does set standards for professional review actions affecting a health practitioner's practice privileges,<sup>45</sup> but it does so in the context of a statutory scheme that shields the review participants from civil liability arising from the review action if that action satisfies [§ 11112](#)'s procedural criteria.<sup>46</sup> See [42 U.S.C. § 11111; Decker v. IHC Hospitals, Inc., 982 F.2d 433, 436 \(10th Cir. 1992\)](#).

now moot and I take it ought to be, you don't have any problem with that determination, *your motion, that is you're dismissing those claims?*

MS. ROSE: Uh, yes.

THE COURT: Isn't that right, the EMTALA and Health Care Quality Improvement Act claims?

MS. ROSE: That would be fine.

THE COURT: It was your motion and I think we can grant that at this point without further [\[\\*\\*90\]](#) ado. .

(Transcript of Hearing, dated January 7, 2003, at 4:23-5:10 (emphasis added).) The dismissal of plaintiff's EMTALA and HCQIA claims was duly noted in the Minute Entry. (See Minute Entry, dated January 7, 2003 (dkt. no. 480) ("Grants, motion to dismiss (Dkt # 463)." See also Transcript of Hearing, dated February 24, 2003, at 30:19-31:8 (The Court).)

<sup>45</sup> [HCQIA § 412](#) reads in part:

(a) [HN28](#)[] In general. For purposes of the protection set forth in [section 11111 \(a\)](#) of this title, a professional review action must betaken-

- (1) in the [\[\\*\\*91\]](#) reasonable belief that the action was in the furtherance of quality health care,
- (2) after a reasonable effort to obtain the facts of the matter,
- (3) after adequate notice and hearing procedures are afforded to the physician involved or after such other procedures as are fair to the physician under the circumstances, and
- (4) in the reasonable belief that the action was warranted by the facts known after such reasonable effort to obtain facts and after meeting the requirement of paragraph (3).

A professional review action shall be presumed to have met the preceding standards necessary for the protection set out in [section 11111 \(a\)](#) of this title unless the presumption is rebutted by a preponderance of the evidence.

[42 U.S.C. §11112\(a\) \(2000\).](#)

<sup>46</sup> [11 of HCQIA](#) provides:

**(1) [HN29](#)[] Limitation on damages for professional review actions**

If a professional review action (as defined in [section 11151 \(9\)](#) of this title) of a professional review body *meets all the standards specified in [section 11112 \(a\)](#) of this title*, except as provided in subsection (b) of this section-

- (A) the professional review body,
- (B) any person acting as a member or staff to the body,
- (C) any person under a contract or other formal [\[\\*\\*92\]](#) agreement with the body, and
- (D) any person who participates with or assists the body with respect to the action,

shall not be liable in damages under any law of the United States or of any State (or political subdivision thereof) with respect to the action.

[42 U.S.C. § 11111 \(2000\)](#) (emphasis added). [HN30](#)[] [Section 11111](#) makes an express exception as to liability under "any law of the United States or any State relating to the civil rights of any person or persons, including the Civil Rights Act of 1964, [42](#)

The court of appeals has determined that [HN31](#)<sup>46</sup> the HCQIA does not create a private civil cause of action in favor of plaintiffs whose staff privileges at a medical facility have been adversely affected by a professional or peer review action. See, e.g., [Hancock v. Blue Cross-Blue Shield](#), 21 F.3d 373, 374 (10th Cir. 1994). Therefore, in the context of a grievance by a health care professional whose staff privileges have been limited or denied by a peer review process, the question posed by the HCQIA is not whether the participants in the review process [\[\\*\\*93\]](#) are *liable under the HCQIA*, but whether the HCQIA operates to immunize those participants from private civil liability based upon other legal theories. Therefore, as a matter of law, the Part I Plaintiffs can plead no claim "for violation of the guarantees found in" the HCQIA as such.

#### (4) Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C. § 1395dd \(2000\)](#)

[HN32](#)<sup>47</sup> The Emergency Medical Treatment and Active Labor Act (EMTALA), as added by [§ 9121\(b\)](#) of the Consolidated Omnibus Budget Reconciliation Act of 1985, 100 Stat. 164,, and as amended, [42 U.S.C. § 1395dd](#), places obligations of screening and stabilization upon hospitals and emergency rooms that receive patients suffering from an "emergency medical condition."

[Roberts v. Galen of Virginia, Inc.](#), 525 U.S. 249, 250, 142 L. Ed. 2d 648, 119 S. Ct. 685 (1999). Among other provisions, EMTALA requires the emergency departments of hospitals participating in the federal Medicare program to provide appropriate medical screening and stabilizing treatment for all persons who present themselves at the emergency room and request care:

[HN33](#)<sup>48</sup> (a) **Medical screening requirement.** In the case of a hospital that has a hospital emergency department, [\[\\*\\*94\]](#) if any individual (whether or not eligible for benefits under this subchapter) comes to the emergency department and a request is made on the individual's behalf for examination or treatment for a medical condition, the hospital must provide for an appropriate medical screening examination within the capability of the hospital's emergency department, including ancillary services routinely available to the emergency department, to determine whether or not an emergency medical condition (within the meaning of subsection (e)(1) of this section) exists.

##### [\*1140] (b) Necessary stabilizing treatment for emergency medical conditions and labor

###### (1) In general

If any individual (whether or not eligible for benefits under this subchapter) comes to a hospital and the hospital determines that the individual has an emergency medical condition, the hospital must provide either-

(A) within the staff and facilities available at the hospital, for such further medical examination and such treatment as may be required to stabilize the medical condition, or

(B) for transfer of the individual to another medical facility in accordance with subsection (c) of this section.

[42 U.S.C. § 1395dd\(a\), \(b\) \(2000\)](#). [HN34](#)<sup>49</sup> Subsection (c) of § 1395dd [\[\\*\\*95\]](#) sets standards governing the transfer of emergency room patients to other health care facilities, and [subsection \(d\)](#) provides for the enforcement of [§ 1395dd](#)'s requirements through civil monetary penalties collected by the Secretary of Health and Human Services and through private civil actions by "any individual who suffers personal harm as a direct result of a participating hospital's violation of a requirement of this section." [42 U.S.C. § 1395dd\(d\)\(2\) \(2000\)](#).<sup>47</sup> The statute

[U.S.C. 2000e, et seq.](#) and the Civil Rights Acts, [42 U.S.C. 1981, et seq.](#)" and for actions by the Attorney General under the federal antitrust laws. *Id.*

<sup>47</sup> Subsection (d) of § 1395dd reads:

[HN35](#)<sup>50</sup> (2) **Civil enforcement**

has been construed as imposing strict liability on hospitals for violations of its screening and stabilization requirements. See *Abercrombie v. Osteopathic Hosp. Founders Ass'n*, 950 F.2d 676, 681 (10th Cir. 1991); *Stevision v. Enid Health Systems, Inc.*, 920 F.2d 710, 713 (10th Cir. 1990).

**HN36** [↑] A hospital's duty to provide the required emergency medical screening and stabilizing treatment to persons requesting such care cannot be delayed by any inquiry as to that person's "method of payment or insurance status." [42 U.S.C. § 1395dd\(h\)](#). Nor is the participating hospital's duty to provide emergency screening and treatment under [§ 1395dd\(a\)](#) and [\(b\)](#) limited to those persons who are regularly in the care of physicians or health care providers having current staff privileges or practice privileges at that hospital.

As to plaintiff Helen Valdez, counsel at the time of pretrial asserted the "violation of Mrs. Valdez' entitlement [\*\*97] to an equal standard of care and to be examined upon her presentation to the emergency room of the hospital as mandated by [42 USC 1395dd](#)," apparently invoking EMTALA's private civil remedy. (Proposed Amended Complaint at 14 P(22); Proposed Pretrial Order at 5 P(23).)

The event in question occurred on April 14, 1999, yet plaintiff Valdez did not plead a claim under [§ 1395dd\(d\)\(2\)](#) of EMTALA in the original complaint in this action filed on July 25, 2000,<sup>48</sup> and did not attempt to [\*1141] plead such a claim until the Proposed Amended Complaint, submitted on November 6, 2002 -- one week before pretrial and "more than two years after the date of the violation with respect to which the action is brought," [42 U.S.C. § 1395dd\(d\)\(2\)\(C\)](#)-- as an attachment to the "Plaintiffs' [Rule 15](#) Motion to Amend and "Supplement Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," (dkt. no. 438).

On the eve of pretrial, the SJHSD defendants filed a [Rule 12\(b\)\(6\)](#) motion to dismiss plaintiff's EMTALA claim as asserted in the Proposed Pretrial Order on the ground of the two-year statute of limitations. (See Defendants' Motion to Dismiss Plaintiffs' EMTALA Claims, filed November 13, 2002 (dkt. no. 447); Memorandum in Support of Defendants' Motion to Dismiss Plaintiff's EMTALA Claim, filed November 13, 2002 (dkt. no. 448).)

**(A) Personal harm** Any individual who suffers personal harm as a direct result of a participating hospital's violation of a requirement of this section may, in a civil action against the participating hospital, obtain those damages available for personal injury under the law of the State in which the hospital is located, and such equitable relief as is appropriate:

**(B) [\*\*96] Financial loss to other medical facility** Any medical facility that suffers a financial loss as a direct result of a participating hospital's violation of a requirement of this section may, in a civil action against the participating hospital, obtain those damages available for financial loss, under the law of the State in which the hospital is located, and such equitable relief as is appropriate.

**(C) Limitations on actions** No action may be brought under this paragraph more than two years after the date of the violation with respect to which the action is brought.

<sup>48</sup> Plaintiffs' counsel now points to two paragraphs out of 523 in the original Complaint as invoking the EMTALA civil remedy:

365. In violation of EMPTALA [sic] and COBRA violations Mrs. Valdez was not examined, checked, asked what her problem was, nor had her temperature and blood pressure checked [\*98] while Mrs. Valdez was in such a condition.

\* \* \* \*

377. Mrs. Valdez had a right to expect an examination by a Dr. Of her choice at San Juan Hospital at the time of presentment with her malady pursuant to her insurance contracts and EMPTALA [sic] and COBRA statutes and regulations.

(Complaint (Verified), filed July 25, 2000 (dkt. no. 1), at 108-109 PP365, 377.) Besides the fact that neither paragraph accurately states an EMTALA requirement, the original Complaint makes no reference to EMTALA or COBRA in its extended statement of the plaintiffs' "Causes of Action," (*id.* at 118-154 PP443-523).

Clearly, the original Complaint did not give fair notice to the SJHSD of any claim of liability under EMTALA, even if one had been intended.

Absent leave to amend her pleadings **[\*\*99]** under [Fed. R. Civ. P. 15\(a\)](#) & [\(b\)](#), or incorporation of the claim as a triable issue in a pretrial order pursuant to [Fed. R. Civ. P. 16\(c\)](#), even taking all of Ms. Valdez' alleged facts as true, the conclusion would necessarily follow that her claim under EMTALA is time-barred.<sup>49</sup>

#### **(5) "Medicare Patient Bill of Rights" ([42 U.S.C. § 1395a](#))**

Plaintiffs' counsel points to § 1802 of Title XVIII of the Social Security Act, [42 U.S.C. § 1395a](#), as an additional footing for plaintiff Helen Valdez' claims, alleging a "violation of Mrs. Valdez' Medicare Patient Bill of Rights to see the medicare provider of her choice," and a violation of her right "to freely contract and associate with the provider of her choice as found in [42 USC 1395a](#)." (Proposed Amended Complaint at 13, 14 PP(19), (24); Proposed Pretrial Order at 5, 6 PP(20), (25).)

Concerning Medicare beneficiaries, [§ 1395a](#) provides in part:

##### **[§ 1395a](#). Free choice by patient guaranteed**

**(a) [HN37](#)[] Basic freedom of choice** Any individual entitled to insurance benefits under this subchapter may obtain health services from any institution, agency, or person qualified to participate **[\*\*100]** under this subchapter if such institution, agency, or person undertakes to provide him such services.

**[HN38](#)[]** This statute, the so-called Medicare "freedom of choice provision," reflects one of the fundamental principles upon which the Medicare program was founded, and guarantees Medicare beneficiaries the freedom to choose health care providers, who would then be paid by Medicare at the program's prescribed rates. [Section 1395a\(a\)](#) bars interference by the Secretary of Health and Human Services (or his subordinates **[\*1142]** in the administration of the Medicare program) with a beneficiary's selection of a physician.<sup>50</sup>

Nothing in the Proposed Amended Complaint or in counsel's proffers at the Pretrial Conference suggests that the Secretary, Medicare program officials -- or anyone else involved in HHS administration of Medicare benefits -- attempted to interfere with Ms. Valdez' choice of health care providers from among those qualified to participate in the Medicare program. No claim whatsoever is made that Dr. Penn **[\*\*101]** or any other qualified provider was denied Medicare payment or reimbursement for medical care provided to Ms. Valdez as an eligible Medicare recipient.

#### **(6) [42 U.S.C. § 1981](#)**

[Section 1981 of Title 42, United States Code](#) reads:

**[HN39](#)[] (a) Statement of equal rights.** All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts, to sue, be parties, give evidence, and to the full and equal benefit of all laws and proceedings for the security of persons and property as is enjoyed by white citizens, and shall be subject to like punishment, pains, penalties, taxes, licenses, and exactions of every kind, and to no other.

**(b) "Make and enforce contracts" defined.** For purposes of this section, the term "make and enforce contracts" includes the making, performance, modification, and termination of contracts, and the enjoyment of all benefits, privileges, terms, and conditions of the contractual relationship.

<sup>49</sup> Her EMTALA claim fails on its merits as well. (See *infra* at 109 & n. 81.)

<sup>50</sup> The remaining language of this section gives limited statutory authority for beneficiaries to contract for health care services, e.g., with managed care networks. [42 U.S.C. § 1395a\(b\)](#).

**(c) Protection against impairment.** The rights protected by this section are protected against impairment by nongovernmental discrimination and impairment under color of State law.

[42 U.S.C. § 1981 \(2000\)](#).<sup>51</sup> [HN40](#) [↑] [Section 1981](#) [\*\*102] addresses intentional racial discrimination in the making and enforcement of contracts: "A [§ 1981](#) ... plaintiff must prove by a preponderance of the evidence that the defendant intentionally discriminated against him or her on the basis of race." [Guides, Ltd. v. Yarmouth Group Property Mgmt., Inc.](#), 295 F.3d 1065, 1073 (10th Cir. 2002) (citing [Stewart v. Adolph Coors Co.](#), 217 F.3d 1285, 1288 (10th Cir. 2000)). As to the scope of the protection afforded by [§ 1981](#):

[HN41](#) [↑] The Supreme Court has construed the language that secures to all the same contracting rights as "white citizens" to refer only to the racial (as opposed to, say, gender-based or religious) character of the prohibited discrimination .... Whites as well as blacks may assert contract denial claims under [§ 1981](#) on the basis of race.

[\*1143] Harold S. Lewis, Jr., *Civil Rights and Employment Discrimination Law* § 1.2, at 3 (1997) (footnote omitted) (citing [McDonald v. Santa Fe Trail Transp. Co.](#), 427 U.S. 273, 49 L. Ed. 2d 493, 96 S. Ct. 2574 (1976); see also [Guides, Ltd. v. Yarmouth Group Property Mgmt., Inc.](#), 295 F.3d at 1081 n.3 (dissenting opinion) ("In this Circuit, a racial-identity is the cornerstone of a [section 1981](#) and [1982](#) cause of [\*\*103] action and a necessary element of a plaintiff's *prima facie* case. See [Shawl v. Dillards, Inc.](#), 17 Fed. Appx. 908, 2001 WL 967887, at \*2 (10th Cir. 2001) ("To establish a claim under [§ 1981](#), the plaintiffs must show that (1) they are members of a protected class ...." (citing [Hampton v. Dillard Dep't Stores, Inc.](#), 247 F.3d 1091, 1101 (10th Cir. 2001)))."). The Supreme Court understands "race" to include "ancestry," defined as genetic membership in an "ethnically and physiognomically distinctive subgrouping of *homo sapiens*." [St. Francis College v. Al-Khzraji](#), 481 U.S. 604, 613, 95 L. Ed. 2d 582, 107 S. Ct. 2022 (1987) (quoting [Al-Khzraji v. Saint Francis College](#), 784 F.2d 505, 517 (3d Cir. 1986)).

Based on the history of [§ 1981](#), we have little trouble in concluding that Congress intended to protect from discrimination identifiable classes of persons who are subjected to intentional discrimination solely because of their ancestry or ethnic characteristics. Such discrimination is racial discrimination that Congress intended [§ 1981](#) to forbid, whether or not it would be classified as racial in terms of modern scientific theory.

*Id.* (footnote omitted). However, "ancestry" as "race" -- [\*\*104] as a prohibited basis for discrimination for purposes of [§ 1981](#)-- does not embrace national origin, religion or status as an alien. [Id. at 613](#) ("If respondent on remand can prove that he was subjected to intentional discrimination based on the fact that he was born an Arab, rather than solely on the place or nation of his origin, or his religion, he will have made out a case under [§ 1981](#)."); [King v. Township of East Lampeter](#), 17 F.Supp.2d 394, 417 (E.D.Pa. 1998) ("The scope of [§ 1981](#) is not so broad as to include disparity in treatment on the basis of religion, sex, or national origin."), affirmed, 182 F.3d 903 (3d Cir.) (mem.), cert. denied, 528 U.S. 951, 120 S. Ct. 373, 145 L. Ed. 2d 291 (1999); [Vuksta v. Bethlehem Steel Corp.](#), 540 F.Supp. 1276, 1281 (E.D.Pa.1982), affirmed, 707 F.2d 1405, cert. denied, 464 U.S. 835, 104 S. Ct. 121, 78 L. Ed. 2d 119 (1983)

Thus, to state a claim under [§ 1981](#), the plaintiffs must show that (1) they are members of an identifiable racial or ancestral group; (2) the defendant had an intent to discriminate on the basis of their race or ancestry; and (3) the discrimination concerned one or more of the activities enumerated in the statute, viz., the making and enforcing of a contract. See [Green v. State Bar of Texas](#), 27 F.3d 1083, 1086 (5th Cir. 1994); [Mian v. Donaldson, Lufkin & Jenrette Securities Corp.](#), 7 F.3d 1085, 1087 (2d Cir. 1993). A [§ 1981](#) claim for. "interference with the right to make

<sup>51</sup> [42 U.S.C. § 1981 \(2000\)](#) was originally enacted as part of the [HN42](#) [↑] [Civil Rights Act of 1866, Act of April 9, 1866, ch. 31, 14 Stat. 27](#), the first of the Reconstruction Era civil rights acts, and was grounded upon the [Thirteenth Amendment](#), ratified a year earlier. The provision was re-enacted in 1870, two years after the ratification [\*\*105] of the [Fourteenth Amendment](#). See. Act of May 31, 1870, ch. 114, § 16, 16 Stat. 144. It was amended more recently by the Civil Rights Act of 1991, [Pub. L. No. 102-166, title I, § 101, 105 Stat. 1071 \(1991\)](#) (designated then-existing provisions as subsection (a) and added subsections (b) and (c)). See also [Guides, Ltd. v. Yarmouth Group Property Mgmt., Inc.](#), 295 F.3d 1065, 1080 (10th Cir. 2002) (dissenting opinion) ("The protection afforded by these statutes finds its roots in the [Thirteenth](#) and [Fourteenth Amendments](#)...." (citations omitted).)

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and enforce a contract must allege the actual loss of a contract interest, not [\*\*106] merely the possible loss of future contract opportunities." [Morris v. Office Max, Inc., 89 F.3d 411, 414-15 \(7th Cir. 1996\)](#) (citing [Phelps v. Wichita Eagle-Beacon, 886 F.2d 1262 \(10th Cir. 1989\)](#)). Moreover, "It has been held that [HN43](#) [↑] 'prudential limitations on standing ordinarily require that an action under section[] 1981 ... be brought by the direct victims of the alleged discrimination because they are best situated to assert the individual rights in question.'" [Guides, Ltd., 295 F.3d at 1072](#) (quoting [Clifton Terrace Assoc., Ltd. v. United Technologies Corp., 289 U.S. App. D.C. 121, 929 F.2d 714, 721 \(D.C.Cir. 1991\)](#)).

[\*1144] None of the allegations of the Proposed Amended Complaint plead facts that would serve as direct evidence of intentional discrimination against the Part I Plaintiffs in the making or enforcement of contracts based upon these plaintiffs' race or ancestry. See [Durham v. Xerox Corp., 18 F.3d 836, 841 \(10th Cir.\)](#) ("Without proof of pretext or direct evidence of discriminatory intent, Durham cannot meet her ultimate burden of proving intentional discrimination."), cert. denied, 513 U.S. 819, 115 S.Ct. 80, 130 L.Ed. 2d 33 (1994). Several paragraphs repeat comments allegedly [\*\*107] made by one defendant, Dr. Redd, in which he referred to Dr. Nathaniel Penn as a "little New York Jew," or words to that effect. (Proposed Amended Complaint at 53 P168(B); 58 P133(F); 59 P138; 68-69 P166.) Such comments may or may not address Dr. Penn's "ancestry" for purposes of [§ 1981](#), cf. [Shaare Tefila Congregation v. Cobb, 481 U.S. 615, 95 L.Ed. 2d 594, 107 S.Ct. 2019 \(1987\)](#) (42 U.S.C. § 1982 protects property rights of Jewish congregation in synagogue); [Singer v. Denver Sch. Dist. No. 1, 959 F. Supp. 1325, 1331 \(D.Colo. 1997\)](#), but that question is not now before this court because Dr. Penn is no longer a plaintiff in this action. (See Minute Entry, dated March 1, 2002 (dkt. no. 296).)

#### (7) [42 U.S.C. § 1985\(3\)](#)

[Section 1985\(3\) of Title 42, United States Code](#) reads:

(3) [HN44](#) [↑] **Depriving persons of rights or privileges.** If two or more persons in any State or Territory conspire or go in disguise on the highway or on the premises of another, for the purpose of depriving, either directly or indirectly, any person or class of persons of the equal protection of the laws, or of equal privileges and immunities under the laws; or for the purpose of preventing or hindering the constituted authorities [\*\*108] of any State or Territory from giving or securing to all persons within such State or Territory the equal protection of the laws; or if two or more persons conspire to prevent by force, intimidation, or threat, any citizen who is lawfully entitled to vote, from giving his support or advocacy in a legal manner, toward or in favor of the election of any lawfully qualified person as an elector for President or Vice President, or as a Member of Congress of the United States; or to injure any citizen in person or property on account of such support or advocacy; in any case of conspiracy set forth in this section, if one or more persons engaged therein do, or cause to be done, any act in furtherance of the object of such conspiracy, whereby another is injured in his person or property, or deprived of having and exercising any right or privilege of a citizen of the United States, the party so injured or deprived may have an action for the recovery of damages occasioned by such injury or deprivation, against any one or more of the conspirators.

[42 U.S.C. § 1985\(3\) \(2000\).](#) <sup>52</sup>

[HN45](#) [↑] To state a claim under [§ 1985](#), there "must be some racial, or perhaps otherwise class-based, invidiously discriminatory animus behind the conspirators' action." [Griffin v. Breckenridge, 403 U.S. 88, 102, 29 L.Ed. 2d 338, 91 S.Ct. 1790 \(1971\)](#). A plaintiff who fails to allege racial or class-based discrimination cannot state a claim under [§ 1985\(3\)](#). See [Burns v. County of King, 883 F.2d 819, 821 \(9th Cir. 1989\)](#) (citing [Bretz v. Kelman, 773 F.2d 1026, 1028 \(9th Cir. 1985\)](#) (en banc)).

[\*1145] In this case, the Part I Plaintiffs allege "civil rights violations regarding freedom to contract, free speech, free association, including 1985 conspiracy," and a "conspiracy to deprive the Plaintiffs of their legal entitlements of due process, equal protection, privacy, rights of association, rights to contract," as well as "state license

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<sup>52</sup> [Section 1985](#) was enacted as part of the [Ku Klux Klan Act of 1871, Act of April 20, 1871, ch. 22, § 2, 17 Stat. 13.](#) [\*\*109]

entitlements," "Medicaid entitlements," and even an "entitlement to a contract with the District that is based upon principles of good faith and fair dealing, with adequate consideration," (Proposed Pretrial Order at 3 P(1), 4 PP(9), (10), (12), (13) & (14)), but they do not allege discrimination against any remaining Part I Plaintiff based upon that plaintiff's race. [\*\*110]

(8) [42 U.S.C. § 1983](#)

Section 1983 of Title 42, United States Code, provides, in pertinent part:

**HN46** Every person who, under color of any statute, ordinance, regulation, custom, or usage, of any State ..., subjects, or causes to be subjected, any citizen of the United States or other person within the jurisdiction thereof to the deprivation of any rights, privileges, or immunities secured by the Constitution and laws, shall be liable to the party injured in an action at law, suit in equity, or other proper proceeding for redress, ....

[42 U.S.C. § 1983 \(2000\)](#).<sup>53</sup> **HN47** "Section 1983 provides an enforcement remedy for one who is deprived under color of state law of any rights, privileges, or immunities secured by the Constitution." *Trujillo v. Board of County Comm'r's of Santa Fe*, 768 F.2d 1186, 1189 (10th Cir. 1985). "There are two elements to a section 1983 claim: (1) the conduct must have subjected the plaintiff to a deprivation of constitutional rights," or rights protected by federal law. *Jones v. Community Redevelopment Agency*, 733 F.2d 646, 649 (9th Cir. 1984) (citing *Williams v. Gorton*, 529 F.2d 668, 670 (9th Cir. 1976)).

**HN48** Section 1983 does not specify the state of mind on the part of someone who "subjects, or causes to be subjected" a person to a deprivation of civil rights which a plaintiff must allege and prove to establish liability under the statute; the question is "did the defendant violate the plaintiff's *Fourteenth Amendment* rights? The defendant's state of mind is relevant only to the existence of the claimed *Fourteenth Amendment* violation." 1 Sheldon H. Nahmod, *Civil Rights and Civil Liberties Litigation: The Law of Section 1983* § 3:2 (4th ed. Rev. 2004) (footnote omitted).

Although this section does not require a specific state of mind for actionability, see *Parratt v. Taylor*, 451 U.S. 527, 534, 101 S.Ct. 1908, 1912, 68 L.Ed.2d 420 (1981), a court must examine closely the nature of the constitutional right asserted to determine whether a deprivation, of that right requires any particular state of mind, *McKay v. Hammock*, 730 F.2d 1367, 1373 (10th Cir. 1984) (en banc). For instance, it is well established that deprivations of equal protection require proof of discriminatory intent on the part of the state actor, see, e.g., *Washington v. Davis*, 426 U.S. 229, 96 S.Ct. 2040, 48 L.Ed.2d 597 (1976), [\*\*112] while deprivations under the *Eighth Amendment* require a showing of deliberate indifference, see, e.g., *Estelle v. Gamble*, 429 U.S. 97, 97 S.Ct. 285, [\*1146] 50 L.Ed.2d 251 (1976). Moreover, some deprivations of *First Amendment* rights require proof that the state's action was intended to repress an individual's protected speech or association. See, e.g., *Mt. Healthy City Sch. Dist. Bd. of Educ. v. Doyle*, 429 U.S. 274, 287, 97 S. Ct. 568, 576, 50 L. Ed. 2d 471 (1977); ....

*Trujillo*, 768 F.2d at 1189 (some citations omitted).<sup>54</sup>

<sup>53</sup> Like § 1985, § 1983 was originally enacted as part of the *Ku Klux Klan Act of 1871, Act of April 20, 1871, ch. 22, 17 Stat. 13.* [\*\*111]

<sup>54</sup> See 1 Nahmod, *supra*, at § 3:2:

Different *Fourteenth Amendment* violations (and hence *Bill of Rights* violations) require different states of mind, apparently because of the language and history of the applicable constitutional provisions. For example, equal protection violations

**HN49** [↑] In order to state a claim under [42 U.S.C. § 1983](#), a complaint must assert a right to recover under the Constitution or other federal laws and not be wholly insubstantial and frivolous. See, e.g., [Keniston v. Roberts](#), 717 F.2d 1295, 1298 (9th Cir. 1983).

"Conclusionary allegations, unsupported by facts, [will be] rejected as insufficient to state a claim under the Civil Rights Act." [Sherman v. Yakahi](#), 549 F.2d 1287, 1290 (9th Cir. 1977). The plaintiff must "allege with at least some degree of particularity overt acts which defendants engaged in" that support the plaintiff's claim. *Id.*, quoting [Powell v. Workmen's Compensation Board](#), 327 F.2d 131, 137 (2d Cir. 1964).

[Jones](#), 733 F.2d at 649.

Here, the Part I Plaintiffs assert civil rights "violations regarding freedom to contract, free speech, free association," and "retaliation for speaking and association," as well as the denial of due process guaranteed by the [Fourteenth Amendment](#). (Proposed Pretrial Order at 3 PP(1), (2), (3).<sup>55</sup>) They allege "interference with the patients' [\*\*114] and [plaintiffs'] ability to freely contract for services with the District, with each other, with patients as guaranteed by the [Fourteenth Amendment](#), Utah Unfair Practices Act, and federal common law," (*id.* at 4 P(8)), and as to plaintiff Helen Valdez, a denial of equal protection of the laws. (*id.* at 5 P(21).)

Whether these allegations are wholly insubstantial and frivolous, or whether they raise genuine issues requiring a trial was examined in detail by court and counsel during the Pretrial Conference. See [Fed. R. Civ. P. 16\(c\)\(1\)](#).

### [§ 1983 Conspiracy](#)

The Part I Plaintiffs also allege a "conspiracy to deprive the Plaintiffs of their legal entitlements of due process, equal protection, privacy, rights of association, rights to contract," (Proposed Pretrial Order at 4 P(13)), but they do not plead specific facts showing both conspiratorial agreement and concerted action by the named defendants.

**HN50** [↑] In order to prevail on such a claim, "a plaintiff must plead and prove not only a conspiracy, but also an actual deprivation [\*\*115] of rights; pleading and proof of one without the other will be insufficient." [\*1147] [/Dixon v. Lawton](#), 898 F.2d 1443, 1449 (10th Cir. 1990); [Snell v. Tunnell](#), 920 F.2d 673, 701 (10th Cir. 1990). In pleading conspiracy, a plaintiff must allege "specific facts showing agreement and concerted action among [the alleged co-conspirators]." [Hunt v. Bennett](#), 17 F.3d 1263, 1266 (10th Cir. 1994). "Conclusory allegations of conspiracy are insufficient to state a valid [§ 1983](#) claim." [Durre v. Dempsey](#), 869 F.2d 543, 545 (10th Cir. 1989). Thus, a plaintiff fails to state a claim for conspiracy absent specific facts showing a "meeting of the minds" among the alleged co-conspirators. See [Hunt](#), 17 F.3d at 1268.

[Marino v. Mayger](#), 118 Fed.Appx. 393, 404-405, 2004 WL 2801795, \*\*10 (10th Cir. 2004) (unpublished disposition). The Part I Plaintiffs' conclusory assertion of a conspiracy, without more, fails to state a viable claim under [§ 1983](#).

### **Liability of the SJHSD & San Juan County**

To state a colorable claim against San Juan County or the SJHSD under [§ 1983](#), the Part I Plaintiffs each must allege that a policy or custom of the County or the SJHSD was the proximate cause of the plaintiffs' constitutional injury. [\*116] See [Monell v. Dept. of Social Services](#), 436 U.S. 658, 690, 56 L. Ed. 2d 611, 98 S. Ct. 2018 (1978) **HN51** [↑] (local government may be liable under [§ 1983](#) if "the action that is alleged to be unconstitutional

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require purposeful discrimination, [Eighth Amendment](#) violations require deliberate indifference, and due process violations require more than mere negligence. The Supreme Court finally made clear the distinction between [§ 1983](#) and the underlying constitutional violation in [Parratt v. Taylor](#) when it held that, as a matter of statutory interpretation, [§ 1983](#) imposed no independent state-of-mind requirement [\*\*113] for the *prima facie* case, in contrast to state-of-mind requirements for the violation of particular constitutional provisions themselves. [Footnotes omitted.]

<sup>55</sup> Plaintiffs also assert their reliance upon a due process guarantee in the provisions of the Health Care Quality Improvement Act, [42 U.S.C. § 11112 \(2000\)](#), discussed *infra*.

implements or executes a policy, statement, ordinance, regulation or decision officially adopted and promulgated by that body's officers."). Causation presents a threshold question: "our first inquiry in any case alleging [local governmental] liability under § 1983 is the question whether there is a direct causal link between a [local governmental] policy or custom and the alleged constitutional deprivation," because "it is only when the 'execution of the government's policy or custom ... inflicts the injury'" that a local government entity may be held liable under § 1983. *City of Canton, Ohio v. Harris*, 489 U.S. 378, 385, 103 L. Ed. 2d 412, 109 S. Ct. 1197 (1989) (internal citation omitted). [HN52](#)[] Assuming that causation may be shown,

To subject a governmental entity to liability, "a municipal policy must be a 'policy statement, ordinance, regulation, or decision officially adopted and promulgated by [a municipality's] officers.'" See *Lankford v. City of Hobart*, 73 F.3d 283, 286 (10th Cir. 1996) [\*\*117] (quoting *Starrett v. Wadley*, 876 F.2d 808, 818); see also *Monell v. New York City Dep't of Social Servs.*, 436 U.S. 658, 98 S.Ct. 2018, 56 L.Ed.2d 611 (1978). Absent such an official policy, a municipality may also be held liable if the discriminatory practice is "so permanent and well settled as to constitute a 'custom or usage' with the force of law." *Lankford*, 73 F.3d at 286 (quoting *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 168, 90 S.Ct. 1598, 26 L.Ed.2d 142 (1970)).

*Murrell v. School Dist. No. 1*, 186 F.3d 1238, 1249 (10th Cir. 1999). Thus, acts that do not rise to the level of official policy may nonetheless create liability if they are "sufficiently widespread and pervasive so as to constitute a 'custom.'" *Id. at 1250*. However, conduct directed solely at a plaintiff may not "demonstrate a custom or policy" of the entity "to be deliberately indifferent" to that conduct as a general matter. *Id.* (citing *Monell*, 436 U.S. at 691 & n. 56).

[HN53](#)[] This deliberate indifference standard may be satisfied "when the municipality has actual or constructive notice that its action or failure is substantially certain to result in a constitutional violation, and it consciously and deliberately chooses [\*\*118] to disregard the risk of harm." [\*1148] *Barney v. Pulsipher*, 143 F.3d 1299, 1307 (10th Cir. 1999). Although a single incident generally will not give rise to liability, *Oklahoma City v. Tuttle*, 471 U.S. 808, 823, 105 S.Ct. 2427, 85 L.Ed.2d 791 (1985), "deliberate indifference may be found absent a pattern of unconstitutional behavior if a violation of federal rights is a 'highly predictable' or 'plainly obvious' consequence of a municipality's action." *Barney*, 143 F.3d at 1307 (internal citations omitted). The official position must operate as the "moving force" behind the violation, and the plaintiff must demonstrate a "direct causal link" between the action and the right violation. *Bd. of County Comm'r's v. Brown*, 520 U.S. 397, 399, 117 S.Ct. 1382, 137 L.Ed.2d 626 (1997).

*Olsen v. Layton Hills Mall*, 312 F.3d 1304, (10th Cir. 2002).

Plaintiffs contend that "the County and District had a de facto policy of deliberate indifference to those who complained of suffering from Dr. Redd and other District staff members," and that "the County and District had a policy of harming the reputations of persons in retaliation for challenging their authority." (Proposed Pretrial Order at 20-21 P52-53; see Proposed [\*\*119] Amended Complaint at 34 PP52-53 (same)). In the Proposed Amended Complaint, they allege that the SJHSD administrators and Board members, as well as the County Commissioners, County Administrator and County Attorney "behaved in a deliberately indifferent manner, failed to adequately investigate the problems Mrs. Lyman and Dr. MacArthur identified in the District, did not hold hearings on the matters, did not enforce, or take any actions to rectify the situations identified by Mrs. Lyman and Dr. MacArthur." (Proposed Amended Complaint at 16-17.) "A pattern of deliberated indifference as a policy was exhibited by the County Commission, County Attorney, Health District board, administrators and medical staff." (*Id.* at 17.) <sup>56</sup>

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<sup>56</sup> More recently, counsel argued that "[a] repeated pattern of a government entity's conduct is a *de facto* 'silent' policy enabling [individual defendants] to *ultra vires* arbitrarily deny a plaintiff of his liberty and property rights," that "careful or heightened scrutiny attaches when these liberty and property rights are compromised by government," and that the federal civil rights acts are "designed to specifically cure a situation wherein the officials refuse [\*\*120] to enforce provisions of the law." (Memorandum in Support of Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), at 5 (citing *Planned Parenthood of Southeastern Pa. v. Casey*, 505 U. S. 833, 120 L. Ed. 2d 674, 112 S. Ct. 2791 (1992), and *Monell v. Dep't of Soc. Servs.*, 436 U.S. 658, 56 L. Ed. 2d 611, 98 S. Ct. 2018(1978)).)

Of course, [HN54](#)<sup>↑</sup> the policy "causation" question presupposes that a deprivation of constitutional rights has occurred; if there was no deprivation, the policy or custom is immaterial. Before the Part I Plaintiffs can plead and prove an arguable legal claim against San Juan County or the SJHSD for liability under [§ 1983](#), they first must allege "the deprivation of [a] right[], privilege[], or immunity secured by the Constitution and laws." [42 U.S.C. § 1983](#).

For the reasons explained hereafter, on the factual allegations now before the court, Dr. MacArthur suffered no arguable deprivation of a constitutional "liberty" or "property" interest, or other federally protected right. See *infra* at 83-94. Likewise, for reasons explained hereafter, [\[\\*121\]](#) Ms. Lyman has not alleged facts showing such a deprivation. See *infra* at 94-105. Finally, Ms Valdez asserts that--as a woman of advancing years, married to a Mexican-American husband--being refused examination [\[\\*1149\]](#) and treatment at an emergency room denies her the equal protection of the laws guaranteed by the [Fourteenth Amendment](#), yet, as examined in greater detail below, the specific facts pleaded and proffered in support of her claim show *no* actual refusal or denial of examination or treatment on the date in question, and therefore prove insufficient to raise a genuine issue as to constitutional deprivation that would require a trial. See *infra* at 106-111.

#### **Plaintiffs' [§ 1983](#) Claims Against the County Commissioners & SJHSD Board Members**

In the Proposed Amended Complaint, the plaintiffs alleged that the SJHSD "Board members and County Commissioners ... behaved in a deliberately indifferent manner; failed to adequately investigate the problems Mrs. Lyman and Dr. MacArthur identified in the District, did not hold hearings on the matters, did not enforce, or take any actions to rectify the situations identified by Mrs. Lyman and Dr. MacArthur." (Proposed Amended Complaint at 16-17.) The plaintiffs [\[\\*122\]](#) characterize the SJHSD Board's inaction on their grievances as "[a] pattern of deliberated indifference as a policy" that "was exhibited by the County Commission, County Attorney, Health District board, administrators and medical staff." (*Id.* at 17; see also *id.* at 21 ("The County and District ... evidenced a pattern of deliberate indifference to [plaintiffs'] plight."); *id.* at 87 P237 ("The Health District and the County did not did not reprimand Dr. Redd or any other medical staff member for their treatment of Mrs. Lyman or Dr. MacArthur, or Helen Valdez.").) As noted above, plaintiffs also asserted at pretrial that "the County and District had a de facto policy of deliberate indifference to those who complained of suffering from Dr. Redd and other District staff members." (Proposed Pretrial Order at 21 P52.)

#### **Vicarious Liability, Respondeat Superior & [§ 1983](#)**

The defendants respond that "with respect to each of the plaintiffs' discrimination and due process claims, San Juan County, the Health District, Roger Atcity, John Lewis, John Housekeeper, Karen Adams, Patsy Shumway and Gary Holliday are not liable because respondeat superior liability does not attach for purposes of [42 U.S.C. § 1983](#) [\[\\*123\]](#) unless the adverse treatment resulted from a policy or custom of the Health District, of which there is no evidence in this case." (Proposed Pretrial Order at 7 Pvii.)

It has long been understood that [HN55](#)<sup>↑</sup> "the doctrine of respondeat superior was not applicable to render a supervisor or other superior liable under [§ 1983](#) for the unconstitutional conduct of his subordinates." 1 Sheldon H. Nahmod, *Civil Rights and Civil Liberties Litigation: The Law of Section 1983* § 3:90, at 3-330 (4th ed. rev. 2004) (footnotes omitted); see [Draeger v. Grand Central, Inc.](#), *504 F.2d 142, 145 (10th Cir. 1974)* ("Generally speaking, the doctrine of vicarious liability or respondeat superior has been ruled out in cases arising under the Federal Civil Rights statutes."). [Monell v. Dept. of Social Services](#), *436 U.S. 658, 56 L. Ed. 2d 611, 98 S. Ct. 2018 (1978)*, clearly holds that vicarious liability under the doctrine of respondeat superior "cannot be applied either to superiors or to local government entities" under [§ 1983](#), under any circumstances. 1 Nahmod, *supra*, at § 3:91, at 3-332 (emphasis in original; footnote omitted). Instead, *Monell* held that local governmental entities "are suable persons under [§ 1983](#) [\[\\*124\]](#) and can be held liable for *their* unconstitutional policies, practices and customs." *Id.* (emphasis in original).

[\[\\*1150\]](#) Consequently, in light of *Monell*, . . . [HN56](#)<sup>↑</sup> the superior does not and should not invariably have a [§ 1983](#) duty, solely by reason of position, to compensate a person whose constitutional rights have been violated by subordinates. What is currently required in order for the superior to have such a duty is that the superior personally either acted unconstitutionally or with deliberate indifference. That is, the superior must

have possessed either the state of mind for the particular constitutional violation or deliberate indifference, and *must also have played a causal role in plaintiff's constitutional deprivation.*

*Id.* (emphasis added & footnote omitted). [HN57](#) [Section 1983](#) addresses conduct which "subjects, or causes to be subjected" the plaintiff to a deprivation of civil rights, requiring pleading and proof of a causal connection between a defendant's conduct and the constitutional deprivation suffered by the plaintiff. See [Rizzo v. Goode, 423 U.S. 362, 376-377, 46 L. Ed. 2d 561, 96 S. Ct. 598 \(1976\)](#) ("the responsible authorities had played no affirmative part in depriving any members [\[\\*\\*125\]](#) of the two respondent classes of any constitutional rights").

Thus, theories of vicarious liability are not available to [§ 1983](#) plaintiffs. "Only the direct acts or omissions of government officials, not the acts of subordinates, will give rise to individual liability under [§ 1983](#)." [Coleman v. Houston Indep. Sch. Dist., 113 F.3d 528, 534 \(5th Cir. 1997\)](#). Where an official becomes aware of a constitutional violation only after the fact, he or she cannot be held liable for the violation under [§ 1983](#) because the violation has already occurred and the official played no causal role in it. See [Schultz v. Baumgart, 738 F.2d 231, 238-239 \(7th Cir. 1984\)](#). Thus, "some personal involvement of the supervisory official in the subordinate's unconstitutional conduct -- analogous to *Monell*'s official policy or custom requirement for local government liability -- must be shown for [§ 1983](#) liability." 1 Nahmod, *supra*, § 6.6, at 6-24 (emphasis in original). See Annotation, *Vicarious Liability of Superior Under 42 USCS § 1983 for Subordinate's Acts in Deprivation of Civil Rights*, 51 A.L.R. Fed. 285 (1981 & Supp. 2004), and cases cited therein.

The Part I Plaintiffs plead the language of "deliberate indifference," [\[\\*\\*126\]](#) "pattern," and "policy," but allege no specific facts showing that the individual SJHSD Board members knew of or directly instigated any denial [HN58](#) [\[\\*\\*126\]](#) of constitutional due process or other actionable deprivation by SJHSD medical and support staff members; nor do they assert that the alleged violations were directly effected pursuant to an existing policy or custom instituted by each Board member named as a defendant. Instead, plaintiffs contend that the SJHSD Board members owed an affirmative duty to provide the plaintiffs with post- deprivation relief--that is, a duty after the fact to investigate matters that the plaintiffs complained of, to "find and hold accountable the responsible parties," and to thereby "resolve the provider and patients' and public's concerns." Cf. 1 Nahmod, *supra*, § 6:6 at 6-24 ("Plaintiffs may be expected to try to fit local government failure to act cases into *Monell*'s category of official policy or custom.")

Plaintiffs have not cited to pertinent authority establishing such an affirmative duty on the part of senior public officials to vindicate plaintiffs' interests in that fashion--the breach of which would render the County Commissioners or SJHSD Board members [\[\\*\\*127\]](#) individually liable to plaintiffs under [§ 1983](#). Absent such authority, the court has discerned no basis in the law or policy of [§ 1983](#) for finding the existence of such an affirmative duty. See generally [\[\\*1151\] Baker v. McCollan, 443 U.S. 137, 61 L. Ed. 2d 433, 99 S. Ct. 2689 \(1979\)](#) (sheriff has no affirmative duty under [§ 1983](#) to investigate arrestee's claims of innocence and mistaken identity).

Even assuming that plaintiffs' claims of due process violations or discrimination by SJHSD medical or support staff could be proven, holding the County Commissioners and SJHSD Board members individually liable for failing to vindicate the plaintiffs' interests *after the fact*-- failing to investigate their complaints, "not holding hearings on the matters," and not "taking any actions to rectify the situations identified by Mrs. Lyman and Dr. MacArthur"-- would attach [§ 1983](#) liability to *post hoc* conduct that can bear no causal relationship to the alleged constitutional deprivations themselves. Remembering that [§ 1983](#) imposes liability only upon one who "subjects, or causes to be subjected" a person to a constitutional deprivation, the requirement that a plaintiff must demonstrate a "direct causal [\[\\*\\*128\]](#) link" between the defendant's conduct and the civil rights violation, [Bd. of County Comm 'rs v. Brown, 520 U.S. 397, 399, 137 L. Ed. 2d 626, 117 S. Ct. 1382 \(1997\)](#), would appear to preclude the imposition of [§ 1983](#) liability upon the County Commissioners and the SJHSD Board members based upon the "failure to vindicate" theory urged by the Part I Plaintiffs.

**The SJHSD Board & the SJHSD Medical Staff's "Policy" re: Physician Assistants**

Referring to the SJHSD medical staff's alleged adoption in 1999 of a staff "policy" requiring Physician Assistants exercising SJHSD staff privileges to be supervised by a local physician having SJHSD staff privileges,<sup>57</sup> plaintiffs complain that "while the [Physician Assistant] policies in question appear to be facially neutral, in application they applied only to Mrs. Lyman and were not approved by the District Board. However, [\*1152] *the District Board knew of them and did nothing to stop them from being used to prevent Mrs. Lyman's practice.*" (Proposed Amended Complaint at 22 (emphasis added).)"<sup>58</sup>

Ms. Lyman's contention that the 1999 staff "policy" re: local supervision (or the other alleged "denials" of privileges of which she complains) resulted in a constitutional deprivation under [§ 1983](#) presupposes that she had a constitutional right to exercise practice privileges at SJHSD facilities free of any such limitation or restraint imposed by the **[\*\*131]** SJHSD medical staff.

#### **Qualified Immunity & Plaintiffs' [§ 1983](#) Claims**

In the Proposed Pretrial Order, the defendants asserted that

because San Juan County and the Health District are political subdivisions of the State of Utah and the alleged acts and/or omissions by County commissioners, officials or employees or Health District trustees, employees or staff members, about which plaintiffs complain, were carried out within the scope of and pursuant to their official duties as trustees, employees or staff members of the Health District, plaintiffs' claims are barred by the doctrine of qualified immunity,

as well as "the provisions of the Utah Governmental Immunity Act, Utah Code Ann. § 63-30-1 *et seq.*, including but not limited to § 63-30-3 and § 63-30-10." (Proposed Pretrial Order at 10-11 Pxxxvi.)

The Supreme Court has held that [HN59](#) [↑] "government officials performing discretionary functions generally are shielded from liability from civil damages insofar as their conduct does not violate clearly established statutory or

<sup>57</sup> Plaintiff Lyman alleges:

31. Though Dr. Penn and Dr. Mena were staff members, Michele Lyman did not enjoy full privileges while supervised by them.

32. Dr. Redd **[\*\*129]** and Dr. Jones and Dr. Cook and Dr. Nelson did not approve Mrs. Lyman having privileges unless her doctor was a medical staff member and then only if the physician was in the same town as she.

33. While the policy for P.A.s appears neutral, it effected only Michele Lyman in how it was applied, monitored, and carried out.

\* \* \* \*

209. Dr. Penn and Ms. Lyman attended the Medical staff Meeting for June, 1999. Dr. Penn and Ms. Lyman requested full privileges be restored and Dr. Redd and Jones both stated that only if Dr. Penn was willing to sit in Blanding with Ms. Lyman while Ms. Lyman took ER call and they would not supervise me. Mr. Bryant as a P.A. working under Dr. Jones while Dr. Jones was not in Blanding, had no such restraints. Mrs. Lyman pointed out that she covered the ER (Blanding urgent care clinic) in Blanding by herself on many occasions. There was no response. (Cmplt. 137-145) Staff had previously voted for her privileges and then the County, Board, and medical staff did nothing while District staff Ora Lee Black, Dr. Redd, Gloria Yanito denied her the same. Some privileges as to labs and xrays were eventually restored.

(Proposed Amended Complaint at 31 PP31-33; 78 P209; see **[\*\*130]** Proposed Pretrial Order at 18 PP31-33; 54 P209 (same).)

Recounting that the medical staff "passed a policy saying in order to have privileges your supervising physician has to be in the same town," Ms. Lyman's counsel asserted that she did not see "where the governing board adopted that policy so it was an action taken by medical staff but under the bylaws the governing board is the body that sets the policy." (Tr. 11/15/02, at 15:7-24 (Ms. Rose).) Apparently the argument is that the SJHSD Board adopted a "policy" of letting the medical staff make "policy" concerning Physician Assistants' staff privileges, but that it did so without any formal Board action.

<sup>58</sup> Plaintiffs also allege that "as a policy and pattern of practice, those who inform those in power of problems are subjected to reputation assassination within the area." (*Id.* at 17.)

constitutional rights of which a reasonable person would have known." [Harlow v. Fitzgerald, 457 U.S. 800, 818, 73 L. Ed. 2d 396, 102 S. Ct. 2727 \(1982\)](#). This grant of immunity [\*\*132] is intended to balance two competing interests. On the one hand, when an official abuses his office, "an action for damages may offer the only realistic avenue for vindication of constitutional guarantees." [Id. 457 U.S. at 814](#). On the other hand, exposing government officials to damages suits "entails substantial social costs," [Anderson v. Creighton, 483 U.S. 635, 638, 97 L. Ed. 2d 523, 107 S. Ct. 3034 \(1987\)](#), such as "the expenses of litigation, the diversion of official energy from pressing public issues, . . . the deterrence of able citizens from acceptance of public office . . . [and the deterrence of public officials from] 'the unflinching discharge of their duties.'" [Harlow, 457 U.S. at 814](#). "The Supreme Court has attempted to strike the balance between these two concerns by shielding government officials from suits for civil damages 'insofar as their conduct does not violate clearly established statutory or constitutional rights of which a reasonable person would have known.'" [Lawrence v. Reed, 406 F.3d 1224, 1230 \(10th Cir. 2005\)](#) (quoting [Harlow, 457 U.S. at 818](#)). "Although courts have derived from this statement a variety of multi-part tests, the essential inquiry is: would an [\*\*133] objectively reasonable official have known that his conduct was unlawful?" [Id.](#) (citing [Anderson v. Creighton, 483 U.S. at 640](#)).

**HN60** [↑] In the Tenth Circuit, we employ a three-step inquiry. See [Roska ex rel. Roska v. Peterson, 328 F.3d 1230, 1239-40, 1247, 1251 \(10th Cir. 2003\)](#). First, we ask "whether the plaintiff's allegations, if [\*1153] true, establish a constitutional violation." [Id. at 1239-40](#). If not, the suit is dismissed; if so, we move to the second step: "whether the law was clearly established at the time the alleged violations occurred." [Id. at 1247](#). This step gives the official an opportunity to show that he "neither knew nor should have known of the relevant legal standard" because the law was not clearly established at the time he acted. [Harlow, 457 U.S. at 819, 102 S.Ct. 2727](#). Where the law is not clearly established, courts do not require officials to anticipate its future developments, and qualified immunity is therefore appropriate.

If the law was clearly established, we reach the third step of the inquiry: whether, in spite of the fact that the law was clearly established, "extraordinary circumstances"--such as reliance on the advice of counsel or on a statute--"so 'prevented' [\*\*134] [the official] from knowing that his actions were unconstitutional that he should not be imputed with knowledge of a clearly established right." [Roska, 328 F.3d at 1251](#). This occurs only "rarely." [Id.](#)

*Id.* <sup>59</sup> **HN61** [↑] Whether an official is protected by qualified immunity thus turns upon the objective legal reasonableness of the action, in light of legal rules clearly established at the time the action was taken. <sup>60</sup> The contours of the right allegedly violated must be sufficiently clear so that a reasonable official would understand that what he or she is doing violates that right. [Anderson v. Creighton, 483 U.S. 635, 639, 97 L. Ed. 2d 523, 107 S. Ct. 3034 \(1987\)](#). "This is not to say that an official action is protected by qualified immunity unless the very action in question has previously been held unlawful, . . . but it is to say that in light of pre-existing law that unlawfulness must be apparent." [Hope v. Pelzer, 536 U.S. 730, 739, 153 L. Ed. 2d 666, 122 S. Ct. 2508 \(2002\)](#) (quoting [Anderson v. Creighton, 483 U.S. at 640](#)) (internal citation omitted). Thus, if prior case law provides "fair warning"

<sup>59</sup> **HN62** [↑] Once a defendant raises a the defense of qualified immunity, "the burden shifts to the plaintiff [to] satisfy a heavy two-part burden" to "demonstrate that the defendant violated a constitutional or statutory right[,] and "that the right at issue was clearly established at the time of the defendant's unlawful conduct." [Gross v. Pirtle, 245 F.3d 1151, 1155, 1156 \(10th Cir. 2001\)](#). If the plaintiff cannot make both showings, the defendant is entitled to qualified immunity; if he can, the burden shifts to the defendant "to prove that there are no genuine issues of material fact and that he or she is entitled to judgment as a matter of law." [Id. at 1156](#).

<sup>60</sup> The Supreme Court has expressly held that **HN63** [↑] qualified immunity is governed by an objective reasonableness standard, and that "evidence concerning the defendant's subjective intent is simply irrelevant to that defense." [Crawford-El v. Britton, 523 U.S. 574, 588, 140 L. Ed. 2d 759, 118 S. Ct. 1584 \(1998\)](#).

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that an officer's conduct would violate the plaintiff's constitutional rights, "officials [\*\*135] can still be on notice that their conduct violates established law even in novel factual circumstances." *Id. at 739-740, 741.*<sup>61</sup>

It is important to note that [HN65](#) qualified immunity "establishes a right not to be tried." *Elliott v. Thomas, 937 F.2d 338, 341 (7th Cir. 1991)*. Accordingly, the [\*1154] courts often find it appropriate to make a determination on this issue prior to commencement of trial.

"The 'entitlement [to qualified immunity] is an immunity from suit rather than a mere defense to liability; and like an absolute immunity, it is effectively lost if a case is erroneously permitted to go to trial.'" *National Commodity and Barter Association v. Archer, 31 F.3d 1521, 1532 n. 8 (10th Cir. 1994)* (quoting *Mitchell v. Forsyth, 472 U.S. 511, 526, 86 L. Ed. 2d 411, 105 S. Ct. 2806 (1985)*).

[Chavez v. City of Albuquerque, 402 F.3d 1039, 1044 \(10th Cir. 2005\)](#).

#### Dr. MacArthur's [§ 1983](#) Claim

#### Dr. MacArthur's [\*137] "Right" to Practice at SJHSD Facilities

Counsel asserts that "Dr. MacArthur's ability to practice medicine entering into patient contracts which are property constitutes a liberty and property right," relying on an oft-quoted passage from the Declaration of Independence and an excerpt from Justice Bradley's dissenting opinion in *The Slaughter-House Cases, 83 U.S. (16 Wall.) 36, 21 L. Ed. 394 (1873)*, referring to the right to pursue a common calling.<sup>62</sup> (Memorandum in Support of Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), at 4-5.) In counsel's view, this "liberty and property right" to practice medicine amounts to a *carte blanche* entitlement to full practice privileges at county-sponsored hospital and clinical facilities. Counsel elaborated on this view at the Pretrial Conference:

THE COURT: Okay. Now what's, what's Dr. MacArthur complaining about?

MS. ROSE: He's complaining about one, he had, he had a medical license that allowed him privileges.

THE COURT: Well you don't get privileges as a matter [of] course do you?

MS. ROSE: I think that when [\*138] you're, I think that when there is a Congressional policy for encouraging people, providers to go to rural areas to increase competition in those areas and so forth.

THE COURT: But the hospital as a hospital grants privileges and denies privileges or revokes privileges?

MS. ROSE: And that's, that's the key question here Your Honor. He has, I mean they're not claiming that I'm aware of that he was unqualified to work there, they're claiming that those 2 documents weren't in his file. Dr. Redd said he saw the documents.

\* \* \* \*

<sup>61</sup> According to the court of appeals, [HN64](#) "In order for the law to be clearly established there must have been [\*136] a Supreme Court or other Tenth Circuit decision on point so that 'the contours of the right [were] sufficiently clear that a reasonable official would understand that what he is doing violates that right.' *Finn v. N.M., State Pers. Office, 249 F.3d 1241 (10th Cir. 2001)* at 1250 (quoting *Anderson v. Creighton, 483 U.S. 635, 640, 107 S.Ct. 3034, 97 L.Ed.2d 523 (1987)*)." *McFall v. Bednar, 407 F.3d 1081, 2005 WL 1023433 (10th Cir. 2005)*.

<sup>62</sup>

This right to choose one's calling is an essential part of that liberty which it is the object of government to protect; and a calling, when chosen, is a man's property right.... A law which prohibits citizens ... from adopting a lawful employment, or from following a lawful employment previously adopted, does deprive them of liberty as well as property, without due process of law.

[83 U.S. \(16 Wall.\), at 116, 122](#) (Bradley, J., dissenting); see Tr. 11/14/02 at 28:11-23 (Ms. Rose) (quoting Justice Bradley's dissenting opinion, [\*140] [83 U.S. \(16 Wall.\) at 120](#)).

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THE COURT: Well no one says that you're entitled to have hospital privileges. Show me a provision that says that you're entitled, as a matter of right to have hospital privileges?

MS. ROSE: Well here's another way of rephrasing that. Where is the provision that allows a tax supported publicly funded district to prohibit an otherwise [\*1155] qualified physician from using the facilities for these patients and I think that's more of the crux of it.

We've got, we've, you know, the district's powers are limited by statute. Where's the statute that allows this district to deny and limit the powers and rights and privileges that Dr. MacArthur gets from having that medical license[?].

\* [\*\*139] \* \* \*

THE COURT: Yes. The fact that you have a medical license doesn't give you automatically hospital privileges. You've got to have a different kind of relationship established.

MS. ROSE: And what right, what statutory source allows the hospital to maintain a monopoly or attempt to maintain a monopoly and reserve its privileges to those they arbitrarily and capriciously choose to bestow them upon[?]

Nothing, there is no source for a publicly funded tax supported hospital accepting Medicare and Medicaid to do so because to do so deprives the Medicare patients in the area of the right to choose who their providers are.

(Tr. 11/14/02, at 19:7-23, 24:13-25:1, 28:24-29:10.)

As counsel suggests, [HN66](#)<sup>63</sup> the [\*Fourteenth Amendment's\*](#) "liberty" guarantee includes an individual's right "to engage in any of the common occupations of life":

"While this court has not attempted to define with exactness the liberty ... guaranteed (by the [\*Fourteenth Amendment\*](#)), the term has received much consideration and some of the included things have been definitely stated. Without doubt, it denotes not merely freedom from bodily restraint but also the right of the individual to contract, to engage in any of the common occupations of life, to acquire useful knowledge, to marry, establish a home and bring up children, to worship God according to the dictates of his own conscience, and generally to enjoy those privileges long recognized ... as essential to the orderly pursuit of happiness by free men." [\*Meyer v. Nebraska\*, 262 U.S. 390, 399, 43 S.Ct. 625, 626, 67 L.Ed. 1042](#). In a Constitution for a free people, there can be no doubt that the meaning of 'liberty' must be broad indeed. See, e.g., [\*Bolling v. Sharpe\*, 347 U.S. 497, 499-500, 74 S.Ct. 693, 694, 98 L.Ed. 884](#); [\*Stanley v. Illinois\*, 405 U.S. 645, 92 S. Ct. 1208, 31 L. Ed. 2d 551](#) (1972).

[\*Board of Regents of State Colleges v. Roth\*, 408 U.S. 564, 572, 33 L. Ed. 2d 548, 92 S. Ct. 2701](#) (1972) [\*\*141] (quoting [\*Meyer v. Nebraska\*, 262 U.S. 390, 399, 67 L. Ed. 1042, 43 S. Ct. 625](#) (1923)).<sup>63</sup> As the Fifth Circuit more recently elaborated in [\*Martin v. Memorial Hosp. at Gulfport\*, 130 F.3d 1143](#) (5th Cir. 1997):

[HN67](#)<sup>63</sup> "The [\*Due Process Clause\*](#) ... protects an individual's liberty interest which is viewed as including an individual's freedom to work and earn a living and to establish a home and position in one's community." [\*Cabrol v. Town of Youngsville\*, 106 F.3d 101](#) (5th Cir. 1997), citing [\*1156] [\*Roth, supra, 408 U.S. at 572, 92 S.Ct. at 2706-07\*](#). "It requires no argument to show that the right to work for a living in the common occupations of the community is of the very essence of the personal freedom and opportunity that it was the purpose of the [fourteenth] Amendment to secure." [\*Phillips v. Vandygriff\*, 711 F.2d 1217, 1222](#) (5th Cir. 1983), quoting [\*Truax v. Raich\*, 239 U.S. 33, 41, 36 S.Ct. 7, 10, 60 L.Ed. 131](#) (1915). See also: [\*Meyer v. Nebraska\*, 262 U.S. 390, 399, 43 S.Ct. 625, 626, 67 L.Ed. 1042](#) (1923) ("Without doubt, ['liberty' in the [\*fourteenth amendment\*](#)] denotes

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<sup>63</sup> Thomas M. Cooley, *A Treatise on the Constitutional Limitations which rest upon the Legislative Power of the States of the American Union* 824 (8th ed. 1927):

"Liberty" as used in [the Due Process] clause denotes not merely freedom from bodily restraint but also the right of the individual to contract, to engage in any of the common occupations of life, to acquire useful knowledge, to marry, to establish a home and bring up children, to worship God according to the dictates of his own conscience, and generally to enjoy those privileges long recognized at common law as essential to the orderly pursuit of happiness by free men. [Footnote omitted.]

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not merely freedom from bodily restraint but also the right of the individual to contract, to engage in any of the common occupations [\*\*142] of life ..."); and *Schware v. Board of Bar Examiners*, 353 U.S. 232, 238-39, 77 S.Ct. 752, 756, 1 L.Ed.2d 796 (1957) ("A state cannot exclude a person from the practice of law or from any other occupation ... for reasons that contravene the Due Process or *Equal Protection Clause of the Fourteenth Amendment*.").

*Id.* at 1148.

Nonetheless, **HN68**[<sup>64</sup>] a physician's "liberty" interest in pursuing his or her professional practice and establishing a home and position in" a particular community does not *per se* entitle the physician to exercise plenary staff privileges [\*\*143] at public hospitals or medical facilities. To the contrary, "Suits by physicians who have been denied hospital staff privileges are not new. It has been clearly established for years that a doctor has no constitutional right to the staff privileges of a hospital merely because he is licensed to practice medicine. *Hayman v. Galveston*, 273 U.S. 414, 47 S. Ct. 363, 71 L. Ed. 714 (1927)." *Sosa v. Board of Managers of Val Verde Mem. Hosp.*, 437 F.2d 173, 175 (5th Cir. 1971).<sup>64</sup> Generally, a physician is limited to assertion of a substantive due process right not to be excluded from staff privileges except for reasons related to the operation of the hospital which are not arbitrary or capricious, and a right to procedural due process sufficient to ensure that the physician has an opportunity to demonstrate that the exclusion is not justified. See *Woodbury v McKinnon*, 447 F.2d 839, 842 (5th Cir. 1971); *Sosa v. Board of Managers of Val Verde Mem. Hosp.*, 437 F.2d at 176-177; Sarasota Cty Pub Hosp Bd v Shahawy, 408 So.2d 644, 646-647 (Fla. 1981).

Absent the recognition of a *per se* right to pursue medical practice through the exercise of full staff privileges at government-sponsored medical facilities, the SJHSD's exercise of supervisory power to grant, limit or deny practice privileges at those facilities--by requiring physicians to apply for and obtain privileges under the medical staff bylaws--did not deny a substantive constitutional "liberty and property right" to practice medicine or to make contracts with patients for his professional services.<sup>65</sup>

**HN69**[<sup>64</sup>] [\*1157] A physician's liberty interest in pursuing a professional practice raises *procedural* due process concerns with respect to the grant or denial of staff privileges at a public hospital or medical facility once a request for such privileges has been made.

### Dr. MacArthur's Request for Privileges & Procedural Due Process

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<sup>64</sup> In *Hayman*, the Court stated that

the only protection claimed here is that of appellant's privilege to practice his calling. However extensive that protection [\*\*144] may be in other situations, it cannot, we think, be said that all licensed physicians have a constitutional right to practice their profession in a hospital maintained by a state or a political subdivision, the use of which is reserved for purposes of medical instruction. It is not incumbent on the state to maintain a hospital for the private practice of medicine.

*Hayman v. City of Galveston*, 273 U.S. 414, 416-417, 71 L. Ed. 714, 47 S. Ct. 363 (1927).

<sup>65</sup> Justice Sutherland's opinion in *Adkins v. Children's Hospital*, 261 U.S. 525, 67 L. Ed. 785, 43 S. Ct. 394 (1923), cited by plaintiffs, extolls the virtue of freedom of contract, but does so in the context of state legislation prescribing [\*\*145] minimum wages for women and children in private employment, without reference to the pursuit of a particular line of employment. See *id. at 545-546* ("the right to contract about one's affairs is a part of the liberty of the individual protected by this [Due Process] clause," and although "there is, of course, no such thing as absolute freedom of contract[,] ... freedom of contract is, nevertheless, the general rule, and restraint the exception, and the exercise of legislative authority to abridge it can be justified only by the existence of exceptional circumstances"), overruled by *West Coast Hotel Co. v. Parrish*, 300 U.S. 379, 81 L. Ed. 703, 57 S. Ct. 578 (1937). The Court has long since abandoned *Adkins'* expansive view of freedom of contract. See *Planned Parenthood of Southeastern Pennsylvania v. Casey*, 505 U.S. 833, 860, 120 L. Ed. 2d 674, 112 S. Ct. 2791 (1992).

Dr. MacArthur's [\*\*146] [§ 1983](#) claim also attempts to raise an issue of *procedural* due process concerning a right to notice and hearing concerning his December 1999 request for full provisional privileges at SJHSD facilities:

MS. ROSE: All right. This is what the crux of it is. There was no due process, there was no notice. He was never told there was a problem. He was never given an opportunity to rectify the problem. There's no, by the bylaws there's no hearing process available for physicians that have temporary privileges. He was given no hearing basis except that, you know, he was not told any time in advance that this February 2nd hearing was going to be held to discuss his staff privileges.

(Tr. 11/14/02, at 20:25-21:8 (Ms. Rose).) <sup>66</sup> Counsel referred to a February 2, 2000 SJHSD staff meeting at which it is alleged that Dr. MacArthur's December 1999 request for privileges was discussed, but no formal action was taken. Dr. MacArthur was not present for the February 2 meeting; he had accompanied his wife out of town for a medical procedure. (See Tr. 11/14/02, at 11:13-19 (Ms. Rose).) SJHSD's executive director, Cleal Bradford, also was not in attendance. Mr. Bradford's signature would have been required [\*\*147] for any grant of provisional privileges or any further extension of Dr. MacArthur's "temporary" privileges beyond their February 2 expiration date. (See Tr. 11/14/02, at 16:1-21, 17:25-18:16 (Ms. Rose).)

[\*1158] According to the facts alleged by the plaintiffs, the SJHSD had neither granted nor denied Dr. MacArthur's request for full provisional privileges as of February 2, 2000, when his "temporary" privileges expired; the matter was tabled pending the receipt of further documentation. At that point, as counsel explained, Dr. MacArthur moved his practice to Ely, Nevada. (Tr. 11/14/02, at 18:17-19:6 (Ms. Rose).)

THE COURT: After his temporary hospital privileges expired what did he do in reference to having that issue be examined?

MS. ROSE: At that point he left.

THE COURT: He went to Ely?

MS. ROSE: Starting May 1st I believe.

(*Id.* at 25:22-26:2.) According to counsel, Dr. MacArthur chose to go to Ely, Nevada, because the situation in San Juan County "was so inhospitable." (*Id.* at 26:12-21 (Ms. Rose); see *id.* [\*\*149] at 37:8-38:8 (Ms. Cox).) "The working conditions in the area were so hostile, not only to him but to his patients that he felt he had no alternative but to leave ...." (*Id.* at 42:20-23 (Ms. Rose).)

Whether an environment is hospitable or hostile is a matter of perception, based upon an aggregation of circumstances and events. Taking plaintiffs' factual allegations as true, it appears that in providing medical care to his patients at SJHSD facilities, Dr. MacArthur experienced several unpleasant and frustrating instances involving a lack of sterile and functional medical instruments; conduct on the part of SJHSD nurses or staff that was disrespectful, ill-mannered, rude, and at times, unprofessional; and he became the subject of disparaging rumors circulated among the SJHSD support staff by a few antagonists, rumors that threatened to injure his personal

<sup>66</sup> In arguing the denial of procedural due process, Dr. MacArthur's counsel retreated somewhat from her substantive due process theory:

THE COURT: Okay. Well your idea is that in rural areas a doctor with a medical degree and a medical license has unrestricted power to practice in a local hospital?

MS. ROSE: No, Your Honor, it is subject to what is called peer review. It is subject to notice and due process and that's verified in [42 U.S.C. § 11112](#) ....

Tr. 11/14/02, at 31:25-32:5.) In counsel's view, the Health Care Quality Improvement Act, [42 U.S.C. § 11112](#), discussed *supra*, "requires that if you're going to limit or deny privileges to a doctor you do it with adequate and fair notice and due process." (Tr. 11/14/02, at 33:7-9 (Ms. Rose).) As noted above, § 411 of the HCQIA, [42 U.S.C. § 11111](#), encourages the use of peer review procedures in supervising physicians' practice privileges by immunizing the review participants from civil liability arising from a review action (with specific exceptions) [\*\*148] if that action meets [§ 11112](#)'s procedural criteria. The HCQIA does not impose due process *requirements* on hospitals and health care facilities; it provides an incentive for the adoption of notice-and-hearing procedures by the facilities themselves. [Section 11111\(a\)\(1\)](#) does not immunize peer review participants from liability under the federal civil rights acts, including [42 U.S.C. § 1983](#).

reputation and his professional practice. All of these factors contributed to his perception that the SJHSD environment was inhospitable, and led ultimately to his decision in February of 2000 to forsake his request for privileges at SJHSD and move his practice to Nevada.

**HN70**[] The essence of *Fourteenth Amendment* due process analysis is the [\*\*150] implication of a liberty or property interest. See [\*Board of Regents v. Roth\*, 408 U.S. 564, 571-72, 33 L. Ed. 2d 548, 92 S. Ct. 2701 \(1972\)](#). "Under the *Fourteenth Amendment*, procedural due process requires notice and a pre-deprivation hearing before property interests are negatively affected by governmental actors." [\*Marcus v. McCollum\*, 394 F.3d 813, 820 \(10th Cir. 2004\)](#). Health care professionals have been held to have a property interest in their professional licenses. See, e.g., [\*Seay v. Campbell\*, 130 Fed. Appx. 268, 2005 WL 1023400 \(10th Cir. 2005\)](#) ("property" interest in license to practice dentistry); Annotation, *Rights as to notice and hearing in proceeding to revoke or suspend license to practice medicine*, 10 A.L.R. 5th 1 (1993).

Some courts have expressed the view that "hospital staff privileges are generally considered to be a property or liberty interest of the physician," at least where they have already been granted by a government-sponsored facility. [\*Beyer v. Lakeview Community Hosp.\*, 187 F.3d 634, \(Table\), 1999 WL 552606, \\*\\*3 \(6th Cir. 1999\)](#) (citing [\*Foster v. Mobile County Hospital Bd.\*, 398 F.2d 227, 229 \(5th Cir. 1968\)](#)). A limitation, revocation or termination of existing [\*\*151] hospital staff privileges would thus have due process implications.

At least two circuits have held that "seeking staff privileges, which entitle a physician to admit patients to a particular hospital, has been held to be a protected liberty interest ...." [\*Silverstein v. Gwinnett Hosp. Authority\*, 861 F.2d 1560, 1566 \(11th Cir. 1988\)](#) (citations omitted). See [\*Burkette v. Lutheran General Hospital\*, 595 F.2d 255, 255-256 \[\\*1159\] \(5th Cir. 1979\)](#) ("We have held that a physician in private practice denied staff privileges in a hospital that is subject to the *fourteenth amendment* possesses a protectible 'liberty' interest that can ground a complaint on such a denial. [\*Shaw v. Hospital Authority\*, 507 F.2d 625 \(5th Cir. 1975\)](#).").<sup>67</sup>

**HN71**[] To pursue a due process claim in the courts based upon a denial of hospital staff privileges, however, those privileges must in fact be *denied* before the claim may be pursued in the courts. See [\*Unnamed Physician v. Board of Trustees of Saint Agnes Medical Center\*, 93 Cal. App. 4th 607, 113 Cal. Rptr. 2d 309 \(Ct. App. 2001\)](#) (physician challenging hospital's denial or withdrawal of staff privileges must pursue the internal remedies afforded by that hospital to a final decision on the merits before resorting to the courts for relief); [\*Eufemio v. Kodiak Island Hosp.\*, 837 P.2d 95 \(Alaska 1992\)](#) (exhaustion of administrative remedies required); [\*Eidelson v. Archer\*, 645 P.2d 171 \(Alaska 1982\)](#). The reported cases involving due process claims and hospital staff privileges arise from the actual denial, restriction, non-renewal or revocation of staff privileges. See generally Annotation, *Exclusion Of, or Discrimination Against, Physician or Surgeon by Hospital*, 28 A.L.R. 5th 107 (1995 & Supp. 2004) and cases cited therein.

In this instance, the SJHSD had neither granted nor denied Dr. MacArthur's [\*\*153] request for full one-year provisional privileges at the time that he decided to move his practice to Nevada in February or March of 2000. For his part, Dr. MacArthur did not press the issue after his "temporary" privileges expired by their own terms on February 2, 2000--temporary privileges that in fact had afforded Dr. MacArthur the use of the SJHSD hospital and Blanding birthing center to treat his patients and deliver babies during most of the time that his request for full provisional privileges was pending. Close examination of plaintiffs' allegations turns up no instance in which Dr. MacArthur was denied access to SJHSD facilities to provide care to a patient during the time that his request for full privileges was pending and his temporary privileges--twice extended--remained in effect.

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<sup>67</sup> The Utah courts have also entertained contractual "due process" claims involving the limitation or revocation of practice privileges at private hospitals based upon notice-and-hearing requirements found in hospital bylaws. See, e.g., [\*Rees v. Intermountain Health Care, Inc.\*, 808 P.2d 1069 \(Utah 1991\)](#); [\*Houston v. Intermountain Health Care, Inc.\*, 933 P.2d 403, 408 \(Utah Ct. App. 1997\)](#). In this case, Dr. MacArthur and Ms. Lyman have not pleaded such claims based upon the SJHSD [\*\*152] medical staff bylaws, instead choosing to attack the validity of the bylaws themselves. See *infra* note 104.

Taking Dr. MacArthur's factual allegations as true, the court concludes that Dr. MacArthur had not in fact been denied access to SJHSD facilities by any final action or determination by the SJHSD before Dr. MacArthur deliberately chose to forsake his request for full one-year SJHSD provisional staff privileges in favor of pursuing his medical practice elsewhere. Dr. MacArthur's election to move [\*\*154] his practice out of state waived his request for staff privileges at SJHSD facilities, and mooted any § 1983 claim based upon a denial of such privileges on due process grounds. His claim of denial or exclusion never became ripe for judicial review prior to February 2, 2000, the point at which Dr. MacArthur effectively abandoned his request for SJHSD privileges. See, e.g., Unity Ventures v. Lake County, 841 F.2d 770, 775-776 (7th Cir. 1988) (absent final governmental action denying intended use of property, § 1983 due process challenge to local land use regulation was not ripe [\*1160] for judicial review); Unnamed Physician v. Board of Trustees of Saint Agnes Medical Center, 93 Cal. App. 4th 607, 113 Cal. Rptr. 2d 309 (Ct. App. 2001).

His § 1983 claim cannot raise a triable issue, and must therefore be dismissed as against all of the defendants. Fed. R. Civ. P. 16(c)(1).

#### **Ms. Lyman's § 1983 Claim**

#### **Substantive Due Process**

From the colloquy at the Final Pretrial Conference, it became ever more apparent that even though plaintiffs MacArthur and Lyman have pleaded many parallel allegations concerning the question of staff privileges, their positions differ in fundamental ways. For one thing, Dr. MacArthur [\*\*155] as a licensed physician was free to compete for patient business with other licensed physicians; Ms. Lyman, as a licensed Physician's Assistant, is required by Utah law to work under the direct supervision of a physician. Under Utah law, the scope of practice for a Physician Assistant is defined in pertinent part as follows:

##### **58-70a-501. Scope of practice.**

- (1) A physician assistant may provide any medical services that are not specifically prohibited under this chapter or rules adopted under this chapter, and that are:
  - (a) within the physician assistant's skills and scope of competence;
  - (b) within the usual scope of practice of the physician assistant's supervising physician; and
  - (c) provided under the supervision of a supervising physician and in accordance with a delegation of services agreement.

Utah Code Ann. § 58-70a-501 (2002) (emphasis added). <sup>68</sup> State Administrative Rule R156-70a, the Physician Assistant Practice Act Rules, provides:

##### **R156-70a-501. Working Relationship and Delegation of Duties.**

HN72[] In accordance with Section 58-70a-501, the working relationship and delegation of duties between the supervising physician and the physician assistant are specified as follows:

- (1) The supervising [\*\*156] physician shall provide supervision to the physician assistant to adequately serve the health care needs of the practice population and ensure that the patient's health, safety and welfare will not be adversely compromised. The degree of on-site supervision shall be outlined in the Delegation of Services Agreement maintained at the site of practice. Physician assistants may authenticate with their signature any form that may be authenticated by a physician's signature.
- (2) There shall be a method of immediate consultation by electronic means whenever the physician assistant is not under the direct supervision of the supervising physician.

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<sup>68</sup> This statutory definition has been in effect since its enactment in 1997. See 1997 Utah Laws ch. 229, § 11.

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(3) The supervising physician shall review and co-sign sufficient numbers of patient charts and medical records to ensure that the patient's health, safety, and welfare will not be adversely compromised. The Delegation of Services Agreement, maintained at the site of practice, shall outline specific parameters for review that are appropriate for the working relationship.

(4) A supervising physician shall not supervise more than two full time equivalent (FTE) physician assistants without the prior approval of the division and [\*161] the board, and if patient [\*\*157] health, safety, and welfare will not be adversely compromised.

Utah Admin Code § R156-70a-501 (2004).

**HN73** [+] While it is true that under these provisions, a Physician Assistant may provide "any medical services" not specifically prohibited that are within the range of her skills and scope of competence and the skills and scope of practice of her supervising physician, she cannot lawfully exercise the identical degree of independent professional judgment and discretion that a physician could exercise, and logically she could not be entitled as a matter of constitutional right to exercise practice privileges at hospitals, clinics and similar facilities identical to those that physicians may enjoy. (Cf. Tr. 11/15/02, at 34:21-39:5 (Ms. Rose).)

**HN74** [+] Limiting a Physician Assistant's practice privileges to take into account the statutory and regulatory requirement of direct supervision and review by a physician cannot operate to deprive the Physician Assistant of "liberty" or "property" otherwise guaranteed by the *Fourteenth Amendment*. Nor is it arbitrary or unreasonable for a health care facility [\*\*158] to require that Physician Assistants exercise staff privileges under the supervision of a physician who currently has staff privileges at the same facility.

The restrictions on plaintiff Lyman's practice privileges at SJHSD facilities described in the Proposed Amended Complaint and at pretrial,<sup>69</sup> fall short of a constitutional deprivation,<sup>70</sup> and thus cannot serve as the factual footing

<sup>69</sup> Starting from the [\*\*159] premise that "while working for Dr. Redd, Mrs. Lyman applied for and received privileges with the District, with the same scope of privileges as Dr. Redd," (Proposed Pretrial Order at 27 P117; see *id.* at 39 P127 ("Mrs. Lyman's scope of privileges was originally for duties equal to Dr. Redd's.")), Ms. Lyman alleges that after leaving Dr. Redd's supervision in October, 1998, her privileges were restricted in several respects: "Mrs. Lyman could not admit or discharge patients without first her supervising doctor initially and officially and physically signing off on the patient's admit or discharge," (*id.* at 48 P169); she was told on one occasion in December 1998 that she could not give orders to SJHSD staff, (*id.* at 48-49 P170); later that same day, she was told she "could use the lab and xray *only during Dr. Penn's office hours*, [and that] otherwise Ms. Lyman did not have privileges," (*id.* at 49 P186 (emphasis in original)); "later the limited privileges of lab and exray [sic] were extended to her for her patients as required by State law," (*id.* at 49 P187), but in September 1999, her secretary was told "that Ms. Lyman would not be allowed to order labs until Ms. Lyman sent a letter to [\*\*160] Dr. Redd stating who her supervising physician was." (*Id.* at 55 P213). (See Proposed Amended Complaint at 55 P127; 69-70 P11 169-170; 70-71 P1 186-187; 79-80 P213 (same); Tr. 11/15/02, at 8:20-10:25, 17:6-11, 19:2-20:19, 22:15-20, 28:8-19, 30:4-20, 31:9-32:17, 40:22-42:3, 44:22-45:5, 46:7-20, 54:9-20.)

Ms. Lyman also alleges interference with her care for individual patients: in one instance, her request for a Holter monitor for a patient was denied (*id.* at 49 P185); on at least two occasions, her request for patient medical records was refused by Dr. Redd, (*id.* at 50-51 PP189, 193-194); despite an understanding with the SJHSD medical staff concerning injections, "Ms. Lyman tried on several occasions to call in injections to the ... ER (Blanding Urgent Care Clinic) and was denied every time. Ms. Lyman always had to call Dr. Penn's office and have him call the order in requests to the Blanding Urgent Care Center for injections for patients were denied by SJHSD staff," (*id.* at 54-55 P210). (See Proposed Amended Complaint at 70-73 PP185, 189, 193-194, 210 (same); Tr. 11/15/02, at 16:10-17:5, 21:19-21, 22:5-14, 26:12-25, 30:4-31:6, 39:3-40:12; compare *supra* n. 12.)

<sup>70</sup> Substantive due process [\*\*161] requires that a termination, suspension, denial or restriction of a plaintiff's practice privileges not be "arbitrary, capricious, or without a rational basis." *Tonkovich v. Kansas Bd. of Regents*, 159 F.3d 504, 528 (10th Cir. 1998) (quoting *Brenna v. Southern Colo. State College*, 589 F.2d 475, 477 (10th Cir. 1978)).

The Tenth Circuit recently reiterated the standards for evaluating substantive due process claims:

In analyzing plaintiff's substantive due process claim, the court assumes plaintiff's employment was an interest entitled to protection. In *Uhlrig v. Harder*, 64 F.3d 567 (10th Cir. 1995), we stated that "the standard for judging a substantive due process claim is whether the challenged government action would 'shock the conscience of federal judges.'" *Id. at*

for Ms. [\*1162] Lyman's [§ 1983](#) claim against any of the individual defendants, including the SJHSD Board and San Juan County Commissioners. (See Tr. 11/15/02, at 26:14-32:17, 34:20-44:7 (Ms. Rose).) Or, looking at it another way, plaintiffs' allegations, taken as true, fail to establish a violation of a clearly established constitutional right to unrestricted practice privileges as a state-licensed Physician Assistant at publicly-sponsored medical facilities, and as a result, plaintiff's [§ 1983](#) claim against the individual defendants is barred by the doctrine of qualified immunity. Plaintiff Lyman likewise fails to allege an arguable claim of constitutional deprivation resulting from a "policy" or "custom" of the SJHSD or San Juan County, and cannot hold either entity liable under [§ 1983](#).

## Procedural Due-Process

Plaintiffs plead a "Lack of Notice and Due Process," (Proposed Amended Complaint at 46-52 PP129-167; see Proposed Pretrial Order at 33-37 PP161-199 (same)), but relatively few of the factual allegations pleaded under that heading pertain to Ms. Lyman, and they address the alleged alteration of dates on her CPR certification cards--cards curiously discovered to be "missing" from her SJHSD file at the time that she requested staff privileges to practice under Dr. MacArthur's supervision in December, 1999. (See *id.* at 46-48 PP129-140, 142-146.)<sup>71</sup> Other than alleging that "the Medical staff and Cleal Bradford and Laurie Shafer discussed Mrs. Lyman's CPR card problems of [\*1163] wrong dates without Mrs. Lyman being present," (*id.* at 46-47 P133), and "the medical staff and Cleal Bradford and Laurie Shafer unanimously decided to publish the altered cards to the American Heart Association by vote of the medical [\*\*163] staff, who was considering privileges for Mrs. Lyman, without Mrs. Lyman being present," (*id.* at 48 P142), Ms. Lyman does not plead specific facts showing a denial of fair notice and an opportunity to be heard on the CPR card issue. (*Cf.* Proposed Pretrial Order at 63 P255 ("she was not notified immediately that her cards were in some way in error").) In fact, she alleges that the CPR card problem was brought to her attention, that she furnished accurate CPR certification information to the SJHSD, but that her SJHSD privileges ultimately were not renewed. She did not pursue the request any further. (See Tr. 11/15/02, at 52:3-53:17 (Ms. Rose).)

While the specific instances of interference with her exercise of her SJHSD privileges may raise contract-based claims under Utah law, see *infra*, Ms. Lyman has not alleged specific facts showing a denial of procedural due process guaranteed by the [Fourteenth Amendment](#).

## Misogyny & "Hostile Environment" under [§ 1983](#)

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[573](#) (quoting [Collins v. City of Harker Heights](#), 503 U.S. 115, 112 S.Ct. 1061, 117 L.Ed.2d 261 (1992)) (further quotations omitted). To "satisfy the 'shock the conscience' standard, a plaintiff must do more than show that the government actor intentionally or recklessly caused injury to the plaintiff by abusing or misusing government power." [Id. at 574](#). Rather, a plaintiff "must demonstrate a degree of outrageousness and [\*\*162] a magnitude of potential or actual harm that is truly conscience shocking." *Id.*

[Babbar v. Ebadi](#), 2000 U.S. App. LEXIS 11798, 2000 WL 702428, at \*10 (10th Cir. 2000).

[Ferraro v. Board of Trustees of Labette County Medical Center](#), 106 F. Supp. 2d 1195, 1202 (D.Kan. 2000).

<sup>71</sup> Ms. Lyman also asserts that she "had sought privileges ever since they were de facto terminated by district policy after she began working for Dr. Penn, having left the practice of Dr. Redd," in October 1998, (Proposed Amended Complaint at 40 P91), but her specific factual allegations reflect that she continued to exercise her privileges through 1999. The scope of her privileges was the subject of discussion involving Ms. Lyman, Dr. Penn and the SJHSD medical staff in which it was acknowledged by the medical staff that Ms. Lyman could, *inter [\*\*164] alia*, request x-rays, lab work and injections for patients, and could continue to exercise privileges under local physician supervision. See *supra* at n. 69. In December of 1999, she requested *renewal* of her existing privileges, which had a renewal date of December 22, 1999. (See Tr. 11/15/02, at 49:6-52:6 (Ms. Rose).)

Whether certain SJHSD nurses or other employees interfered with the exercise of her existing privileges is another matter, (see Proposed Pretrial Order at 14 ("Privileges for Mrs. Lyman were de facto denied by nursing personnel and medical staff without any action by the District governance board.")), raising potential claims of breach of contract or the implied covenant of good faith and fair dealing, or interference with contract.

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Ms. Lyman complains that Dr. Redd, the "Chief of Medical Staff has a long standing animus toward women," that during the time she [\*\*165] was employed by Dr. Redd in his private practice from June 1996 until October 1998, she observed Dr. Redd being angry and verbally abusive in dealing with his female employees, e.g., referring to Ms. Lyman as an "idiot" and another employee as an "incompetent bitch," and that

149. Mrs. Lyman observed that each nurse, in order to avoid Dr. Redd's tirades would turn on each other or disassociate with the person who Dr. Redd targeted that day.

150. Thus, an atmosphere of distrust and hostility permeated the office creating a hostile work and patient environment.

(Proposed Amended Complaint at 60-61 PP143, 149-150.)

Generally, to plead a viable "hostile environment" claim, a plaintiff must show "that under the totality of the circumstances (1) the harassment was pervasive or severe enough to alter the terms, conditions, or privilege of employment, and (2) the harassment was racial or stemmed from racial animus," or other forbidden class-based discriminatory animus, such as gender. *Bolden v. PRC Inc.*, 43 F.3d 545, 551 (10th Cir. 1994) (citation omitted). In a case involving discrimination on account of race, "[a] plaintiff cannot meet this burden by demonstrating "a few isolated incidents [\*\*166] of racial enmity" or "sporadic racial slurs," or the like. *Id.* (quoting *Hicks v. Gates Rubber Co.*, 833 F.2d 1406, 1412-13 (10th Cir. 1987)). Instead, "there must be a steady barrage of opprobrious racial comments." *Chavez v. New Mexico*, 397 F.3d 826, 832 (10th Cir. 2005). Where the enmity is based upon gender, a plaintiff must likewise allege a "steady barrage" or "steady stream" of misogynistic abuse in order to sustain a "hostile environment" claim. See, e.g., *Gross v. Burggraf Constr. Co.*, 53 F.3d 1531, 1539 (10th Cir. 1995) ("It is beyond dispute that evidence that a woman was subjected to a steady stream of vulgar and offensive epithets because of her gender would be sufficient to establish a claim under Title VII"); *Winsor v. Hinckley Dodge, Inc.*, 79 F.3d 996, 1000-1001 (10th Cir. 1996) ("Over the course of her employment, plaintiff was called a 'whore,' 'floor whore,' 'curb whore,' 'curb side cunt,' and 'bitch,' on a consistent basis. These sexual epithets have been identified [\*1164] as 'intensely degrading' to women." (internal quotation & citation omitted)).

"Hostile work environment harassment occurs when unwelcome sexual conduct "unreasonably interferes with an individual's work [\*\*167] performance or creates an intimidating, hostile, or offensive working environment." *Meritor Sav. Bank, FSB v. Vinson*, 477 U.S. 57, 65, 106 S. Ct. 2399, 91 L. Ed. 2d 49 (1986) (quoting 29 C.F.R. § 1604.11(a)(3)). According to the court of appeals,

*Meritor* states that "for sexual harassment to be actionable, it must be sufficiently severe or pervasive 'to alter the conditions of [the victim's] employment and create an abusive working environment.'" *Id. at 67, 106 S.Ct. at 2405* (citation omitted). The mere utterance of a statement which "engenders offensive feelings in an employee" would not affect the conditions of employment to [a] sufficiently significant degree to violate Title VII." *Id.* (quoting *Rogers v. EEOC*, 454 F.2d 234, 238 (5th Cir. 1971), cert. denied, 406 U.S. 957, 92 S.Ct. 2058, 32 L.Ed.2d 343 (1972)).

*Smith v. Northwest Financial Acceptance, Inc.*, 129 F.3d 1408, 1412 (10th Cir. 1997).<sup>72</sup> In the context of a hostile environment claim, courts must "filter out complaints attacking the ordinary tribulations of the workplace, such as the sporadic use of abusive language, gender-related jokes, and occasional teasing." *Forager v. City of Boca*

<sup>72</sup> *Harris v. Forklift Systems, Inc.*, 510 U.S. 17, 114 S. Ct. 367, 126 L. Ed. 2d 295 (1993), clarified the elements of a claim for gender discrimination resulting from a hostile work environment. The Supreme Court held that conduct within the purview of Title VII of the 1964 Civil Rights Act, 42 U.S.C. §§ 2000e-1 et seq., must be severe or pervasive enough to create both "an objectively hostile or abusive work environment--an environment that a reasonable person would find hostile"--and an environment the victim-employee subjectively perceives as abusive or hostile. *Id. at 21-22*. Whether an environment is "hostile" or "abusive" is determined by looking at the totality of circumstances, such as "the frequency of the discriminatory conduct; its severity; whether it is physically threatening or humiliating, or a mere offensive utterance; ... whether it unreasonably interferes with an employee's work performance"; and the context in which the conduct occurred. *Id. at 23*. Additionally, the *Harris* Court specifically noted that any relevant factor "may be taken into account, [but] no single factor is required." *Id.*

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[Raton, 524 U.S. 775, 788, 118 S. Ct. 2275, 141 L. Ed. 2d 662 \(1998\)](#) [\*\*168] (internal quotation marks and citation omitted).

Plaintiff Lyman did not plead [\*\*169] and does not assert a "hostile environment" claim under Title VII of the 1964 Civil Rights Act, [42 U.S.C. §§ 200e-1 et seq.](#) However, the court of appeals has held that, apart from Title VII, gender discrimination and sexual harassment can result in a violation of the [Fourteenth Amendment](#) right to equal protection of the law that is actionable under [§ 1983](#).<sup>73</sup> However, a [\*1165] plaintiff must allege "the state action necessary to support a [§ 1983](#) claim,<sup>74</sup> and each individual defendant must act under color of state law; a "state actor" must serve as the plaintiff's "supervisor or in some other way exercise state authority over her." [Noland v. McAdoo, 39 F.3d 269, 271 \(10th Cir. 1994\)](#); see also [David v. City & County of Denver, 101 F.3d 1344, 1354 \(10th Cir. 1996\)](#) (public co-employees may act under color of law if they exercise de facto authority over victim), cert. denied, 522 U.S. 858, 118 S. Ct. 157, 139 L. Ed. 2d 102 (1997).<sup>75</sup>

Here, the "state action" requirement proves somewhat problematic. During the time Ms. Lyman worked for Dr. Redd, Dr. Redd was engaged in private medical practice, and was not a SJHSD employee. His conduct in that context would lack the requisite "state action" needed to sustain a [§ 1983](#) claim. The plaintiffs' factual allegations suggest that Dr. Redd was speaking to Ms. Lyman and his other employees as a private employer, and not in any official capacity.<sup>76</sup> Though [\*\*172] Dr. Redd became employed by the SJHSD in March of 1999 and would likely be held to be a "state actor" as to his conduct as SJHSD medical director or "Chief of Medical Staff,"<sup>77</sup> the plaintiffs'

<sup>73</sup>

If a plaintiff can show a constitutional violation by someone acting under color of state law, then the plaintiff has a cause of action under [Section 1983](#), regardless of Title VII's concurrent application. See [Owens v. Rush, 654 F.2d 1370, 1380 \(10th Cir. 1981\)](#) [\*\*170] ("Title VII did not impair in any way [plaintiff's] independent, substantive rights created by the [First](#) and [Fourteenth Amendments](#) . . . . Substantive rights conferred in the 19th Century were not withdrawn, sub silentio, by the subsequent passage of the modern statutes.") (quoting [Great Am. Fed. Sav. & Loan Ass'n v. Novotny, 442 U.S. 366, 377, 99 S.Ct. 2345, 2351, 60 L. Ed. 2d 957](#)); [Day v. Wayne County Bd. of Auditors, 749 F.2d 1199, 1205 \(6th Cir. 1984\)](#) ("Where an employee establishes employer conduct which violates both Title VII and rights derived from another source--the Constitution or a federal statute . . . the claim based on the other source is independent of the Title VII claim, and the plaintiff may seek the remedies provided by [§ 1983](#) in addition to those created by Title VII."); cf. [Meade v. Merchants Fast Motorline, Inc., 820 F.2d 1124, 1127 \(10th Cir. 1987\)](#) ("plaintiff may properly pursue his cause of action under [§ 1981](#) for private employment discrimination despite the applicability of Title VII to the same conduct").

[Starrett v. Wadley, 876 F.2d 808, 814 \(10th Cir. 1989\)](#).

<sup>74</sup> To be successful, [section 1983](#) claimants must make two showings to establish that the conduct at [\*\*171] issue constituted state action. 'First, the deprivation must be caused by the exercise of some right or privilege created by the State or by a rule of conduct imposed by the State or by a person for whom the State is responsible.' [Lugar v. Edmondson Oil Co., 457 U.S. 922, 937, 102 S.Ct. 2744, 73 L.Ed.2d 482 \(1982\)](#). 'Second, the party charged with the deprivation must be a person who may fairly be said to be a state actor.' *Id.* [Nieto v. Kapoor, 268 F.3d 1208, 1215 \(10th Cir. 2001\)](#).

<sup>75</sup> State action under [§ 1983](#) can occur when a supervisor "participates in or consciously acquiesces in sexual harassment . . . by co-workers." [Murrell v. School Dist. No. 1, 186 F.3d 1238, 1250 \(10th Cir. 1999\)](#) (quotation marks and citation omitted).

<sup>76</sup> At that time, Dr. Redd was also a member of the SJHSD medical staff, and at different times in 1996 may have served as chief of staff. (See Tr. 11/15/02, at 3:20-22 (Ms. Rose). Dr. Redd's conduct as the SJHSD chief of staff may be state action under [§ 1983](#). See, e.g., [Nieto v. Kapoor, 268 F.3d 1208, 1215-1217 \(10th Cir. 2001\)](#) (non-employee medical director of hospital department acted under color of state law for purposes of [§ 1983](#) "when undertaking his supervisory duties over plaintiffs' work" in that department and was "a state actor for purposes of [section 1983](#)."). Yet plaintiffs do not allege that Dr. Redd was acting as the SJHSD chief of staff--not as a private employer engaged in a private medical practice--in making the alleged derogatory remarks to Ms. Lyman and others who worked for him. (See Proposed [\*\*173] Amended Complaint at 60-68 PP145-166.)

<sup>77</sup> (Proposed Amended Complaint at 60 P143.)

pleadings speak of the "atmosphere of distrust and hostility" that "permeated" Dr. Redd's office in Blanding at the time Ms. Lyman worked there. (Proposed Amended Complaint at 61 P150.)<sup>78</sup>

#### **[\*1166] Qualified Immunity & Ms. Lyman's § 1983 Claim**

Further, as noted above, the defendants contend that because "the alleged acts and/or omissions by County commissioners, officials or employees or Health District trustees, employees or staff members, about which plaintiffs complain, were carried out within the scope of and pursuant to their official duties as trustees, employees or staff members of the Health District, plaintiffs' claims are barred by the doctrine of qualified immunity," (Proposed Pretrial Order at 10 Pxxxvi), at least to the extent those claims are asserted pursuant to 42 U.S.C. § 1983.

**[\*\*174]** Concerning individual defendants who have raised a claim of qualified immunity,

The threshold inquiry is whether the alleged facts (or, on summary judgment, the evidenced facts) taken in the light most favorable to the plaintiff show a constitutional violation. Saucier v. Katz, 533 U.S. 194, 201, 121 S.Ct. 2151, 150 L.Ed.2d 272 (2001). "If no constitutional right would have been violated were the allegations established, there is no necessity for further inquiries concerning qualified immunity." *Id.*

Simkins v. Bruce, 406 F.3d 1239, 1241 (10th Cir. 2005).

From the foregoing summary, it readily becomes apparent that the plaintiffs' allegations as of the eve of pretrial, taken as true and in the light most favorable to the plaintiffs, failed on their face to show a constitutional violation by the individual defendants. "[A] defamatory statement published by state officials is not for that reason alone a Fourteenth Amendment violation," 1 Nahmod, *supra*, § 3:40, at 3-117 (citing Paul v. Davis, 424 U.S. 693, 96 S. Ct. 1155, 47 L. Ed. 2d 405 (1976)), and the making of derogatory remarks, the infliction of verbal abuse, the honking of car horns and other potentially tortious conduct does not **[\*\*175]** automatically implicate the Due Process Clause simply because the actor is employed by a local health services district or is a member of its medical staff. Nor does interference with, or even the breach of a district contract with a health services provider, caused by a district official or staff acting under his direction, necessarily result in a constitutional deprivation of "liberty" or "property" that is actionable under § 1983. Absent a constitutional deprivation, qualified immunity entitles the individual defendants to a dismissal of plaintiff Lyman's § 1983 claims.

#### **Ms. Helen Valdez' § 1983 Claim**

The facts underlying the claim of plaintiff Helen Valdez have already been summarized herein. ( See *supra* at 15-17, 30-31.) Her potential civil claim under EMTALA being time-barred, at least absent leave to amend,<sup>79</sup> the only claim that remained pending for consideration at the time of pretrial was her § 1983 claim of purposeful national origin, gender and age discrimination in violation of the Equal Protection Clause of the Fourteenth Amendment.

In order to state a viable equal protection claim under § 1983, "a plaintiff must show that the defendants acted with **[\*\*176]** an intent or purpose to discriminate against the plaintiff based upon membership in a protected class." Lee v. City of Los Angeles, 250 F.3d 668, 686 (9th Cir. 2001) (citations omitted); see also Washington v. Davis, 426 U.S. 229, 240, 96 S. Ct. 2040, 48 L. Ed. 2d 597 (1976). To support her § 1983 claim, then, Ms. Valdez must come forward with facts indicating a discriminatory intent on the part of the defendants. [\*1167] See Firefighters Local Union No. 1784 v. Stotts, 467 U.S. 561, 583 n. 16, 104 S. Ct. 2576, 81 L. Ed. 2d 483 (1984) ( §§ 1981 & 1983); Village of Arlington Heights v. Metropolitan Housing Dev. Corp., 429 U.S. 252, 265, 97 S. Ct. 555, 50 L. Ed. 2d 450

<sup>78</sup> Ms. Lyman would not have standing to bring a "hostile environment" claim under either Title VII or § 1983 for verbal abuse occurring after October or November of 1998 because at that point she was no longer employed by Dr. Redd. She was working with and being supervised by Dr. Penn; after she left Dr. Redd's supervision in 1998, Dr. Redd's derogatory remarks--rude, offensive, antagonistic and unprofessional as they may have been--could not alter the terms, conditions, or privileges of Ms. Lyman's subsequent employment.

<sup>79</sup> ( See *supra* at 59-60.)

(1977) (equal protection). She must also allege facts showing that a defendant "engaged in specific conduct that denied her equal protection of the laws." [Williams v. Bramer, 180 F.3d 699, 701 \(5th Cir. 1999\)](#).

Ms. Valdez is a white female over the age of 60, married to a Mexican-American husband. (Proposed Pretrial Order at 69 PP14-15.) Counsel asserts that on April 14, 1999, she was "turned away" from the San Juan Hospital emergency room because of her age, her gender, her association with her Mexican-American husband and sister-in-law, [\*\*177] and with her then-primary care physician, Dr. Penn, who was identified as being Jewish. ( See Tr. 11/15/02, at 59:1-15 (Ms. Rose); Memorandum of Points and Authorities Supporting Plaintiff Valdez's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 665), at 6-20.)<sup>80</sup> Counsel relies upon a "disparate treatment analysis," citing [McDonnell Douglas Corp. v. Green, 411 U.S. 792, 802, 93 S. Ct. 1817, 36 L. Ed. 2d 668 \(1973\)](#), based upon allegations that Ms. Valdez "was turned away, when accompanied by her Mexican-American appearing sister-in-law, by nurse Laurie Wallace," while at the same time, "the white young male with no insurance in the ER waiting area was seen by Dr. Penn almost immediately after Mrs. Valdez left." (Proposed Amended Complaint at 86 P232-233; see Proposed Pretrial Order at 22 P66 ("Mrs. Valdez' neighbor who was a white young male and had not insurance was seen immediately.").)

Counsel's proffered inference of discriminatory treatment and discriminatory purpose from the fact that another patient waiting in the emergency room was examined by a physician and Ms. Valdez was not collides with a key fact: Ms. Valdez was not refused screening, examination, or treatment; nor was she instructed or ordered by any emergency room personnel to leave the facility. ( See *supra* at 15-17.) At pretrial, counsel argued that Ms. Valdez "was told to go"--an assertion belied by the plaintiffs' own pleadings and Ms. Valdez' own deposition testimony. (Tr. 11/15/02, at 60:7 (Ms. Rose).) Ms. Valdez explained that she decided [\*\*179] to leave the emergency room and return home after her sister-in-law told her that she had overheard a nurse, Lori Wallace, tell the emergency room clerk who had assisted Ms. Valdez in filling out her patient admittance form to tell Ms. Valdez to go to her physician's clinic. ( See *supra* at 15-16 & nn. 18-19; Tr. 11/15/02, at 57:1-4 (Ms. Rose) ("Laurie [sic] Wallace had told the receptionist, tell them to go to the clinic, it's open, something to that effect. The exact words were tell them to go to the [\*1168] clinic.")) Shortly before that, however, Ms. Valdez had observed Lori Wallace tell the same clerk that "she could set both her patients up in the emergency room for the physician," apparently referring to Ms. Valdez and Michael Bailey, the other individual then waiting in the emergency room. ( *Id.*)

Yet Ms. Valdez did not speak directly to either the nurse or the clerk about her symptoms or ask whether or when she would be seen by a doctor at the emergency room. She left the facility, apparently assuming that she would not be examined. She explained her reticence in her deposition:

A Well, living in San Juan County for many years and living in a Mexican-American community, you kind of [\*\*180] learn to keep your place. You don't just voluntarily speak out. You just kind of wait until spoken to.

Q How does that apply to being a woman in San Juan County?

A I believe probably about the same.

(Deposition of Helen Valdez, dated December 6, 2001, at 52:17-24.) In this instance, she did not wait to be spoken to; assuming that she would not be examined at the emergency room, Ms. Valdez simply left. Taking the plaintiff's factual averments as true--in particular, the portions of the deposition testimony of Ms. Valdez and Ms. Gonzales submitted to the court by plaintiffs' counsel--it cannot fairly be said that Ms. Valdez was "turned away" from examination and treatment at the San Juan Hospital emergency room on April 14, 1999. No one on the SJHSD staff

<sup>80</sup> Claims of class-based discrimination against a non-minority plaintiff based upon association with the plaintiff's minority spouse have met with mixed results. Compare, [\*\*178] e.g., [Davis v. Southeastern Pennsylvania Transp. Authority, 924 F.2d 51 \(3d Cir. 1991\)](#) (plaintiff white police officer married to African-American spouse prevailed on § 1983 anti-discrimination claim arising out of officer's discharge from employment), with [University Village Music Center v. Seattle School Dist., 844 F.2d 793 \(Table\), 1988 WL 33365, \(9th Cir. 1988\)](#) (unpublished disposition) (conclusory allegations that the defendants discriminated against plaintiff's business because his former wife is of Japanese descent insufficient to state a § 1983 claim).

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told Ms. Valdez that she would not be examined by a physician if she remained there, and both Ms. Valdez and Ms. Gonzales acknowledged that no one on the SJHSD staff expressly instructed Ms. Valdez to leave.<sup>81</sup>

Before Lori Wallace may be held liable under [§ 1983](#) for a constitutional deprivation purposefully inflicted upon Ms. Valdez,<sup>82</sup> there needs to be at least one sworn averment of specific facts in the record showing that Ms. Wallace acted that "with an intent or purpose to discriminate against the plaintiff" based upon the plaintiff's membership in a protected class (or at least her identification with a protected class),<sup>83</sup> and that Ms. Wallace "engaged in specific conduct that denied her equal protection of the laws." None was cited or proffered at pretrial, and none was submitted in connection with either the Proposed Amended Complaint or the Proposed Pretrial Order.

At the conclusion of the pretrial colloquy concerning Ms. Valdez' claim, this court concluded:

Looking at the statutes referred to and particularly the suggestion that implicitly the complaint ought to conform with what is said to be the evidence, [\*1169] namely that she went to an emergency room and wasn't treated, I think under the factual scenario presented that it is insufficient to justify referring the matter to a fact-finder and under the circumstances that cause of action as alleged and as proffered should also be dismissed and I will so order.

(Tr. 11/15/02, at 117:10-18 (the Court).)

"The pretrial conference is never to be used as a substitute for trial . . . . Nevertheless, just as the Court may render judgment on immaterial issues for which there is no dispute of material fact, 'judgment may be ordered . . . if [\*183] there is no triable issue left at the end of the discussion.'" *Pifcho v. Brewer*, 77 F.R.D. 356, 357 (M.D. Pa. 1977) (quoting 6 Charles A. Wright & Arthur R. Miller, *Federal Practice and Procedure* § 1525 (1971).)

#### **(9) Federal Antitrust Laws ([15 U.S.C. §§ 1 et seq.](#))**

Section 4 of the Clayton Act, [15 U.S.C.A. § 15 \(1997\)](#), cited by the Part I Plaintiffs, provides in part that "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor" in an appropriate federal district court "and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee," expressly providing injured parties with a private civil treble damages remedy for violations of the federal antitrust laws. As a remedial provision, [§ 4](#) itself does not proscribe any specific anti-competitive conduct. Conduct "forbidden in the antitrust laws" is defined elsewhere, as in the first two sections of the Sherman Anti-Trust Act. Section 1 of the Sherman Act, [15 U.S.C.A. § 1 \(1997\)](#), states in part:

Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the [\*184] several States, or with foreign nations, is hereby declared to be illegal . . . .

Section 2 of the Sherman Act, [15 U.S.C.A. § 2 \(1997\)](#), states in part:

Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, . . . .

<sup>81</sup> This being so, Ms. Valdez was not denied or refused the screening, examination or stabilizing treatment for an "emergency medical condition" required by EMTALA, [42 U.S.C. § 1395dd\(a\)](#), and has no arguable legal claim arising [\*181] from a violation of that statute. [42 U.S.C. § 1395dd\(d\)](#). ( See *supra at 56-58.*)

<sup>82</sup> Counsel now argues the existence of a County "policy or custom" of disparate treatment of "people of color," relying largely on hearsay assertions of anecdotal evidence. ( See Memorandum of Points and Authorities Supporting Plaintiff Valdez's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 665), at xii, 18-19.) [\*182] This claim was neither pleaded through specific allegations in the Proposed Amended Complaint nor raised as an issue in the Proposed Pretrial Order.

<sup>83</sup> *Muzquiz v. W.A. Foote Memorial Hosp., Inc.*, 70 F.3d 422, 429 (6th Cir. 1995) (witness' "subjective belief that minorities would be treated differently at the hospital was simply not probative of a discriminatory animus").

Section 4 of the Clayton Act "requires a plaintiff to show actual injury," Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 111, 107 S. Ct. 484, 93 L. Ed. 2d 427 (1986), and "the plaintiff must still allege an injury of the type the antitrust laws were designed to prevent." *Id.* (footnote omitted). Indeed, "standing and antitrust injury are essential elements in a private antitrust damages action brought under section 4 of the Clayton Act." Reazin v. Blue Cross and Blue Shield of Kansas, 899 F.2d 951, 960 (10th Cir. 1990) (citing Cargill, 479 U.S. at 110; Associated Gen. Contractors, Inc. v. California State Council of Carpenters, 459 U.S. 519, 103 S. Ct. 897, 74 L. Ed. 2d 723 (1983)). According to the court of appeals, the following factors are "to be considered in determining [\*\*185] antitrust standing:"

the causal connection between the antitrust violations and plaintiff's injury; the defendant's intent; the nature of the plaintiff's injury; the directness or indirectness of the connection between the plaintiff's injury and the allegedly unlawful market restraint; the speculativeness of the plaintiff's damages; and the "risk of duplicative recoveries . . . or the danger of complex apportionment of damages." Associated Gen. Contractors, 459 U.S. at 544, 103 S. Ct. at 912.

Id. at 962 n. 15.

The "nature of the plaintiff's injury factor" is "designed to implement [\*1170] the requirement that only *antitrust* injuries are redressable under ." *Id.* (emphasis in original). "Antitrust injury" is demonstrated "'by a causal relationship between the harm and the challenged aspect of the alleged violation' of the federal antitrust laws." Id. at 961 (quoting Alberta Gas Chems., Ltd. v. E.I. Du Pont de Nemours & Co., 826 F.2d 1235, 1240 (3d Cir. 1987), cert. denied, 486 U.S. 1059, 108 S. Ct. 2830, 100 L. Ed. 2d 930 (1988).).

An antitrust violation may be expected to cause ripples of harm to flow through the Nation's economy; but "despite the broad wording of § 4 there is a point beyond [\*\*186] which the wrongdoer should not be held liable." . . . It is reasonable to assume that Congress did not intend to allow every person tangentially affected by an antitrust violation to maintain an action to recover threefold damages for the injury to his business or property.

Blue Shield of Virginia v. McCready, 457 U.S. 465, 476-477, 102 S. Ct. 2540, 73 L. Ed. 2d 149 (1982) (citation omitted). In evaluating a private plaintiff's standing under § 4, "we look (1) to the physical and economic nexus between the alleged violation and the harm to the plaintiff," and "(2), more particularly, to the relationship of the injury alleged with those forms of injury about which Congress was likely to have been concerned in making defendant's conduct unlawful and in providing a private remedy under § 4." Id. at 478.<sup>84</sup> The "injury suffered by the plaintiff must be of the type the antitrust laws were intended to forestall." Id. at 484 n.21, 486; see Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977) (an antitrust injury is an "injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful"). [\*\*187]

Thus, to "prevail, a private plaintiff must establish both (1) that it has standing and (2) the defendant has violated the antitrust laws. . . . The antitrust injury element of standing demands that the plaintiff's alleged injury result from the threat to competition that underlies the alleged violation." 2 Phillip E. [\*\*188] Areeda, Herbert Hovenkamp & Roger D. Blair, Antitrust Law P335, at 297 (2d ed. 2000) (footnote omitted). "Once it appears, whether early or late in the litigation, that either requirement [of standing or antitrust violation] is lacking, the suit must be dismissed." *Id.*

<sup>84</sup> Ms. McCready, a subscriber to a group health care plan who had been denied reimbursement by the plan for the cost of services of a clinical psychologist, brought her suit under § 4, alleging that the plan had conspired with a professional association of physicians and psychiatrists to exclude psychologists from receiving payment under the plan for outpatient treatment of mental disorders, including psychotherapy in violation of § 1 of the Sherman Act. 457 U.S. at 467-70. The Court concluded that "the injury she suffered was inextricably intertwined with the injury the conspirators sought to inflict on psychologists and the psychotherapy market. In light of the conspiracy here alleged we think that McCready's injury 'flows from that which makes defendants' acts unlawful . . . and falls squarely within the area of congressional concern.' Id. at 484 (footnote omitted).

At the time of the Pretrial Conference, the Part I Plaintiffs asserted that the "District employees as a pattern sought to restrain competition[;] there was inadequate impartiality in 'peer review' or in issuing privileges since the people issuing the privileges are usually in economic competition with those they are giving privileges." (Proposed Pretrial Order at 14-15.) The Proposed Amended Complaint alleged that "District employee doctors and Dr. Jones who was contracted with the District constituted about 80% or greater [\*1171] of the competing doctors in the area," (Proposed Amended Complaint at 30 P26), and that "at all times, Dr. MacArthur and Michele Lyman were subject to District policies regarding their privileges as written and accepted by medical providers and physicians who economically competed with them." ( *Id.* at 30 P27.)

In this case, then, the alleged "conduct forbidden by the antitrust laws" arises in the **[\*\*189]** context of the grant, limitation, or denial of medical practice privileges at a hospital, clinic or birthing center. ( See generally *id.* at 26-34 PP1-49 ("Specific Statements of Facts -- Anti-Trust Claims"); *id.* at 34-58 PP50-168 ("Facts for [42 USC 1983](#), and antitrust and RICO claims"); *id.* at 58-86 PP125-230 (same).)

Plaintiffs assert that the geographic market in which plaintiffs and the "District" health care services providers compete is San Juan County, Utah, with a "rural" or "frontier" population of over 13,000 people; the boundaries of the SJHSD are co-extensive with those of the county. ( *Id.* at 29-30 PP19-25.) Within that geography, plaintiffs assert that the SJHSD is the sole provider of hospital and birthing center services to that population:

37. San Juan Hospital and Blanding Birthing Center are the only facilities in San Juan County for births and are operated solely by San Juan Health Services District.

38. Nearly all emergency ambulance deliveries are made to San Juan Hospital.

39. The next nearest hospital facility to San Juan Hospital in Monticello, Utah is about 65 miles away in either a north (Moab) or east (Cortez, Co.) direction, and about 85 miles from Blanding. **[\*\*190]** Shiprock hospital is between 65 to 85 miles from southern areas of San Juan County in Shiprock, New Mexico.

40. San Juan Hospital is the sole provider for those persons with insurance but without transportation to go outside the county or with physical conditions requiring ambulance transportation.

41. Any physician delivering babies in San Juan County would need to use the closest San Juan District facilities for patients in active labor.

( *Id.* at 32-33 PP37-41.) Further, according to plaintiffs, "With the exceptions of Dr. Jones and a Monument Valley clinic doctor, all other physicians and P.A.'s within San Juan District are employees of San Juan District," and none of these providers specialized in obstetrics and gynecology during the period that Dr. MacArthur--an obstetrician/gynecologist--sought staff privileges at SJHSD facilities. ( *Id.* at 33 PP43, 44.) The Part I Plaintiffs assert that "Dr. MacArthur's practice was in direct competition with District and District associated General Practitioners who delivered babies," and received additional compensation for doing so. ( *Id.* at 34 P48; see *id.* at 33 PP45-47.) According to these plaintiffs, the grant or denial of privileges to **[\*\*191]** Dr. MacArthur and Ms. Lyman was driven by considerations of competitive economics rather than professional practice concerns:

45. Without Dr. MacArthur and Michele Lyman to treat obstetric patients, the patients if they wished a local delivery when they went into labor, had to go to a doctor not specialized in the area of obstetrics.

\* \* \* \*

49. In making the determination of granting privileges, the medical staff and CEOs would analyze the effect of the independent practices of Dr. MacArthur and Michele Lyman upon their income outside any formal 'peer review' **[\*1172]** context and in regards to them obtaining privileges.

( *Id.* at 33-34 PP45, 49.)

The Proposed Amended Complaint speaks of the "anti-competitive effect" of limiting the privileges of Dr. MacArthur and Ms. Lyman:

42. Dr. MacArthur's limited temporary privileges preventing him from fully using the District facilities provided his patients with limited options in where they could receive their care, and prevented some from becoming his patient.

\* \* \* \*

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98. The likely and logical *per se* effect of not granting District privileges to Michele Lyman and Dr. MacArthur is that patients would not be able to choose Michele Lyman or Dr. MacArthur [\*\*192] as providers if they wished to receive to receive their care at the hospital.

(Proposed Amended Complaint at 33 P42, 40-41 P98.)

The restriction or denial of hospital staff privileges as a result of peer review procedures may indeed raise antitrust concerns:

Peer review of physicians holding or applying for hospital or medical staff privileges has given rise to numerous antitrust claims. The courts have recognized that peer review has the potential to be procompetitive by ensuring that only competent, professional, and otherwise qualified practitioners are permitted to practice at health care institutions. On the other hand, staff privilege decisions can raise a risk of anti-competitive abuse insofar as they are typically made upon the recommendations of members of the medical staff who may be direct or indirect competitors of the physician under review. The courts have recognized that a denial or termination of staff privileges arguably can insulate the other medical staff members from competition by the physician under review . . . .

2 American Bar Association Section of *Antitrust Law, Antitrust Law Developments (Fifth)* 1326-1327 (5th ed. 2002) (footnote omitted).

However, civil [\*\*193] liability under the federal antitrust laws for "anticompetitive" conduct is not without limit.

At the outset of the Final Pretrial Conference, the defendants moved to dismiss the Part I Plaintiffs' antitrust claims on the grounds that (1) the claims are barred by the "state action" doctrine announced in *Parker v. Brown, 317 U.S. 341, 351-353, 63 S. Ct. 307, 87 L. Ed. 315 (1945)*; (2) the claims are barred by the Local Government Antitrust Act of 1984, Pub. L. No. 98-544, 98 Stat. 2750, codified at *15 U.S.C. §§ 34-36 (2000)*; (3) the plaintiffs have failed to identify a specific *antitrust law* violation or plead the essential elements of such a violation; and (4) the plaintiffs have failed to plead an effect on interstate commerce. (Memorandum in Support of Defendants' Motion to Dismiss Plaintiffs' Antitrust Claims, filed November 14, 2002 (dkt.no. 455), at 3-8.)

#### **The Local Government Antitrust Act (*15 U.S.C. §§ 34-36*)**

The Local Government Antitrust Act provides that "no damages, interest on damages, costs, or attorney's fees may be recovered under , 4A, or 4C of the Clayton Act (*15 U.S.C. 15, 15a, or 15c*) from [\*\*194] any local government, or official or employee thereof acting in an official capacity," *15 U.S.C. § 35(a)*, or "based on any official action directed by a local government, or official or employee thereof acting in an official capacity." *15 U.S.C. § 36(a)*. Federal courts are thus precluded "from awarding monetary relief on antitrust claims brought against local government [\*1173] entities." *Thatcher Enterprises v. Cache County Corp., 902 F.2d 1472, (10th Cir. 1990)*.

All that the Defendants need show in order to assert a valid claim of immunity from antitrust liability is that they acted in an official capacity or were directed by government officials or employees who were themselves acting in their official capacities. As previously discussed, these standards do not include a consideration of the defendant's intentions. The court considers only the objective questions: (i) whether, in light of the authority invested in a local government, its officials or employees, the actions complained of were lawful and taken within the scope of their authority, . . . or (ii) whether, if the defendant is not a local government official or employee, the actions were directed by a local government or one [\*\*195] of its officials or employees acting within the scope of his authority.

*Sandcrest, supra, at 1148* (citations omitted).

*Cohn v. Wilkes General Hosp., 767 F. Supp. 111, 113 (W.D.N.C. 1991)* (quoting *Sandcrest Outpatient Services, P.A. v. Cumberland County Hospital, 853 F.2d 1139, 1148 (4th Cir. 1988)*), affirmed, *953 F.2d 154 (4th Cir. 1991)*, cert. denied, 505 U.S. 1230, 112 S. Ct. 3057, 120 L. Ed. 2d 922 (1992). In *Cohn*, the court held that the statute applied to bar a chiropractor's antitrust claim against a municipal hospital, its board of trustees and medical staff arising from the hospital's denial of his request for hospital staff privileges for allegedly anti-competitive reasons.

Applying the Local Government Antitrust Act in the context of this action, it appears to bar the damages claims of plaintiffs MacArthur and Lyman as against the SJHSD, San Juan County, the defendant members of the SJHSD Board, SJHSD's administrators and medical staff, and subordinate employees. Both plaintiffs allege that the members of the SJHSD medical staff--Drs. Redd, Jones and Nelson--acted upon plaintiffs' requests for full staff privileges for anti-competitive purposes, *viz.*, to limit competition [\[\\*\\*196\]](#) by Dr. MacArthur and Ms. Lyman with the SJHSD medical staff for patients in the San Juan County area, and that other defendants at least acquiesced in their doing so, in their capacity as SJHSD Board members, administrators or County Commissioners. ( See Proposed Amended Complaint at 26-34 PP1-49 ("Specific Statements of Facts -- Anti-Trust Claims"); *id.* at 34-58 PP50-168 ("Facts for [42 USC 1983](#), and antitrust and RICO claims"); *id.* at 58-86 PP125-230 (same).)

#### **Dr. MacArthur's Federal Antitrust Law Claim**

By the time of pretrial, Dr. MacArthur's federal antitrust claim against the defendants sought only an award of treble damages under § 4 of the Clayton Act, [15 U.S.C. § 15](#). Applying the Local Government Antitrust Act to that claim leaves no viable federal antitrust claim remaining.

Apart from this statutory preclusion, Dr. MacArthur's federal antitrust claim fails on its own facts.

Plaintiffs insist that a denial of the full provisional SJHSD staff privileges requested by Dr. MacArthur in December of 1999 would be anti-competitive in both purpose and effect. Whatever force that argument may have, the fact remains uncontested that the SJHSD did not deny privileges to Dr. MacArthur [\[\\*\\*197\]](#) before he elected to move his practice out of state. The SJHSD, under the authorizing signatures of Mr. Bradford and Dr. Redd, granted Dr. MacArthur "temporary" staff privileges two weeks after he made his [\[\\*1174\]](#) request for full one-year provisional privileges, and extended those privileges twice through February 2, 2000. During that interim period, Dr. MacArthur exercised his temporary privileges in providing care for his patients, and he does not allege specific facts showing that he was unable to provide care for any particular patient because of any limitation of those privileges by number or duration.

Even taking as true Dr. MacArthur's allegation that his request for full privileges was placed in the hands of other SJHSD staff physicians with whom he was competing for patients--competitors who would put their own economic interests first in making such a determination--he has failed to allege any actionable "antitrust injury" to his practice during the brief period of time in which he was exploring the San Juan County market for obstetrics and gynecological care. As explained above, [§ 4](#) of the Clayton Act "requires a plaintiff to show actual injury," [Cargill, Inc., 479 U.S. at 111](#), [\[\\*\\*198\]](#) and "the plaintiff must still allege an injury of the type the antitrust laws were designed to prevent." *Id.* (footnote omitted).

Moreover, because there no final determination by the SJHSD to deny Dr. MacArthur the privileges he sought, his federal antitrust claim, like his [§ 1983](#) claim, was not ripe at the time he elected to move his practice out of the area, and, thereafter was rendered moot by his absence from the San Juan County health care services market after March of 2000. See [Unity Ventures v. Lake County, 841 F.2d at 776-777](#) (absent final governmental action denying intended use of property, federal antitrust claim based on local land use regulation was not ripe).

Consequently, Dr. MacArthur's federal antitrust law claims must be dismissed as against all defendants. [Fed. R. Civ. P. 16\(c\)\(1\)](#).

#### **Ms. Lyman's Federal Antitrust Law Claim**

As explained above, the effect of the Local Government Antitrust Act, [15 U.S.C. § 35\(a\)](#), is to bar plaintiff Lyman's federal antitrust claim for treble damages against the defendants, limiting that claim to a request for declaratory and injunctive relief.

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As explained above, to on a private civil claim under § 4 of the Clayton Act, [15 U.S.C. § 15](#), [\[\\*\\*199\]](#) "a private plaintiff must establish both (1) that it has standing and (2) the defendant has violated the antitrust laws. . . ." 2 Phillip E. Areeda, Herbert Hovencamp & Roger D. Blair, [Antitrust Law](#) P335, at 297. "Once it appears, whether early or late in the litigation, that either requirement [of standing or antitrust violation] is lacking, the suit must be dismissed." *Id.* Likewise, [§ 16](#) of the Clayton Act permits injunctive relief "against threatened loss or damage by a violation of the antitrust laws." [15 U.S.C. § 26](#) (emphasis added).

Plaintiff Lyman claims that one or more of the defendants have violated the antitrust laws, but does not allege the specific nature of that violation. ( See Proposed Amended Complaint at 26-34 PP1-49; *id.* at 34-58 PP50-168; *id.* at 58-86 PP125-230.) Gleaning the elements of a particular [antitrust law](#) violation from the dense thicket of the plaintiffs' pleadings, original or amended, proves a daunting and largely fruitless task.

Taking action that is intended to disadvantage a competitor, or that has that effect, intended or not, by itself does not violate the antitrust laws. Yet plaintiff Lyman has alleged little more than that one or more SJHSD medical [\[\\*\\*200\]](#) staff defendants--Drs. Redd, Jones and Nelson-- [\[\\*1175\]](#) took their own economic interests into consideration when addressing matters involving the plaintiff's practice privileges at SJHSD facilities in 1999, or that the effect of one or another limitation upon Ms. Lyman's privileges as a Physician Assistant operated to limit her ability to compete directly with physicians in the market for medical care in the San Juan County area.

Moreover, according to Ms. Lyman's counsel, Ms. Lyman did not have SJHSD privileges after December 22, 1999, the date her existing privileges expired, her request for renewal of her privileges in December 1999 ultimately was denied, and she made no further application for SJHSD privileges after that date:

THE COURT: Did she subsequently apply again for privileges at the hospital?

MS. ROSE: No, sir.

THE COURT: The district, she never applied again?

MS. ROSE: No, Sir.

(Tr. 11/15/02, at 53:13-17.) Thus, there exists no currently existing controversy between Ms. Lyman and the defendants concerning her entitlement to exercise of staff privileges at SJHSD facilities or the potential for denial of those privileges in violation of the federal antitrust laws. In this context, [\[\\*\\*201\]](#) any claim for declaratory relief under [28 U.S.C. §§ 2201-2202](#) has "become moot because a declaratory judgment would no longer have any effect on defendants' behavior. See [Utah Animal Rights Coalition v. Salt Lake City Corp.](#), 371 F.3d 1248, 1256-57 (10th Cir. 2004) (holding that an action for declaratory relief was moot when the requested declaration involved past conduct not likely to recur)." [GF Gaming Corp. v. City of Black Hawk, Colo.](#), 405 F.3d 876, 883 (10th Cir. 2005); see [Cox v. Phelps Dodge Corp.](#), 43 F.3d 1345, 1348 (10th Cir. 1994) ("What makes a declaratory judgment action 'a proper judicial resolution of a 'case or controversy' rather than an advisory opinion is the settling of some dispute which affects the behavior of the defendant toward the plaintiff.'") (quoting [Hewitt v. Helms](#), 482 U.S. 755, 761, 107 S. Ct. 2672, 96 L. Ed. 2d 654 (1987)).<sup>85</sup>

<sup>85</sup> As the court of appeals recently elaborated:

It is not enough that a plaintiff wishes to have the moral satisfaction of a judicial ruling that he was right and his adversary was wrong; the relief sought must have legal effect in determining the present and future rights and obligations of the parties. "The crucial question is whether [\[\\*\\*202\]](#) 'granting a present determination of the issues offered . . . will have some effect in the real world.'" [Citizens for Responsible Gov't State Political Action Comm. v. Davidson](#), 236 F.3d 1174, 1182 (10th Cir. 2000), quoting [Kennecott Utah Copper Corp. v. Becker](#), 186 F.3d 1261, 1266 (10th Cir. 1999); see also [Colorado Off-Highway Vehicle Coalition v. United States Forest Serv.](#), 357 F.3d 1130, 1133 (10th Cir. 2004) ("A 'case or controversy' no longer exists when it is impossible for the court to grant any effectual relief whatsoever to a prevailing party."); [Air Line Pilots Assn., Int'l v. UAL Corp.](#), 897 F.2d 1394, 1396-97 (7th Cir. 1990) (the test is whether the relief sought would "make a difference to the legal interests of the parties (as distinct from their psyches, which might remain deeply engaged with the merits of the litigation)").

[Utah Animal Rights Coalition v. Salt Lake City Corp.](#), 371 F.3d 1248, 1263 (10th Cir. 2004).

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Similar mootness problems afflict Ms. Lyman's request for injunctive relief. See, e.g., [Facio v. Jones, 929 F.2d 541, 544 \(10th Cir. 1991\)](#) ("plaintiff cannot maintain a declaratory or injunctive action unless he or she can demonstrate a good chance of being [\*\*203] likewise injured in the future"); Moreover, if, as the Proposed Amended Complaint indicates, Ms. Lyman seeks injunctive relief "to protect patients of Mrs. Lyman and her supervising physician, and [\*1176] give Mrs. Lyman's patients uniform and considerate care with District staff sensitive to the unique needs of the patient," and allowing Ms. Lyman "to minimally go into any facility to at least speak and associate with her patient, regardless of whether she has privileges at the District," (Proposed Amended Complaint at 93), that relief would not be granted as "against threatened loss or damage by a violation of the antitrust laws" as provided by § 16 of the Clayton Act, [15 U.S.C. § 26](#). Nor would "ordering the [SJHSD] governance board to make physicians and chiefs of staff accountable for patient complaints and treat all medical providers and physician's equally and uniformly," (Proposed Amended Complaint at 94), be tailored to redress a specific antitrust violation.

As framed in plaintiffs' pleadings, Ms. Lyman's claim under the federal antitrust laws did not assert an arguable legal theory at the time of pretrial.

#### (10) [Utah Constitution, art. I, §§ 1, 7, 25, 26, 27](#)

The Part I Plaintiffs [\*\*204] point to several provisions of the Utah Constitution as a footing for their allegations of "due process violations" or "violation of Mrs. Valdez' Utah Constitutional rights" by the defendants, (Proposed Amended Complaint at 11 P(3), 14 P(23)):

##### **Article I, [Section 1. \[Inherent and inalienable rights.\]](#)**

All men have the inherent and inalienable right to enjoy and defend their lives and liberties; to acquire, possess and protect property; to worship according to the dictates of their consciences; to assemble peaceably, protest against wrongs, and petition for redress of grievances; to communicate freely their thoughts and opinions, being responsible for the abuse of that right.

\*\*\*

##### **Article I, [Section 7. \[Due process of law.\]](#)**

No person shall be deprived of life, liberty or property, without due process of law.

\*\*\*

##### **Article I, [Section 25. \[Rights retained by people.\]](#)**

This enumeration of rights shall not be construed to impair or deny others retained by the people.

##### **Article I, [Section 26. \[Provisions mandatory and prohibitory.\]](#)**

The provisions of this Constitution are mandatory and prohibitory, unless by express words they are declared to be otherwise.

##### **Article I, [Section 27. \[\\*\\*205\] \[Fundamental rights.\]](#)**

Frequent recurrence to fundamental principles is essential to the security of individual rights and the perpetuity of free government.

[Utah Const., art. I, §§ 1, 7, 25-27. The Utah Constitution's Due Process Clause, Article I, § 7](#), provides a footing for a direct private right of action seeking a remedy for an alleged deprivation of life, liberty or property, but only in "appropriate"--that is, extraordinary--circumstances:<sup>86</sup>

<sup>86</sup> The source of judicial authority to grant relief in "appropriate circumstances" in Utah is the common law:

20. We begin by identifying the source of our authority to award damages for constitutional violations. Except for the [Takings Clause](#), the Utah Constitution does not expressly provide damage remedies for constitutional violations. Thus, aside from the [Takings Clause](#), there is no textual constitutional right to damages for one who suffers a constitutional tort. Nor has the legislature enacted any laws authorizing damage claims for constitutional violations in general, or the violation of the [Due Process Clause](#) or the [Open Education Clause](#) in particular. Thus, there is no express statutory right to damages

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[\*1177] 22. To ensure that damage actions are permitted only "under appropriate circumstances," we therefore hold that a plaintiff must establish the following three elements before he or she may proceed with a private suit for damages.

23. First, a plaintiff must establish that he or she suffered a "flagrant" violation of his or her constitutional rights. See *Dick Fischer Dev. v. Department of Admin.*, 838 P.2d 263, 268 (Alaska 1992); see also *Bott*, 922 P.2d at 734-35, 739-40 (describing the level of defendants' culpability necessary to create damages liability). In essence, this means that a defendant must have violated "clearly established" constitutional rights "of which a reasonable person would have known." *Harlow v. Fitzgerald*, 457 U.S. 800, 818, 102 S.Ct. 2727, 73 L.Ed.2d 396 (1982). [\*\*206] To be considered clearly established, "the contours of the right must be sufficiently clear that a reasonable official would understand that what he is doing violates that right." *Anderson v. Creighton*, 483 U.S. 635, 639-40, 107 S.Ct. 3034, 97 L.Ed.2d 523 (1987) (citations omitted). The requirement that the unconstitutional conduct be "flagrant" ensures that a government employee is allowed the ordinary "human frailties of forgetfulness, distractibility, or misjudgment without rendering him or herself liable for a constitutional violation." *Bott*, 922 P.2d at 739-40.

24. Second, a plaintiff must establish that existing remedies do not redress his or her injuries. See *Schweiker v. Chilicky*, 487 U.S. 412, 425, 108 S.Ct. 2460, 101 L.Ed.2d 370 (1988) (refusing to create a damages remedy for an alleged due process violation where Congress had provided meaningful safeguards or remedies); *Bush v. Lucas*, 462 U.S. 367, 378, 103 S.Ct. 2404, 76 L.Ed.2d 648 (1983) (same with respect to alleged First Amendment violation); *Dick Fischer Dev.*, 838 P.2d at 268; *Bonner v. City of Santa Ana*, 45 Cal.App.4th 1465, 53 Cal.Rptr.2d 671, 673, 676-78 (1996) (refusing to create damages remedy for [\*1178] alleged due [\*\*207] process violation where alternative common law tort cause of action existed); *Restatement (Second) of Torts* § 874A cmt. h, at 309 (suggesting courts should consider the adequacy of existing remedies when deciding whether to provide a tort remedy). This second requirement is meant to ensure that courts use their common law remedial power cautiously and in favor of existing remedies. See *Lynch v. Jacobsen*, 55 Utah 129, 138-39, 184 P. 929, 933 (1919). We urge caution in light of the myriad policy considerations involved in a decision to award damages against a governmental agency and/or its employees for a constitutional violation. Moreover, we urge deference to existing remedies out of respect for separation of powers' principles. In general, the legislative branch has the authority, and in many cases is better suited, to establish appropriate remedies for individual injuries. By requiring courts to defer to relevant legislative determinations of appropriate remedies, we respect the legislature's important role in our constitutional system of government.

for one who suffers a constitutional tort. In the absence of applicable constitutional or statutory authority, Utah courts employ the common law. See *Utah Code Ann. § 68-3-1* (1996). Under the common law, "individuals had access to remedies of money damages for violations of their individual rights, and these rights, enumerated in fundamental documents, were the forerunners of many of the provisions adopted in federal and state bills of rights." *Bott*, 922 P.2d at 739 [\*\*210] (citations omitted). Hence, a Utah court's ability to award damages for violation of a self-executing constitutional provision rests on the common law. The *Restatement (Second) of Torts* supports this view. *Restatement section 874A* states that when no specific remedy is mentioned, a court may accord an appropriate remedy to one injured from the violation of a constitutional provision. See *Restatement (Second) of Torts* § 874A & cmt. a (1979). *Comment (g) to section 874A* suggests that a court's authority to do so arises from the common law. See *id.* cmt. g, at 306-07; see also Jennifer Friesen, *State Constitutional Law* § 7-5(c) (2d ed. 1996) (stating that *section 874A* espouses a common law doctrine).

21. This common law ability to award damages for constitutional violations requires policy decisions by the court, and it should be aware of them and face them candidly. . . . The court is not required to provide the civil remedy, and yet judicial tradition gives it the authority to do this under appropriate circumstances. The court has discretion and it must be careful to exercise that discretion cautiously and soundly.

*Restatement § 874A cmt. d*, at 303.

*Spackman ex rel. Spackman v. Board of Educ. of Box Elder County School Dist.*, 2000 UT 87, PP20-21, 16 P.3d 533, 537-538 [\*\*211] (quoting *Bott v. DeLand*, 922 P.2d 732, 739 (Utah 1996)) (footnotes omitted).

25. Third, a plaintiff must establish that equitable relief, such as an injunction, was and is wholly inadequate to protect the plaintiff's [\*\*208] rights or redress his or her injuries. See, e.g., *Bott, 922 P.2d at 739* (stating that "if prisoners' rights under article I, section 9 are violated, injunctive relief may not be adequate to remedy prisoners' injuries"); see also, e.g., *Davis v. Passman, 442 U.S. 228, 245, 99 S.Ct. 2264, 60 L.Ed.2d 846 (1979)* (stating that damages are an appropriate remedy where plaintiff was unconstitutionally terminated from her job on a congressional staff because, in part, "equitable relief in the form of reinstatement would be unavailing" in light of the fact that her former employer was no longer a congressman); cf. *Rockhouse Mountain Property Owners Ass'n, Inc. v. Town of Conway, 127 N.H. 593, 503 A.2d 1385, 1388 (1986)* (stating that damages are an inappropriate remedy for a constitutional violation where the alleged injury "can be undone" by the judiciary). This final requirement is meant to take advantage of the meaningful role equitable relief can play in redressing constitutional injuries, while not implicating so many of the difficult policy considerations raised by a decision to award damages.

[Spackman ex rel. Spackman v. Board of Educ. of Box Elder County School Dist., 2000 UT 87, PP22-25, 16 P.3d 533, 538-539](#) [\*\*209] (footnotes omitted).

The Part I Plaintiffs have not even attempted to plead these three essential elements of a direct civil action under the Utah Constitution in either the Proposed Amended Complaint and the Proposed Pretrial Order. They did not raise them as issues at the Final Pretrial Conference. Nor have they addressed them in the legal memoranda submitted either prior to the Final Pretrial Conference, or since. "Failure of counsel to identify an issue for the court can result in waiver: 'If counsel fail to identify an issue for the court, the right to have the issue tried is waived.' *Fed.R.Civ.P. 16* advisory committee's note." *Smith v. Gulf Oil Co., 995 F.2d 638, 644 (6th Cir. 1993)*.

Besides failing to address the essential elements of a direct civil action under the Utah Constitution, the Part I Plaintiffs have not identified the specific constitutional right(s) that come within the scope of Article I, §§ 1, 25, 26, and 27, that purportedly have been violated by the conduct of one or more of the defendants.

To date, the reported case law construing the Article I, § 25 "retained rights" provision has involved parental rights [\*\*212] issues. [\*1179] See, e.g., *In re P., 648 P.2d 1364 (Utah 1982)*; *In re K.B.E., 740 P.2d 292 (Utah Ct. App. 1987)*; *T.R.F. v. Felan, 760 P.2d 906 (Utah Ct. App. 1988)*; *P.O. v. S.G., 927 P.2d 202 (Utah Ct. App. 1996)*; *J.R. v. State of Utah, 261 F. Supp. 2d 1268 (D. Utah 2003)*. Article I, §§ 26 and 27 appear to be declaratory of general constitutional principles rather than an enumeration of individual constitutional rights as such. See *Ritchie v. Richards, 14 Utah 345, 361-363, 47 P. 670 (1896)* (Bartch & Miner, JJ.) (constitutional provisions prescribing formalities to be observed in the enactment of laws are mandatory and binding on the legislature); see generally Comment, *Fundamental Principles, Individual Rights, and Free Government: Do Utahns Remember How to Be Free?, 1996 Utah L. Rev. 661* ("exploring the meaning of [art. I] Section 27 of the Utah Constitution").

Having considered the pleadings, proffers, arguments and memoranda submitted by counsel, the court cannot "identify the litigable issues" that plaintiffs believed would arise under these provisions. See *Fed. R. Civ. P. 16(c)(1)*; see also *Fed. R. Civ. P. 8(a)(2)*; *Fed. R. Civ. P. 11(b)*; *Chavez v. New Mexico, 397 F.3d 826, 839 (10th Cir. 2005)* [\*\*213] ("the Court refuses to go on a fishing expedition in search of legal analysis and facts to support these claims").

#### (11) Utah Unfair Practices Act ([Utah Code Ann. §§ 13-5-1 et seq.](#) (2001))

The Utah Unfair Practices Act, [Utah Code Ann. §§ 13-5-1 through 13-5-18](#) (2001), disallows the use of a list of specific unfair trade practices by persons "engaged in commerce," including anti-competitive price discrimination,<sup>87</sup>

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<sup>87</sup> [Utah Code Ann. § 13-5-3](#) [\*\*215] (2001). [Section 13-5-3\(1\)\(a\)](#) provides:

(1)(a) It is unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchasers involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the state and where the effect of such discrimination may be substantially to lessen competition or tend to

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advertising or sale of goods at a price less than cost,<sup>88</sup> and advertising goods, wares, or merchandise that the advertiser is not prepared to supply.<sup>89</sup> These forbidden practices involve trade in "goods," "merchandise," "articles," "products" and "commodities," and services or facilities furnished in connection with such trade, as well as the services of someone "who performs work upon, renovates, alters or improves any personal property belonging to another person, except necessary repairs due to damage in transit . . . ." *Utah Code Ann. § 13-5-12(2)* (2001). As the Utah Supreme Court explains, "The immediate stimuli for the enactment of such acts were in part the rapid rise of chain stores, and in part the general sharpening of [\*1180] competitive practices under pressure of the [\*\*214] depression." *Burt v. Woolsulate, Inc.*, 106 Utah 156, 160, 146 P.2d 203 (1944).

One of the practices aimed at by these [Unfair Practices Acts] statutes is that, common in chain stores, of selling at lower prices in one locality than in another and making up losses incurred by profits in other stores. Even more important in the application of anti-discrimination statutes today is the prevention of discrimination sales by manufacturers to customers with unusually strong bargaining power who can force large price concessions. . . .

On the whole the anti-discrimination provisions of the Unfair Practices Acts seem best fitted to reach manufacturers and producers who, in the past have placed certain retail buyers in preferred competitive positions by giving them special, rebates or other price favors. . . .

*Id.* (quoting Comment, *Prohibiting Price Discrimination and Sales Below Cost: The State Unfair Practices Acts*, 32 Ill. L. Rev. 816 (1938)); see also 54A Am. Jur. 2d *Monopolies, etc.* §§ 1077-1106 (1997); Annot., *Validity, Construction and Application of State Statutory Provision Prohibiting Sales of Commodities Below Cost-Modern Cases*, 41 A.L.R. 4th 612 (1985).<sup>90</sup>

create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them.

<sup>88</sup> *Utah Code Ann. § 13-5-7(1)* (2001):

(1) It is hereby declared that any advertising, offer to sell, or sale of any merchandise, either by retailers or wholesalers, at less than cost as defined in this act with the intent and purpose of inducing the purchase of other merchandise or of unfairly diverting trade from a competitor or otherwise injuring a competitor, impairs and prevents fair competition, injures public welfare, is unfair competition contrary to [\*\*216] public policy and the policy of this act and is declared to be a violation of this act.

See also *Utah Code Ann. § 13-5-9* (2001) (selling goods in quantity below cost); *Utah Code Ann. § 13-5-10* (2001) (advertising and segregation of below-cost goods at forced liquidation or close-out sales).

<sup>89</sup> *Utah Code Ann. § 13-5-8* (2001).

<sup>90</sup> In *Trade Comm. v. Skaggs Drug Centers, Inc.*, 21 Utah 2d 431, 446 P.2d 958 (Utah 1968), the Utah Supreme Court upheld the constitutionality of the Utah Unfair Practices Act, and elaborated upon its purpose:

It has been argued that the purpose of statutes such as the Utah Unfair Practices Act is to preserve a competitive climate by preventing large business concerns through the unrestrained use of size and resources alone, from overwhelming and destroying their smaller competitors. These statutes it is claimed seek to preserve the right of a competitor to enter a market and compete with those already operating.

It has been further argued that unrestrained price cutting on a massive scale has had disastrous effect on the small independent retailer with limited resources. That the below cost selling has become a weapon in the fight for markets and customers, characterized [\*\*217] by the deliberate use of below cost selling to undercut, overwhelm and destroy competition, all to the benefit and further enrichment of the big interests. It is further claimed that to correct the unscrupulous conduct of these vested groups it became necessary for government to adopt such unfair trade practices acts as the one here in question.

Plaintiffs allege "interference with the patients' and plaintiffs MacArthur and Lyman's ability to freely contract for services with the District, with each other, with patients as guaranteed by the . . . Utah Unfair Practices Act," among other laws, (Proposed Pretrial Order at 4 P(8)), and the "violation of the Utah Unfair Practices Act," (*id.* at 4 P(15); Proposed Amended Complaint at 12 P14), but nowhere in their pleadings do they detail the nature of that alleged **[\*\*218]** violation. Instead, plaintiffs appear to cite the Act for its general policy statement "fostering economic competition," <sup>91</sup> and as a footing for an award of treble damages. (Proposed **[\*1181]** Amended Complaint at 26 P2; *id.* at 97 (Prayer for Relief) ("Mrs. Lyman is praying for damages in excess of Six (6) Million Dollars, some of which is treble damages, due to unfair practices . . .").)

The Utah Unfair Practices Act does provide for an award of treble damages in favor of a private plaintiff who has been injured by "any act in violation of this chapter" and has sustained actual damages,<sup>92</sup> but such acts would be those expressly defined by the Act as "a violation of this act" or as "unlawful." Neither the Act's general purpose "to safeguard the public against the creation **[\*\*219]** or perpetuation of monopolies and to foster and encourage competition" nor the "liberal construction" of its terms can extend civil liability--or the Act's criminal sanctions--beyond the "unfair and discriminatory practices" expressly "prohibited" by the Act itself. [Utah Code Ann. § 13-5-17](#) (2001).

Where, as here, the plaintiffs fail to plead or otherwise identify acts by one or more defendants that violate the Utah Unfair Practices Act's specific provisions, neither the conclusory allegation of a violation **[\*\*220]** nor the generalized assertion of interference with freedom of contract can sustain their treble damages claims under that Act.

#### **(12) Utah Civil Rights Act ([Utah Code Ann. §§ 13-7-1 et seq.](#)(2001))**

[Utah Code Ann. § 13-7-3](#) (2001) reads:

##### **13-7-3. Equal right in business establishments, places of public accommodation, and enterprises regulated by the state.**

All persons within the jurisdiction of this state are free and equal and are entitled to full and equal accommodations, advantages, facilities, privileges, goods and services in all business establishments and in all places of public accommodation, and by all enterprises regulated by the state of every kind whatsoever, without discrimination on the basis of race, color, sex, religion, ancestry or national origin. Nothing in this act shall be construed to deny any person the right to regulate the operation of a business establishment or place of public accommodation or an enterprise regulated by the state in a manner which applies uniformly to all

We do not suggest that a purpose to divert or capture a competitor's business is wrong or unethical. It is perfectly legitimate so long as it is not carried out unfairly. The legislature simply has declared it unfair to accomplish it through giving away goods or services or selling them for less than cost.

*Id.*, 21 Utah 2d at 438, 441, 446 P.2d at 962-963, 965 (footnote omitted).

<sup>91</sup> [Utah Code Ann. § 13-5-17](#) (2001) reads: **Policy of act.**

The Legislature declared that the purpose of this act is to safeguard the public against the creation or perpetuation of monopolies and to foster and encourage competition, by prohibiting unfair and discriminatory practices by which fair and honest competition is destroyed or prevented. This act shall be liberally construed that its beneficial purposes may be subserved.

<sup>92</sup> Under [Utah Code Ann. § 13-5-14](#) (2001):

Any person or the state of Utah may maintain an action to enjoin a continuance of any act in violation of this chapter, and, if injured by the act, for the recovery of damages. If, in such action, the court finds that the defendant is violating or has violated any of the provisions of this chapter, it shall enjoin the defendant from a continuance of the violation. It is not necessary that actual damages to the plaintiff be alleged or proved. In addition to such injunctive relief, the plaintiff is entitled to recover from the defendant three times the amount of the actual damages sustained or \$ 2,000, whichever is greater, plus court costs.

persons without regard to race, color, sex, religion, ancestry, or national origin; or to deny any religious organization the right to regulate the operation and procedures of its establishments. [\*\*221]

This explicit guarantee of equal treatment reflects Utah's public policy "to assure all citizens full and equal availability of all goods services and facilities offered by" business establishments, places of public accommodation and state-regulated enterprises "without discrimination because of race, color, sex, religion, ancestry, or national origin," and the State's recognition since 1965 that "the practice of discrimination on the basis of race, color, sex, religion, ancestry, or national origin . . . endangers the health, safety, and general welfare of this state and its inhabitants." [Utah Code Ann. § 13-7-1](#) (2001).<sup>93</sup> [Section 13-7-4\(3\)](#) [\*1182] provides that "any person who is denied the rights provided for in [Section 13-7-3](#) shall have a civil action for damages and any other remedy available in law or equity against any person who denies him the rights provided for in [Section 13-7-3](#) or who aids, incites or conspires to bring about such denial."

Plaintiffs' pleading alleges the "violation of Mrs. Valdez' state right to receive services equally with all other patients as found in [Utah Code Ann. 13-7-2](#)," (Proposed Amended Complaint at 13 P(21)), but she does not allege specific facts showing discrimination against her on the basis of *her* race, color, sex, religion, ancestry or national origin, or plead specific facts from which such discrimination may reasonably be inferred. Nor does she allege specific facts showing that she was denied "full and equal accommodations, advantages, facilities, privileges, goods and services" in a "place[] of public accommodation," as guaranteed by the Utah statute.

### **(13) Interference with Contract and with Prospective Business Relations**

The tort of "interference with contract" addresses "conduct which 'intentionally and improperly interferes with the performance of a contract . . . between another and a third person by inducing or otherwise causing the third person not to perform the contract.' [Restatement \(Second\) of Torts § 766](#) (1979). See also [Bunnell v. Bills](#), 13 Utah 2d 83, 90, 368 P.2d 597, 602 (1962); W. Prosser, *Handbook* [\*223] of the Law of Torts § 129 at 929-30 (4th ed. 1971); Annot., 26 A.L.R.2d 1227 (1952)." [Leigh Furniture and Carpet Co. v. Isom](#), 657 P.2d 293 (Utah 1982).

"The tort of intentional interference with prospective economic relations reaches beyond protection of an interest in an existing contract and protects a party's interest in prospective relationships of economic advantage not yet reduced to a formal contract (and perhaps not expected to be)." [Leigh](#), 657 P.2d at 302 (citing [Buckaloo v. Johnson](#), 14 Cal.3d 815, 537 P.2d 865, 868-69, 122 Cal.Rptr. 745, 748-49 (1975); [Restatement \(Second\) of Torts § 766B comment c](#); [Prosser, supra](#), at § 130). In the *Leigh* case, the Utah Supreme Court recognized "a common-law cause of action for intentional interference with prospective economic relations," and adopted the Oregon definition of this tort. *Id. at 304* (citing [Straube v. Larson](#), 287 Ore. 357, 361, 600 P.2d 371, 374 (1979); [Top Service Body Shop, Inc. v. Allstate Insurance Co.](#), 283 Ore. 201, 205, 209, 582 P.2d 1365, 1368, 1371 (1978)). "Under this definition, in order to recover damages, the plaintiff must prove (1) that the defendant intentionally interfered with the plaintiffs existing or potential [\*\*224] economic relations, (2) for an improper purpose or by improper means, (3) causing injury to the plaintiff." *Id.*

The "economic relations" protected by this theory are diverse. "Driving away an individual's existing or potential customers is the archetypical injury this cause of action was devised to remedy. E.g., [Guillory v. Godfrey](#), 134 Cal.App.2d 628, 286 P.2d 474 (1955); [Tuttle v. Buck](#), 107 Minn. 145, 119 N.W. 946 (1909); W. Prosser, *Handbook of the Law of Torts* § 130 (4th ed. 1971); [Restatement \(Second\) of Torts § 766B\(a\)](#)," [Leigh](#), 657 P.2d at 306, but protection extends to "any prospective contractual [\*1183] relations . . . if the potential contract would be of pecuniary value to the plaintiff" (excluding contracts to marry), as well as "a continuing business or other customary relationship not amounting to a formal contract." [Restatement \(Second\) of Torts § 766B comment c](#) (1979).

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<sup>93</sup> This statute was first enacted by the Utah Legislature in 1965, (1965 Utah Laws ch. 174), a watershed year for civil rights, government reform and other significant Utah legislation. A 1973 amendment added discrimination on the basis of sex [\*\*222] to the conduct prohibited by the statute. See 1973 Utah Laws ch. 18, § 3.

The question of interference for an "improper purpose" or by an "improper means" requires the weighing of several relevant factors:

In determining whether an actor's conduct in intentionally interfering with a contract or a prospective contractual relation of another is improper or not, consideration is given **[\*\*225]** to the following factors:

- (a) the nature of the actor's conduct,
- (b) the actor's motive,
- (c) the interests of the other with which the actor's conduct interferes,
- (d) the interests sought to be advanced by the actor,
- (e) the social interests in protecting the freedom of action of the actor and the contractual interests of the other,
- (f) the proximity or remoteness of the actor's conduct to the interference and
- (g) the relations between the parties.

Restatement (Second) of Torts § 767(a)-(g) (1979). As the *Leigh* court observed:

In the rough and tumble of the marketplace, competitors inevitably damage one another in the struggle for personal advantage. The law offers no remedy for those damages--even if intentional--because they are an inevitable byproduct of competition. Problems inherent in proving motivation or purpose make it prudent for commercial conduct to be regulated for the most part by the improper means alternative, which typically requires only a showing of particular conduct.

The alternative of improper purpose will be satisfied where it can be shown that the actor's predominant purpose was to injure the plaintiff. . . .

657 P.2d at 307 (footnote & citations omitted). As the **[\*\*226]** Restatement explains, a competitor's interference with a prospective contractual relation is not improper if, among other things, "his purpose is at least in part to advance his interest in competing with the other." Restatement (Second) of Torts § 768(d) (1979).

*g. The actor's purpose.* The rule stated in this Section developed to advance the actor's competitive interest and the supposed social benefits arising from it. If his conduct is directed, at least in part, to that end, the fact that he is also motivated by other impulses, as, for example, hatred or a desire for revenge is not alone sufficient to make his interference improper. But if his conduct is directed solely to the satisfaction of his spite or ill will and not at all to the advancement of his competitive interests over the person harmed, his interference is held to be improper.

*Id.* § 768 comment g.

The factual allegations underpinning Dr. MacArthur's and Ms. Lyman's interference claims were considered in some detail at the Final Pretrial Conference

**(14) "state common lawdefamation (also a U.S. Constitutional right to reputation as guaranteed by the Ninth Amendment)"**

**(a) Utah Law of Defamation**

"At its core, an action for **[\*\*227]** defamation is intended to protect an individual's interest in maintaining a good reputation." West v. Thomson Newspapers, 872 P.2d 999, 1008 (Utah 1994); see Seegmiller v. KSL, Inc., 626 P.2d 968, 973 (Utah 1981) (recognizing that "the integrity of an individual's reputation is essential to his standing [**\*1184**] in society, in his vocation, and even in his family").

In order to state a claim for defamation under Utah law, a plaintiff must show "that defendants published the statements concerning him [either in print or by spoken words], that the statements were false, defamatory, and not subject to any privilege, that the statements were published with the requisite degree of fault, and that their publication resulted in damage." West, 872 P.2d at 1007-08 (footnotes omitted).

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*Wayment v. Clear Channel Broadcasting, Inc.*, 2005 UT 25, P18 n.2, 116 P.3d 271, 2005 WL 858167; see *DeBry v. Godbe*, 1999 UT 111, P8, 992 P.2d 979, 982; <sup>94</sup> *Cox v. Hatch*, 761 P.2d 556, 561 (Utah 1988); *Seegmiller v. KSL, Inc.*, 626 P.2d 968, 974, 976 (Utah 1981); *Berry v. Moench*, 8 Utah 2d 191, 331 P.2d 814, 818-19, 820-21 (1958); *Utah Code Ann. §§ 45-2-2* (1998); Tracy H. Fowler, Note, *Modernizing Defamation Law in Utah*, [\*\*228] 1980 Utah L. Rev. 535; see also *Restatement (Second) of Torts § 558* (1972). <sup>95</sup> Under Utah law, "a statement is defamatory if it impeaches an individual's honesty, integrity, virtue, or reputation and thereby exposes the individual to public hatred, contempt, or ridicule." *West*, 872 P.2d at 1008 (citing *Cox*, 761 P.2d at 561 (citing *Utah Code Ann. § 45-2-2(1)*)). "A court simply cannot determine whether a statement is capable of sustaining a defamatory meaning by viewing individual words in isolation; rather, it must carefully examine the context in which the statement was made, giving the words their most common and accepted meaning." *Id. at 1009* (citations omitted).

As detailed most recently in the *Wayment* opinion, the question of "requisite degree of fault" that must be shown largely turns upon whether the plaintiff is in some sense a "public figure." *2005 UT 25, PP17-36, 116 P.3d 271*. If a plaintiff is a non-"public" private individual, "the necessary degree of fault which must be shown in a defamation action . . . is negligence." *Seegmiller*, 626 P.2d at 973; accord, *In re I.M.L. v. State of Utah*, 2002 UT 110, P25, 61 P.3d 1038, 1045 ("in a civil action for libel 'actual malice' is required if the statement concerns a public official, whereas only negligence is required if the statement concerns a private citizen"); see *50 Am. Jur. 2d Libel and Slander § 21* (1995).

### (b) Defamation & the *Ninth Amendment*

Plaintiffs have not cited and this court has not found Supreme Court or Tenth Circuit [\*\*230] case authority recognizing "a U.S. Constitutional right to reputation as guaranteed by the *Ninth Amendment*," (Proposed Amended Complaint at 12 P(6)), at least as a theory of legal liability for injury to reputation independent of state defamation law.

Given that "it cannot be presumed that any clause in the constitution is intended to be without effect," *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 174, [\*1185] 2 L. Ed. 60 (1803), the *Ninth Amendment* must be afforded a stature greater than that of a mere "inkblot," <sup>96</sup> and recent scholarship argues various approaches to its interpretation. <sup>97</sup> At

<sup>94</sup> According to *DeBry v. Godbe*,

To establish her claim for defamation, the plaintiff must demonstrate that (1) the defendant published the statements in the letter concerning Ms. DeBry; (2) the statements were false; (3) the statements were not subject to privilege; (4) the statements were published with the requisite degree of fault; and (5) the statements resulted in damages. See *West v. Thomson Newspapers*, 872 P.2d 999, 1007-08 (Utah 1994).

<sup>95</sup> The *Restatement (Second) of Torts § 558* identifies four elements necessary in [\*\*229] order to establish a cause of action in defamation: (a) a false and defamatory statement concerning another; (b) an unprivileged publication to a third party; (c) fault amounting at least to negligence on the part of the publisher; and (d) either actionability of the statement irrespective of special harm or the existence of special harm caused by the publication.

<sup>96</sup> (in the words of Judge Robert Bork, *The Bork Disinforms*, Wall St. J., Oct. 5, 1987, at 22.)

<sup>97</sup> See, e.g., *The Rights Retained by the People: The History and Meaning of the Ninth Amendment* (Randy E. Barnett ed. 1989); *The Rights Retained by the People: The Ninth Amendment and Constitutional Interpretation, Volume II* (Randy E. Barnett ed. 1993); *The Bill of Rights: Original Meaning and Current Understanding* 419-451 (Eugene W. Hickok, Jr., ed. 1991); Congressional Research Service, Library of Congress, *The Constitution of the United States of America: Analysis and Interpretation* 1503-1505 (1992 ed.); Kurt T. Lash, *The Lost Jurisprudence of the Ninth Amendment*, 83 Tex. L. Rev. 597 (February 2005); Kurt T. Lash, *The Lost* [\*\*232] *Original Meaning of the Ninth Amendment*, 83 Tex. L. Rev. 331 (2004); Christopher J. Schmidt, *Revitalizing the Quiet Ninth Amendment: Determining Unenumerated Rights and Eliminating Substantive Due Process*, 32 U. Balt. L. Rev. 169 (2003); Akhil Reed Amar, *The Bill of Rights* 119-133 (1998); John Hart Ely, *Democracy and Distrust--a Theory of Judicial Review* 34-41 (1980); Charles A. Black, Jr., *Decision According to Law* (1981); Raoul Berger, *The Ninth Amendment*, as Perceived by Randy Barnett, 88 Nw. U.L. Rev. 1508 (1994); Raoul Berger, *Suzanna*

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a minimum, the [Ninth Amendment](#) serves as a "constitutional 'saving clause'" <sup>98</sup> avoiding an overly narrow construction of the [Bill of Rights](#). While it may or may not "constitute[] an independent source of rights protected from infringement by either the States or the Federal Government," the [Ninth Amendment](#) "shows a belief of the Constitution's authors that fundamental rights exist that are not expressly enumerated in the first eight amendments and an intent that the list of rights included there not be deemed exhaustive." [Griswold v. Connecticut, 381 U.S. 479, 492, 85 S. Ct. 1678, 14 L. Ed. 2d 510 \(1965\)](#) [\*\*231] (Goldberg, J., concurring).

The [Fifth](#) and [Fourteenth Amendments](#) protect certain fundamental personal liberties from abridgment by the Federal Government or the States. . . . The [Ninth Amendment](#) simply shows the intent of the Constitution's authors that other fundamental personal rights should not be denied such protection or disparaged in any other way simply because they are not specifically listed in the first eight constitutional amendments.

*Id.* (citations omitted).

One recent commentary asserts that reading the [Ninth Amendment](#) in light of the original intent of the Framers (and in particular, James Madison) requires the courts to strike a balance between the competing constitutional right to free speech and non-constitutional legal rights to reputation, but rejects the view that the [Ninth Amendment](#) elevates the right to [\*1186] reputation to constitutional status. Laurence Claus, *Protecting Rights from Rights: Enumeration, Disparagement, and the Ninth Amendment*, 79 *Notre Dame L. Rev.* 585, 587 (2004) (the "right to reputation is not relevantly denied or disparaged unless listing certain rights in the Constitution is construed to leave reputation less protected than it would otherwise have been" under state laws, at least as they existed in 1789 or 1791.) This raises the question whether, e.g., the vindication of [First Amendment](#) interests in free expression [\*\*234] at the expense of state defamation laws protecting the reputation of "public figures" serves "to deny or disparage" unenumerated rights "retained by the people" contrary to the [Ninth Amendment](#). See *id. at 586, 616-621*. However, that issue does not arise here, where no one has asserted that either Dr. MacArthur or Ms. Lyman are "public figures" subject to more limited protection under Utah defamation law. See [Wayment v. Clear Channel Broadcasting, Inc., 2005 UT 25, PP17-36, 116 P.3d 271.](#)

Unless the Part I Plaintiffs are attempting to extend their claims under [42 U.S.C. § 1983](#) to include defamatory injury to reputation (as one among the "rights, privileges, or immunities secured by the Constitution and laws" of the United States),<sup>99</sup> invoking the [Ninth Amendment](#) in the context of their defamation claims does not appear to make

And--the [Ninth Amendment](#), 1994 *B.Y.U. L. Rev.* 51; William Van Alstyne, *Slouching Toward Bethlehem with the Ninth Amendment*, 91 *Yale L. J.* 207 (1981).

<sup>98</sup> At the time of the adoption of the [Bill of Rights](#),

Madison's comments in Congress also reveal the perceived need for some sort of constitutional "saving clause," which, among other things, would serve to foreclose application to the [Bill of Rights](#) of the maxim that the affirmation of particular rights implies a negation of those not expressly defined. See 1 Annals of Cong. 438-440 (1789). See also, e.g., 2 J. Story, *Commentaries on the Constitution of the United States* 651 (5th ed. 1891). Madison's [\*\*233] efforts, culminating in the [Ninth Amendment](#), served to allay the fears of those who were concerned that expressing certain guarantees could be read as excluding others.

[Richmond Newspapers v. Virginia, 448 U.S. 555, 579-80, 100 S. Ct. 2814, 65 L. Ed. 2d 973 & n.15 \(1980\)](#) (Burger, C.J.) (plurality opinion).

<sup>99</sup> The Supreme Court has rejected the assertion of reputation as a discrete interest protected by the [Due Process Clause of the Fourteenth Amendment](#). Reputation alone--apart from some more tangible interests such as employment--does not implicate [\*\*235] any "liberty" or "property" interests sufficient to invoke the procedural protection of the [Due Process Clause](#); hence, to establish a claim under [§ 1983](#) and the [Fourteenth Amendment](#), more must be involved than simply defamation by a state official. [Paul v. Davis, 424 U.S. 693, 701-712, 96 S. Ct. 1155, 47 L. Ed. 2d 405 \(1976\)](#).

[A plaintiff's] interest in reputation is simply one of a number which the State may protect against injury by virtue of its tort law, providing a forum for vindication of those interests by means of damages actions. And any harm or injury to that

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any substantive difference to the legal standards to be applied or the judicial remedies that may be available to them.<sup>100</sup>

**[\*1187] (15) "Federal common law and Utah contract common law and statutory provisions that prohibit contracts of adhesion, bad faith, and lack of fair dealing. Utah Code Ann. 78-12-25(1) (1996)," including the Implied Covenant of Good Faith and Fair Dealing**

Plaintiffs MacArthur and Lyman allege "bad faith void contracts that lack fair dealing," the "denial of their entitlement to a contract with the District that is based upon principles of good faith and fair dealing, with adequate consideration," and "violations of Federal common law and Utah contract common law and statutory provisions that prohibit contracts of adhesion, bad faith, and lack of fair dealing. Utah Code Ann. §§ 78-12-25(1) (1996)." <sup>101</sup> (Proposed Pretrial Order at 4-5 PP(11), (12) & (18).)

#### **(a) Contracts of Adhesion**

"A contract of adhesion is an agreement forced on one party by another who has superior bargaining strength." *Russ v. Woodside Homes, Inc., 905 P.2d 901, 906 n.1 (Utah Ct. App. 1995)* (citing *Wagner v. Farmers Ins. Exch., 786 P.2d 763, 766 n. 2 (Utah Ct. App. 1990)*, <sup>102</sup> overruled on other grounds, *Allen v. Prudential Property and Cas.*

interest, even where, as here, inflicted by an officer of the State, does not result in a deprivation of any "liberty" or "property" recognized by state or federal law, nor has it worked any change of respondent's status as theretofore recognized under the State's laws. For these reasons, we hold that the interest in reputation asserted in this case is neither "liberty" nor "property" guaranteed against state deprivation without due process of law.

*Id.* at 712.

<sup>100</sup> Under Utah law, private civil damages action for common-law defamation are subject to a one-year statute of limitations: "An action may be brought within one year: [\*236] . . . (4) for libel, slander, assault, battery, false imprisonment, or seduction; . . ." Utah Code Ann. § 78-12-29(4) (2002).

"Under Utah law, the statute of limitations begins to run when the cause of action accrues." *Rutherford v. AT & T Communications of the Mt. States, Inc., 844 P.2d 949, 975 (Utah 1992)*; see also Utah Code Ann. § 78-12-1 (2002). "A tort cause of action accrues when all of its elements come into being and the claim is actionable." *Rutherford, 844 P.2d at 975*. Pursuant to Utah Code section 78-12-29(4), "an action may be brought within one year . . . for libel . . . [or] slander." Utah Code Ann. § 78-12-29(4) (2002). "In libel cases, the one-year period of section 78-12-29(4) does not run until the libel is known or is reasonably discoverable by the plaintiff." *Allen v. Ortez, 802 P.2d 1307, 1314 (Utah 1990)*.

*Christensen v. Drossos, 2005 UT App 170, 2005 WL 851700, \*1.*

It appears to be uncontested that in this case, both Dr. MacArthur and Ms. Lyman became aware of the false and malicious rumors allegedly being circulated about them by one or more of the individual defendants contemporaneously with the rumors' circulation. For Dr. MacArthur, the pertinent events [\*237] transpired between October 1999 and March 2000, at which time he relocated to Nevada. Ms. Lyman may have a timely claim for defamatory falsehoods that were known or reasonably discoverable after July 25, 1999, but some of the events of which she complains may have taken place before that date.

<sup>101</sup> Utah Code Ann. § 78-12-25(1) (2002) provides that "an action may be brought within four years:"

(1) upon a contract, obligation, or liability not [\*238] founded upon an instrument in writing; also on an open account for goods, wares, and merchandise, and for any article charged on a store account; also on an open account for work, labor or services rendered, or materials furnished; provided, that action in all of the foregoing cases may be commenced at any time within four years after the last charge is made or the last payment is received;

<sup>102</sup> *Wagner* defined an "adhesion contract" as "a contract entered into between two parties of unequal bargaining strength, expressed in the language of a standardized contract, written by the more powerful bargainer to meet its own needs, and offered to the weaker party on a "take it or leave it basis. . . ."" *786 P.2d at 766 n.2* [\*239] (quoting *Gray v. Zurich Ins. Co., 65 Cal.2d 263, 54 Cal.Rptr. 104, 107, 419 P.2d 168, 171 (1966)*).

Ins. Co., 839 P.2d 798 (Utah 1992)). "In other words, an adhesion contract is one in which the party has no alternative." (*Id.*)

Under Utah law, "adhesion contracts" are not prohibited *per se*. Instead, the Utah Supreme Court has enumerated several equitable doctrines that may be applied to remedy over-reaching in the making of adhesion contracts, including the doctrines of estoppel, waiver, unconscionability, breach of the implied duty of good faith and fair dealing, and the rule that ambiguous language is to be resolved against the drafter. Allen v. Prudential Property and Cas. Ins. Co., 839 P.2d 798, 805-807 & nn. 11-16 (Utah 1992) (rejecting proposed rule that ambiguous insurance contract provisions must be interpreted to effectuate the "reasonable expectations" of the insured). "The existing equitable doctrines, such as waiver, estoppel, and unconscionability, apply to any contractual relationship regardless of context so long as warranted by the facts." *Id. at 806 n.17*.

### (b) Implied Covenant of Good Faith and Fair Dealing

Utah has recognized that all contracts contain a covenant of good faith and fair dealing. Beck v. Farmers Ins. Exchange, 701 P.2d 795, 798 (Utah 1985). [\*1188] As the Utah Supreme Court explained [\*\*240] in Christiansen v. Farmers Ins. Exchange, 2005 UT 21, 116 P.3d 259, 2005 WL 791117:

A breach of express contract claim arises out of the express terms of the contract, and the breach is proven in relation to those terms. See Fairbourn Commercial, Inc. v. Am. Hous. Partners, Inc., 2004 UT 54, P11, 94 P.3d 292 (relying on a contract's express terms to determine the intent of the parties). A claim for breach of the implied covenant of good faith and fair dealing, by contrast, is based on judicially recognized duties not found within the four corners of the contract. See Beck v. Farmers Ins. Exch., 701 P.2d 795, 798 (Utah 1985). These duties, unlike the duties expressly stated in the contract, are not subject to alteration by the parties. They exist whenever a contract is entered, see *id.*, and are imposed on the parties "consistent with the agreed common purpose" of the contract, St. Benedict's Dev. Co. v. St. Benedict's Hosp., 811 P.2d 194, 200 (Utah 1991).

2005 UT 21, at P10. Under Utah law, "the covenant of good faith and fair dealing inheres in all contracts," *id. at 11*, and

Under the covenant of good faith and fair dealing, both parties to a contract impliedly promise not to intentionally [\*\*241] do anything to injure the other party's right to receive the benefits of the contract. St. Benedict's Dev. Co. v. St. Benedict's Hosp., 811 P.2d 194, 199 (Utah 1991). A violation of the covenant is a breach of the contract. *Id.* at 200 (citing Beck v. Farmers Ins. Exch., 701 P.2d 795, 798 (Utah 1985)).

Eggett v. Wasatch Energy Corp., 2004 UT 28, P14, 94 P.3d 193,

HN75[ To determine the legal duty a contractual party has under this covenant, a court will assess whether a "party's actions [are] consistent with the agreed common purpose and the justified expectations of the other party." *Id. at 200*. This court determines the "purpose, intentions, and expectations" by considering "the contract language and the course of dealings between and conduct of the parties." *Id.*

Oakwood Village LLC v. Albertsons, Inc., 2004 UT 101, P43, 104 P.3d 1226, 1239-1240.

HN76[ Under Utah law, "some general principles limit the scope of the covenant," including the following:

First, this covenant cannot be read to establish new, independent rights or duties to which the parties did not agree *ex ante*. Brehany v. Nordstrom, Inc., 812 P.2d 49, 55 (Utah 1991). Second, this covenant cannot create rights and duties inconsistent [\*\*242] with express contractual terms. See id.; Rio Algom Corp. v. Jimco, Ltd., 618 P.2d 497, 505 (Utah 1980). Third, this covenant cannot compel a contractual party to exercise a contractual right "to its own detriment for the purpose of benefitting another party to the contract." Olympus Hills Shopping Ctr. v. Smith's Food & Drug Ctrs., 889 P.2d 445, 457 n. 13 (Utah Ct. App. 1994). Finally, we will not use this covenant to achieve an outcome in harmony with the court's sense of justice but inconsistent with the express terms of the applicable contract. See Dalton v. Jerico Constr. Co., 642 P.2d 748, 750 (Utah 1982).

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*Oakwood Village LLC, 2004 UT 101, P45, 104 P.3d at 1240*; see *Brehany v. Nordstrom, Inc., 812 P.2d 49, 55 (Utah 1991)* (the implied covenant of good faith and fair dealing "cannot be construed . . . to establish new, independent rights or duties not agreed upon by the parties."). **HN77** Generally, "the degree to which a party to a contract may invoke the protections of the covenant turns on the extent to which the contracting parties have defined their expectations and imposed **[\*1189]** limitations on contract terms." *Smith v. Grand Canyon Expeditions, 2003 UT 57, P20, 84 P.3d 1154, 1160*.<sup>103</sup> **[\*\*243]** In all instances, however, "the reach of the implied covenant of good faith and fair dealing extends no further than the purposes and express terms of the contract." *Id.*, *2003 UT 57, P22, 84 P.3d at 1160*.

The "federal common law" reading of this implied covenant finds reflection in *United States ex rel. Norbeck v. Basin Elec. Power Coop., 248 F.3d 781 (8th Cir.2001)*, in which the Eighth Circuit, applying federal **[\*\*245]** common law, was confronted with the application of the implied covenant of good faith and fair dealing to a contract term involving amortization of certain costs. *Id. at 794-97*. *Basin Electric* reversed a portion of the district court's judgment granted for a breach of the implied covenant of good faith and fair dealing, noting that the covenant "does not imply 'an everflowing cornucopia of wished-for legal duties,'" and "does not impose a general requirement that a party act reasonably[;] rather, the covenant acts as a gap filler to deal with circumstances not contemplated by the parties at the time of contracting." *Id. at 796* (internal citations omitted). The implied covenant would not be applied in a fashion that necessitates rewriting the contract to give one party "benefits for which it did not bargain." *Id. at 797-98*.

Plaintiffs assert the "denial of their entitlement to a contract with the District that is based upon principles of good faith and fair dealing, with adequate consideration," (Proposed Pretrial Order at 4 P(12)); "injuries from the defendants' by way of . . . (12) bad faith void contracts that lack fair dealing," (Proposed Amended Complaint at 11-12 P(12)); and that **[\*\*246]** as to Dr. MacArthur, "every time he was given a contract in bad faith with ambiguities [sic] upon which he relied, he has a claim." (*Id. at 95*; Proposed Pretrial Order at 64.) Yet nowhere in the Proposed Amended Complaint, the Proposed **[\*1190]** Pretrial Order, or plaintiffs' more recent written submissions do they plead specific facts identifying the "bad faith void contracts" in question, or detailing the bad faith or over-reaching involved in making those contracts.<sup>104</sup>

<sup>103</sup> According to Justice Nehring, author of the *Smith v. Grand Canyon Expeditions* opinion:

The implied covenant is by its very nature a pliable doctrine. It is inherently amorphous and evades definitional precision. These traits place the implied covenant directly at odds with predictability of conduct, the most basic and cherished characteristic of the contracts which the implied covenant was created to serve. As one commentator observed, "While the varieties of good faith are not quite as infinite as those of religious faith, it would be quite extraordinary if this protean concept were used in the same sense in all . . . assorted instances." Farnsworth, E. Allan, Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code, 30 U. Chi. L.Rev. 666, 668 (1968).

However, this answer is unsatisfactory to many who share the view made evident in the dissent that the implied covenant can too easily turn away from being an ally of contract law and become its antagonist. **[\*\*244]** This happens when courts mishandle the subtle but important distinction between invoking the implied covenant to compel a contracting party to honor the "agreed common purpose" and "justified expectations" of another party to the contract, *Restatement Second of Contracts* § 205 cmt. a (1979), and injecting it to "establish new, independent rights or duties not agreed upon by the parties" or to "nullify a right granted by a contract to one of the parties." *Brehany v. Nordstrom, 812 P.2d 49, 55 (Utah 1991)*.

The parties can reduce the risk that a court will remake their contract and award one party "benefits for which it did not bargain," . . . by bargaining for terms that limit the exercise of unfettered discretion by one party or that otherwise clearly articulate the purposes and expectations of the parties. In short, the parties to a contract are best served when they fill their own gaps.

*Eggett v. Wasatch Energy Corp., 2004 UT 28, P 43-45, 94 P.3d at 204* (Nehring, J., concurring).

<sup>104</sup> If these allegations were intended to refer to the SJHSD medical staff *bylaws* that govern medical practice at District facilities, the reference is well-hidden. Under Utah law, it is understood that "hospital bylaws constitute 'a contract between the hospital

Instead, it appears that plaintiffs' counsel is attempting to weave the equitable doctrines enumerated in *Allen* into an affirmative legal duty of "fair dealing" affecting "all Utah business relations," independent of the terms of a specific contract--a duty to make all contracts on terms that accommodate the economic expectations of the plaintiffs. Indeed, plaintiffs' counsel asserts an "interference with" Dr. MacArthur's "right to pursue his profession and business affairs by lack of good faith and fair dealing inherent and mandated in all Utah business relations." (Memorandum in Support of Plaintiff [\[\\*\\*248\]](#) MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), at 4.)

**HN78** [T]he Utah Supreme Court has taken the position "that the ability of a plaintiff to recover in tort for breach of the implied covenant of good faith and fair dealing in a contract 'has the potential for distorting well-established principles of contract law and will not be permitted.'" *Berube v. Fashion Centre, Ltd.*, 771 P.2d 1033, 1046 (Utah 1989) (Durham, J.) (quoting *Beck v. Farmers Insurance Exchange*, 701 P.2d 795, 799 (Utah 1985)). Utah law thus does not recognize an independent tort cause of action based upon "good faith and fair dealing" apart from the purposes and terms of an existing contract, and in contrast to equitable doctrines such as unconscionability, the implied covenant cannot serve as a basis for invalidating a contract.

**(16) "privacy rights and statutory entitlements to have their credential files and patient files accurately kept by the district under Medicaid and Utah Health Department statutes and regulations"**

The confidentiality of individual patients' medical information has been [\[\\*\\*249\]](#) a matter of long-standing concern, acknowledged in the Hippocratic Oath (ca. 400 B.C.E.).<sup>105</sup>

[\*1191] Drawing from its rich history, confidentiality remains widely acknowledged as a fundamental ethical tenet of medicine, as patients must be willing to confide sensitive and personal information to health care professionals. Therefore, its value in the context of the patient-physician relationship stems partly from the need for patients to trust their physicians, and for physicians to express their loyalty to patients.

Council on Ethical and Judicial Affairs, American Medical Association, *Privacy in the Context of Health Care* (CEJA Report 2-I-01), at 2 (December 2001), available at <[http://www.ama-assn.org/ama/pub/upload/mm/369/ceja\\_2i01.pdf](http://www.ama-assn.org/ama/pub/upload/mm/369/ceja_2i01.pdf)> Concern for the protection of patient confidentiality and privacy finds current expression in the American Medical Association's Principles of Medical Ethics: "A physician shall respect the rights of patients, colleagues, and other health professionals, and shall safeguard patient confidences and privacy within the constraints of the law." American Medical Association, *Principles of Medical Ethics* PIV (2001), available at <<http://www.ama-assn.org/ama/pub/category/2512.html>>. [\[\\*\\*250\]](#)<sup>106</sup>

and the physician," and that "the Hospital must comply with those bylaws when taking actions which effect its staff." *Houston v. Intermountain Health Care, Inc.*, 933 P.2d 403, 408 (Utah Ct. App. 1997) (quoting *Rees v. Intermountain Health Care, Inc.*, 808 P.2d 1069, 1076 (Utah 1991)).

In contrast to *Rees* and *Houston*, the plaintiffs in this action do not seek to enforce the provisions of the SJHSD bylaws, or even to enforce the implied covenant of good faith and fair [\[\\*\\*247\]](#) dealing as an implied term of the bylaws "contract." They list no claim for breach of contract. Instead, they apparently contend that the SJHSD "medical staff bylaws in and of themselves are "unconstitutional [unconscionable?], violative of covenants of good faith and fair dealing." (Tr. 11/14/02, at 43:5-9 (Ms. Rose).) Yet this view of the medical staff bylaws would necessarily hold them to be unenforceable and of no legal effect-leaving plaintiffs MacArthur and Lyman with no procedural mechanism by which they could have obtained or maintained practice privileges at SJHSD facilities.

<sup>105</sup> The Oath of Hippocrates, 4th Century, B.C.E., reads in part:

What I may see or hear in the course of the treatment or even outside of the treatment in regard to the life of men, which on no account one must spread abroad, I will keep to myself, holding such things shameful to be spoken about.

Ludwig Edelstein, *The Hippocratic Oath: Text, Translation, and Interpretation* (1943).

<sup>106</sup> The terms "confidentiality" and "privacy" address distinct, yet overlapping concerns: "In the context of health care, emphasis has been given to confidentiality, which is defined as information told in confidence or imparted in secret. However, physicians

**[HN79]** In Utah, the maintenance and protection of the confidentiality of medical records involves the application of both legal and ethical standards. The Utah Medical Practice Act Rules (Rule R156-67) currently provide:

**R156-67-602. Medical Records.**

**[HN80]** In accordance with [Subsection 58-67-803\(1\)](#), medical records shall be maintained to be consistent with the following: [\[\\*\\*251\]](#)

- (1) all applicable laws, regulations, and rules; and
- (2) the Code of Medical Ethics of the Council on Ethical and Judicial Affairs as published in the AMA Policy Compendium, 2001 edition, which is hereby incorporated by reference.

Utah Admin. Code § R156-67-602 (2005); see [Utah Code Ann. § 58-67-803\(1\)](#) (2002) **[HN81]** ("Medical records maintained by a licensee shall: (a) meet the standards and ethics of the profession; and (b) be maintained in accordance with division rules made in collaboration with the board.").

The advent of electronic storage and computer access to patient medical records and health information has increased patient privacy and confidentiality concerns, as one recent commentary explains:

[As] access to medical information of a sensitive nature has grown, those in the medical community and privacy advocates began to recognize the need for broad privacy protections to medical data. The result of this campaign is the Standards for Privacy of Individually Identifiable Health Information (the "Privacy Rule"), a set of regulations promulgated by the Secretary of Health and Human Services ("HHS"). The Privacy Rule was required by the Health Insurance Portability & Accountability [\[\\*\\*252\]](#) Act of 1996 ("HIPAA"), then popularly known as the Kennedy-Kassenbaum Act. At the time, HIPAA received significant attention, because it made it easier for an employee to maintain health insurance after leaving a job. HIPAA also provided that if Congress did not pass legislation pertaining to medical [\[\\*1192\]](#) privacy within a specified time, HHS would promulgate regulations to that affect. HHS issued a proposed rule in October 1999, and after an unusually long and contentious comment period and a clerical error that nearly derailed the regulations at the last second, the Privacy Rule was implemented in early 2001.

Kevin B. Davis, *Privacy Rights in Personal Information: HIPAA and the Privacy Gap Between Fundamental Privacy Rights and Medical Information*, [19 J. Marshall J. Computer & Info. L. 535, 536 \(2001\)](#) (footnotes omitted).

In enacting the Health Insurance Portability and Accountability Act of 1996 (HIPAA), *Pub. L. No. 104-191, 110 Stat. 1936* (1996), Congress mandated the establishment of national standards for protection of the privacy of individually identifiable health and medical information. As indicated, the U.S. Department of Health and Human Services promulgated such standards in [\[\\*\\*253\]](#) 2001, and most health plans and health care providers that are covered by the new rule were required to comply with the new standards by April of 2003. See [Standards for Privacy of Individually Identifiable Health Information, 65 Fed. Reg. 82462 \(Dec. 28, 2000\)](#), codified at 45 C.F.R. Parts 160-164 (2004).<sup>107</sup>

Prior to the enactment of HIPAA, Utah law already afforded some degree of legal protection for the privacy and confidentiality of patient medical records. See, e.g., [Hoopiiaina v. Intermountain Health Care, 740 P.2d 270, 272 \(Utah Ct. App. 1987\)](#) ("Confidentiality of patient information is required by Utah Code Ann. § 78-25-25 (1987) and Chapter 7.404 of the Utah State Department of Health, Hospital and Psychiatric Hospital Rules and Regulations,

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also should be mindful of patient privacy, which encompasses information that is concealed from others outside of the patient-physician relationship." *Privacy in the Context of Health Care, supra*, at 3.

<sup>107</sup> In mid-2001, HHS released an FAQ-style "Guidance" commentary explaining the new "Privacy Rule" standards and requirements. HHS Office for Civil Rights, *Standards for Privacy of Individually Identifiable Health Information* (2001), at <http://www.hhs.gov/ocr/hipaa/finalmaster.html> (July 6, 2001; last revised January 14, 2002).

Medical Records Department (1984 Revision).").<sup>108</sup> Utah law may afford some common-law privacy protection for [\*\*254] medical records as well.<sup>109</sup>

[\*1193] At this point, however, this court need not reconstruct the pre-HIPAA Utah law of confidentiality of patient medical records; plaintiffs assert the breach of such confidentiality, but plead no specific facts by which such a breach could be established. Plaintiffs asserted at the time of the Pretrial Conference that "Mrs. Lyman had patient files disappear, and patients['] confidentiality breached," (Proposed Pretrial Order at 13), that "patients of Michele Lyman were subjected to ... (3) breach of confidentiality of any medical treatment they did receive in the District facilities," (*id.* at 30 P139), that [\*\*256] "confidentiality of her patients was broken on more than one occasion by medical staff and other SJHSD personnel," (*id.* at 51 P195), but with no specific factual allegations as to particular instances in which such a breach of confidentiality has occurred, or in which it is alleged there was a public disclosure of a patient's embarrassing private medical information.<sup>110</sup> Moreover, absent such specific factual allegations, the court need not decide the threshold question whether the remaining Part I Plaintiffs have the requisite standing to assert claims for a breach of confidentiality or invasion of privacy affecting third persons, *viz.*, their patients. Cf. *Singleton v. Wulff*, 428 U.S. 106, 49 L. Ed. 2d 826, 96 S. Ct. 2868 (1976) (plurality opinion); *Eisenstadt v. Baird*, 405 U.S. 438, 31 L. Ed. 2d 349, 92 S. Ct. 1029 (1972); *Tileston v. Ullman*, 318 U.S. 44, 87 L. Ed. 603, 63 S. Ct. 493 (1943); Henry P. Monaghan, *Third Party Standing*, 84 Colum. L. Rev. 277 (1984).<sup>111</sup>

## (17) Negligent and Intentional Infliction of Emotional Distress

### (a) Intentional Infliction of Emotional Distress

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<sup>108</sup> Originally adopted in 1971 (1971 Utah Laws ch. 213, § 1), Utah Code Ann. § 78-25-25 (2002) addressed attorney access to patient medical records, and was repealed and re-enacted in 2003 in light of HIPAA and the HHS Privacy Rule. See Utah Code Ann. § 78-25-25 (Supp. 2004); [2003 Utah Laws ch. 64, § 2](#).

<sup>109</sup> Under Utah law, to prevail on a claim of public disclosure of embarrassing private facts, a plaintiff must establish the following essential elements:

- (1) the disclosure of the private facts must be a public disclosure and not a private one;
- (2) the facts disclosed to the public must be private facts, and not public ones; [and]
- (3) the matter made public must be one that would be highly offensive and objectionable to a reasonable person of ordinary sensibilities.

*Shattuck-Owen v. Snowbird Corp.*, 2000 UT 94, P 11, 16 P.3d 555, 558 (quoting *Stien v. Marriott Ownership Resorts, Inc.*, 944 P.2d 374, 380 (Utah Ct. App. 1997) (quoting W. Page Keeton et al., *Prosser and Keeton on the Law of Torts* § 117, at 856-857 (5th ed. 1984) (footnote omitted))). See also *Restatement (Second) of Torts* § 652D (1977) ("One who gives publicity to a matter concerning the private [\*\*255] life of another is subject to liability to the other for invasion of his privacy, if the matter publicized is of a kind that (a) would be highly offensive to a reasonable person, and (b) is not of legitimate concern to the public.") *Shattuck-Owen* notes that the *Restatement (Second) of Torts* § 652D (1977) "contains another element requiring that the matter made public not be 'of legitimate concern to the public,'" but did not "decide whether to adopt this requirement as an element of the invasion of privacy tort we address today." [2000 UT 94, P 11, 16 P.3d 555](#) n.1, [16 P.3d at 558](#) n.1.

<sup>110</sup> The Proposed Amended Complaint asserts that "some of Mrs. Lyman's patients[] were subjected to community gossip for conditions that were supposed to be private," (Proposed Amended Complaint at 17-18), at least implying [\*\*257] some breach of confidentiality. That assertion is omitted from the recitation of contested issues of fact in the Proposed Pretrial Order, replaced by the equally conclusory assertions that "Patients of Michele Lyman were subjected to ... (3) breach of confidentiality of any medical treatment they did receive in the District facilities, . . . (6) false rumors as to their medical conditions," still without any reference to particular instances. (Proposed Pretrial Order at 30 P139.)

<sup>111</sup> Ordinarily, a litigant "must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties." *Valley Forge Christian College v. Americans United for Separation of Church & State, Inc.*, 454 U.S. 464, 474, 70 L. Ed. 2d 700, 102 S. Ct. 752 (1982) (quoting *Warth v. Seldin*, 422 U.S. 490, 499, 45 L. Ed. 2d 343, 95 S. Ct. 2197 (1975)).

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In *DeBry v. Godbe*, 1999 UT 111, 992 P.2d 979, the Utah Supreme Court reiterated the essential elements of a claim of intentional infliction of emotional distress:

In *Samms v. Eccles*, we stated the elements [\*\*258] of such a claim:

**HN82**[] An action for severe emotional distress, though not accompanied by bodily impact or physical injury, [may lie] where the defendant intentionally engaged in some conduct toward the plaintiff, (a) with the purpose of inflicting emotional distress, or, (b) where any reasonable person would have known that such would result; and his actions are of such a nature as to be considered outrageous and intolerable in that they offend against the generally accepted standards of decency and morality.

11 Utah 2d 289, 293, 358 P.2d 344, 346-47 (1961).

1999 UT 111, P 25, [\*1194] 992 P.2d at 986.<sup>112</sup> **HN83**[] "To prevail on her claim of intentional infliction of emotional distress," a plaintiff "must prove that the defendants either intentionally or recklessly engaged in intolerable and outrageous conduct that caused her severe emotional distress." *Rutherford v. AT & T Communications*, 844 P.2d 949, 967 (Utah 1992).<sup>113</sup>

### (b) Negligent Infliction of Emotional Distress

**HN85**[] The Utah Supreme Court first expressly recognized a cause of action for negligent infliction of emotional distress in *Johnson v. Rogers*, 763 P.2d 771 (Utah 1988).

In *Johnson*, after surveying the various tests that courts in this country have developed to determine liability for the negligent infliction of emotional distress, we adopted the position taken by *section 313 of the Restatement (Second) of Torts* (1965), as explained in the comments accompanying that section. *Section 313*'s approach, also referred to as the zone of danger approach, allows recovery to plaintiffs who suffer emotional distress because of another's negligence, though they do not suffer any physical impact, only if the plaintiffs are placed in actual physical peril and fear for their own safety. *Johnson*, therefore, does not provide recovery to plaintiffs who are not within the zone of danger created by a defendant's negligence.

Boucher By and Through Boucher v. Dixie Medical Center, 850 P.2d 1179, 1181 (Utah., 1992). [\*\*260]<sup>114</sup> The comments to *Restatement § 313* "restrict the scope of a claim for negligent infliction of emotional distress":

<sup>112</sup> *Godbe* affirmed the district court's conclusion that the plaintiff's "intentional infliction of emotional distress claim could not survive summary judgment because Godbe's conduct was not outrageous and intolerable under *Samms*." *Id.*

<sup>113</sup> **HN84**[] Intentional infliction of emotional distress, [\*\*259] in contrast to negligent infliction of emotional distress, does not require that plaintiff actually be at risk of bodily harm. See *Restatement (Second) of Torts § 312*.

<sup>114</sup> *Section 313 of the Restatement (Second) of Torts* reads:

**HN87**[] (1) If the actor unintentionally causes emotional distress to another, he is subject to liability to the other for resulting illness or bodily harm if the actor

(a) should have realized that his conduct involved an unreasonable risk of causing the distress, otherwise than by knowledge of the harm [\*\*262] or peril of a third person, and

(b) from facts known to him should have realized that the distress, if it were caused, might result in illness or bodily harm.

(2) The rule stated in Subsection (1) has no application to illness or bodily harm of another which is caused by emotional distress arising solely from harm or peril to a third person, unless the negligence of the actor has otherwise created an unreasonable risk of bodily harm to the other.

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Comment "a" declares that the "rule stated in this Section does not give protection to mental and emotional tranquillity in itself." [Restatement \(Second\) of Torts § 313 cmt. a \(1965\)](#). Comment "c" articulates a form of "reasonable person" test by noting that in contrast to the [section 312](#) rule for intentional creation of emotional distress, "one who unintentionally but negligently subjects another to such emotional distress does not take the risk of any exceptional physical sensitiveness to emotion which the other may have unless the circumstances known to the actor should apprise him of it." [Restatement \(Second\) of Torts § 313 cmt. c \(1965\)](#). These comments recognize the fact that "we cannot permit every claim for negligent infliction of emotional distress to go to a jury under such varying standards as [\*1195] each trial judge may choose." [Johnson, 763 P.2d at 785](#) (Zimmerman, J., concurring in part).

[Harnicher v. University of Utah Medical Center, 962 P.2d 67, 70 \(Utah 1998\)](#). [HN86](#)[ One restriction that "provides a check on feigned disturbances, thereby ensuring the genuineness" [\\*\\*261](#) of claims<sup>115</sup> is the requirement that plaintiffs who claim to be the direct victim of negligent infliction of emotional distress must allege resulting illness or bodily harm, including clinically identifiable mental illness. See [id. at 71-72](#) (affirming summary judgment against plaintiffs who "had not suffered any bodily harm or physical injury that would support an action for negligent infliction of emotional distress"); [Hansen v. Mountain Fuel Supply Co., 858 P.2d 970, 974 \(Utah 1993\)](#) ("emotional disturbance that is not severe enough to result in illness or physical consequences is likely to be in the realm of the trivial. Such a disturbance is likely to be so temporary and subjective that to attempt to compensate it would unduly burden defendants and the courts. See [Restatement \(Second\) of Torts § 436A cmt. b \(1965\)](#); ....").

<sup>116</sup>

Given that [Restatement \(Second\) of Torts § 313\(1\)](#) does not give protection to mental and emotional tranquility per se, "consequently, much of the "emotional distress" which we endure ... is not compensable." [Thing v. La Chusa, 48 Cal.3d 644, 257 Cal.Rptr. 865, 771 P.2d 814, 829 \(1989\)](#) (denying recovery for negligent infliction of emotional distress where mother of injured child arrived at the scene after accident had already occurred)." [Harnicher, 962 P.2d at 72.](#) [HN88](#)[ To sustain a claim of negligent infliction of emotional distress, "the emotional distress suffered must be severe; it must be such that 'a reasonable [person,] normally constituted, would be unable to adequately cope with the mental stress engendered by the circumstances of the case.'" [Mountain Fuel, 858 P.2d at 975](#) (quoting [Rodrigues v. State, 52 Haw. 156, 472 P.2d 509, 520 \(1970\)](#)).

### (c) The Part I Plaintiffs' Emotional Distress Claims

Intentional and negligent infliction of emotional distress "are claims for ... different torts, each with separate elements," and "obviously, [a] plaintiff must make the necessary allegations in his complaint [\\*\\*264](#) to support each separate claim, and at trial plaintiff must prove all of the elements of each claim to recover for that cause of action," each by a preponderance of the evidence. [Heiner v. Simpson, 2001 UT 39, PP 8, 9, 23 P.3d 1041, 1043](#) (footnote omitted); *id.* [2001 UT 39 17 n. 3, 23 P.3d at 1043 n.3.](#)

[Restatement \(Second\) of Torts § 313 \(1965\)](#); see also [Hansen v. Sea Ray Boats, 830 P.2d 236, 240-241 \(Utah 1992\)](#) (discussing [§313](#)).

<sup>115</sup> [Hansen v. Mountain Fuel Supply Co., 858 P.2d 970, 974 \(Utah 1993\)](#).

<sup>116</sup> As [Mountain Fuel](#) explains:

The language used in [section 313 of the Restatement](#) provides some guidance. Subsection (1) allows recovery for "illness or bodily harm." [Restatement \(Second\) of Torts § 313\(1\) \(1965\)](#) (emphasis added). The drafters' use of "or" rather than "and" shows an intention to allow a plaintiff to recover not only where bodily harm results from emotional trauma, but where "illness" results as well. "Illness" is "an unhealthy condition of body or mind." [Webster's New Collegiate Dictionary](#) 566 (1981). From this we conclude that [\\*\\*263](#) either physical or mental illness may support the ... cause of action.

Court and counsel reviewed the factual allegations underlying Ms. Lyman's claim of intentional infliction of emotional distress in light of this analytical framework at the Final Pretrial Conference. (See *infra* at 174-176.)

### (18) Fraud

Under Utah law,

The elements that a party must allege "to bring a claim sounding in fraud" are [\*1196] (1) that a representation was made (2) concerning a presently existing material fact (3) which was false and (4) which the representor either (a) knew to be false or (b) made recklessly, knowing that there was insufficient knowledge upon which to base such a representation, (5) for the purpose of inducing the other party to act upon it and (6) that the other party, acting reasonably and in ignorance of its falsity, (7) did in fact rely upon it (8) and was thereby induced to act (9) to that party's injury and damage. *Gold Standard, Inc. v. Getty Oil Co.*, 915 P.2d 1060, 1066-67 (Utah 1996) [\*\*265] (citations omitted); *Educators Mut. Ins. Ass'n. v. Allied Prop. & Cas. Ins. Co.*, 890 P.2d 1029, 1032 (Utah 1995); accord *Crookston v. Fire Ins. Exch.*, 817 P.2d 789, 800 (Utah 1991).

[Armed Forces Ins. Exchange v. Harrison, 2003 UT 14, P 16, 70 P.3d 35, 40.](#)

*Rule 9(b) of the Federal Rules of Civil Procedure* requires that "in all averments of fraud ..., the circumstances constituting fraud ... shall be stated with particularity." "Simply stated, a complaint must 'set forth the time, place and contents of the false representation, the identity of the party making the false statements and the consequences thereof.'" *Schwartz v. Celestial Seasonings, Inc.*, 124 F.3d 1246, 1252 (10th Cir. 1997) (quoting *Lawrence Nat'l Bank v. Edmonds (In re Edmonds)*, 924 F.2d 176, 180 (10th Cir. 1991)). At a minimum, *Rule 9(b)* requires that a plaintiff set forth the "who, what, when, where and how" of the alleged fraud. *Williams v. WMX Techs.*, 112 F.3d 175, 179 (5th Cir. 1997)); see also *Harrison v. Westinghouse Savannah River Co.*, 176 F.3d 776, 784 (4th Cir. 1999) ("The 'circumstances' required to be pled with particularity under *Rule 9(b)* are 'the time, place, and contents of the false representations, as well [\*\*266] as the identity of the person making the misrepresentations and what he obtained thereby.'") (quoting 5 Charles Alan Wright & Arthur R. Miller, *Federal Practice and Procedure* § 1297, at 590 (2d ed. 1990)).

Thus, while a federal court will examine state law to determine whether the elements of fraud have been pled sufficiently to state a cause of action, the *Rule 9(b)* requirement that the circumstances of the fraud must be stated with particularity is a federally imposed rule. One of the main purposes of the rule is to apprise the defendant of fraudulent claims and of the acts that form the basis for the claim.... In other words, "in cases in which *fraud lies at the core of the action*, the rule does not permit a complainant to file suit first, and subsequently to search for a cause of action."

[Hayduk v. Lanna, 775 F.2d 441, 443 \(1st Cir. 1985\)](#) (quoting *Lopez v. Bulova Watch Co., Inc.*, 582 F.Supp. 755, 766 (D.R.I.1984) (emphasis added)).<sup>117</sup> See also Annotation, *Construction and application of provision of Rule 9(b), Federal Rules of Civil Procedure*, that circumstances constituting fraud or mistake be stated with particularity, 27 A.L.R. Fed. 407 (1976 & Supp. 2004).

[\*1197] As discussed above, plaintiff Lyman alleges that her CPR certification cards, "a necessary component of her ability to obtain privileges were altered purposefully," that "the cards were stolen from her file at least on two if not three occasions," that "the forged documents were mailed to the American Heart Association," and that "the

<sup>117</sup> Once past the [\*\*267] pleading stage, a party must then prove the elements of fraud by clear and convincing evidence:

"A finding of fraud must be based on the existence of all its essential elements .... 'Fraud is a wrong of such nature that it must be shown by clear and convincing proof and will not lie in mere suspicion or innuendo.'" *Taylor v. Gasor, Inc.*, 607 P.2d 293, 294-95 (Utah 1980) (internal citations omitted) (quoting *Lundstrom v. Radio Corp. of Am.*, 17 Utah 2d 114, 117-18, 405 P.2d 339, 341 (1965)).

[Armed Forces Ins. Exchange v. Harrison, 2003 PP 14, K27, 70 P.3d at 43.](#)

doctors would have profited from Mrs. Lyman. not being able to work ...." (Proposed Pretrial Order at 63 P255; see also *id.* at 14, 29 PP129-131, 34 PP174-175.) No less than five essential elements of fraud are omitted from her allegations, *viz.*, that the altered cards were sent to the American Heart [\*\*268] Association "[1] for the purpose of inducing the other party to act upon it and [2] that the other party, acting reasonably and in ignorance of its falsity, [3] did in fact rely upon it [4] and was thereby induced to act [5] to that party's injury and damage." *Secor v. Knight, 716 P.2d 790, 794 (Utah 1986)* (quoting *Dugan v. Jones, 615 P.2d 1239, 1246 (Utah 1980)*).

**HN89** [↑] "In order to prevail on a claim of fraud [or misrepresentation], *all the elements of fraud* must be established by clear and convincing evidence. " *Id.* (emphasis added). Under *Rule 9(b)* those missing elements of reasonable reliance, causation and injury are among the "circumstances constituting fraud" that must be pleaded with particularity. Absent such pleading, plaintiffs' fraud claim remains vulnerable to dismissal pursuant to *Fed. R. Civ. P. 9(b)*, independent of a motion under *Rules 12(b)(6)* or *56*.

Would plaintiffs' state law fraud claim fare better in a Utah state court? **HN90** [↑] In applying Utah's parallel civil rule, the Utah Supreme Court has held that "the mere recitation by a plaintiff of the elements of fraud in a complaint does not satisfy the particularity requirement." *Armed Forces Ins. Exch. v. Harrison, 2003 UT 14, P 16, 70 P.3d at 40.* [\*\*269] Rather, Utah *Rule 9(b)* requires a complaint to recite "the relevant surrounding facts" "with sufficient particularity to show what facts are claimed to constitute [the fraud] charges. " " *Id.* (quoting *Williams v. State Farm Ins. Co., 656 P.2d 966, 971 (Utah 1982)* (quoting *Heathman v. Hatch, 13 Utah 2d 266, 372 P.2d 990, 991 (1962)*)). Moreover, as the Utah Court of Appeals recently observed in *Coroles v. Sabey, 2003 UT App 339, 79 P.3d 974, rule 9(b)* also imposes a much more basic and fundamental requirement: a requirement of clarity and conciseness":

In *Heathman v. Hatch, 13 Utah 2d 266, 372 P.2d 990 (1962)*, the Utah Supreme Court affirmed the dismissal of the plaintiffs complaint because the complaint, which was "33 legal size typewritten pages" in length, did not comply with *rule 9(b)*. *372 P.2d at 991-92*. The Court stated the following regarding the complaint's noncompliance with that rule:

Without burdening this opinion with the details of plaintiff's much too long and involved complaint, it is sufficient to say that its shortcomings are such that it was well within the discretion of the trial court to conclude that it failed to comply with [*rules 8(a)* and *9(b)*], and, accordingly, [\*\*270] to grant the motion to dismiss. The objective of these rules is to require that the essential facts upon which redress is sought be set forth with simplicity, brevity, clarity and certainty so that it can be determined whether there exists a legal basis for the relief claimed; and, if so, so that there will be a clearly defined foundation upon which further proceedings by way of responsive pleadings and/or trial can go forward in an orderly manner.

*Id. at 992.*

*2003 UT App 339, P 23, [\*1198] 79 P.3d at 980* (footnote omitted). As *Coroles* explains, **HN91** [↑] pleading a fraud claim without specifying the facts upon which it is based "essentially dumps upon the trial court ... the burden of sifting through the hundreds of paragraphs of alleged facts to ascertain whether Plaintiffs have 'alleged ... facts necessary to make all their elements of fraud.' *DeBry v. Noble, 889 P.2d 428, 443 (Utah 1995)*."

Such an approach is unacceptable. It is Plaintiffs' responsibility, not the courts', to set forth "the relevant surrounding facts" in such a manner that it is evident ""what facts are claimed to constitute [the fraud] charges. " "*Armed Forces, 2003 UT 14 at P 16, 70 P.3d 35* (citations omitted) (emphasis added). See *Arena Land & Inv. Co. v. Petty, No. 94-4196, 1995 WL 645678, at \*1, 1995 U.S.App. LEXIS 31140, at \*3 (10th Cir. Nov. 3, 1995)* [\*\*271] ("The third amended complaint is wordy, repetitive and fails to allege the necessary elements of the claims it is asserting. Indicative of the complaint's inadequacy is the fact that it rambles on for sixty-four pages before reaching the first claim for relief. It is neither the court's nor the appellees' role to sift through a lengthy, conclusory and poorly written complaint to piece together the cause of action.").

*Id. at P 27, 79 P.3d at 980-81* (footnote omitted).

Here, this court is-as was the Utah Court of Appeals in *Coroles*--"unable to ascertain ""what facts are claimed to constitute [the fraud] charges."'" [79 P.3d 974, 2003 UT App 339, P 27 n.12](#) (quoting [Armed Forces Insurance Exchange v. Harrison, 2003 UT 14, P 16, 70 P.3d 35](#) (citations omitted)).

### **Summary re: the Part I Plaintiffs' Causes of Action**

Whether the Part I Plaintiffs' claims had any arguable legal merit or raised genuine issues for trial--a question of further formulation of the issues for trial under [Fed. R. Civ. P. 16\(c\)\(1\)](#) was addressed in some detail at the Final Pretrial Conference. Accepting the Proposed Amended Complaint as the best articulation of the Part I Plaintiffs' claims as of the time of pretrial, [\[\\*\\*272\]](#)<sup>118</sup> it becomes apparent that many of plaintiffs' theories of liability had already failed as a matter of law--one because the statute in question simply does not afford plaintiffs a private civil remedy, the others because they are legally meritless: either the essential elements of the cause of action have no bearing upon the specific facts alleged by these plaintiffs (even if those facts are taken as true and all reasonable inferences are drawn in their favor), or because the plaintiffs have pleaded the claims in conclusory terms, without alleging any specific facts that would provide a viable factual footing for these claims, that is, without a plain statement of the claim showing that they are entitled to relief. See [Fed.R.Civ.P. 8\(a\)\(2\)](#).<sup>119</sup> These legally meritless claims include those pleaded as arising under (i) RICO, [18 U.S.C. § 1961 et seq.](#); (ii) the Freedom of Access to Clinic Entrances Act of 1994, [18 U.S.C. § 248](#); (iii) the Health Care Quality Improvement Act, [42 U.S.C. § 11112](#); (iv) the Emergency Medical Treatment and Active Labor Act (EMTALA), [42 U.S.C. § 1395dd](#); [\[\\*1199\]](#) (v) the "Medicare Patient Bill of Rights," or freedom-of-choice provision, [42 U.S.C. § 1395a](#); (vi) [42 U.S.C. § 1981](#); [\[\\*\\*273\]](#) (vii) [42 U.S.C. § 1985\(3\)](#); (viii) [42 U.S.C. § 1983](#); (ix) the federal antitrust laws; (x) the Utah Constitution, Art. I, [§§ 1, 7, 25, 26, 27](#); (xi) the Utah Unfair Practices Act, [Utah Code Ann. § 13-5-1 et seq.](#), (xii) the Utah Civil Rights Act, [Utah Code Ann. § 13-7-1 et seq.](#); (xiii) "Federal common law and Utah contract common law and statutory provisions that prohibit contracts of adhesion, bad faith, and lack of fair dealing," including the implied covenant of good faith and fair dealing; (xiv) "privacy rights and statutory entitlements to have their credential files and patient files accurately kept by the district under Medicaid and Utah Health Department statutes and regulations"; (xv) negligent infliction of emotional distress; and (xvi) fraud. Those claims may properly be dismissed as frivolous pursuant to [Fed. R. Civ. P. 16\(c\)\(1\)](#) because they are based upon an indisputably meritless legal theory, or are rooted upon conclusory assertions rather than specific facts, as reflected in the Proposed Amended Complaint and the Proposed Pretrial Order.<sup>120</sup> Cf. [Neitzke v. Williams, 490 U.S. 319, 327, 104 L. Ed. 2d 338, 109 S. Ct. 1827 \(1989\)](#) (claim "based on an indisputably meritless legal [\[\\*\\*274\]](#) theory" or founded on "clearly baseless" factual contentions may be dismissed as "frivolous" under [28 U.S.C. § 1915](#)); [Green v. Seymour, 59 F.3d 1073, 1077 \(10th Cir. 1995\)](#) (complaint is "frivolous" under [28 U.S.C. § 1915](#) "where it lacks an arguable basis either in

<sup>118</sup> As noted above, almost all of its allegations were repeated verbatim as the "Plaintiffs' Statement of Contested Issues of Fact" in Section 5 of the Proposed Pretrial Order.

<sup>119</sup> Further, absent leave to amend her pleadings in some fashion, plaintiff Valdez' EMTALA claim--pledged as a cause of action for the first time in the Proposed Amended Complaint and mirrored in the Proposed Pretrial Order--was clearly time-barred. See [42 U.S.C. § 1395dd\(d\)\(2\)\(C\)](#). Plaintiff Lyman's defamation claim may be time-barred as to any actionable conduct known of or reasonably discoverable prior to July 25, 1999.

<sup>120</sup> Neither [Fed. R. Civ. P. 16\(c\)\(1\)](#) nor the accompanying advisory committee notes articulate the legal standard to be applied in determining whether a claim or defense is "frivolous" within the meaning of the rule. The advisory committee note to the 1983 amendment to [Rule 16](#) makes general reference to a case from the D.C. Circuit, [Meadow Gold Products Co. v. Wright, 108 U.S.App.D.C. 33, 278 F.2d 867 \(D.C. Cir. 1960\)](#). That case states that [\[\\*\\*277\]](#) "the primary purpose of the pre-trial procedure is to 'define the claims and defenses of the parties for the purpose of eliminating unnecessary proof and issues, lessening the opportunities for surprise and thereby expediting the trial,'" but does not speak of "frivolous" claims. [278 F.2d at 869](#) (quoting [Rosden v. Leuthold, 107 U.S.App.D.C. 89, 92, 274 F.2d 747, 750 \(D.C. Cir. 1960\)](#)).

Some guidance may be gleaned from case law construing analogous rule and statutory language, e.g., [28 U.S.C. § 1915\(e\) \(2000\)](#). Cf. [Fed. R. Civ. P. 11\(b\)\(2\)](#) (claims and defenses "warranted by existing law or by a nonfrivolous argument for the extension, modification, or reversal of existing law or the establishment of new law").

fact or law."); *Olson v. Stotts*, 9 F.3d 1475, 1476 (10th Cir. 1993) (claim is "frivolous" under [28 U.S.C. § 1915](#) "if the factual contentions supporting the claim are 'clearly baseless,' . . . or the claim is based on a legal theory that is 'indisputably meritless,'"); *Mitchell v. Horn*, 318 F.3d 523, 530 (3d Cir. 2003) (to be "frivolous" under [28 U.S.C. § 1915](#), "a claim must rely on 'an indisputably meritless legal theory' or a 'clearly baseless' . . . factual scenario"); *Taylor v. Johnson*, 257 F.3d 470, 472 (5th Cir. 2001) (complaint is "frivolous" if it "lacks an arguable basis in law or fact, and a complaint lacks such a basis if it relies on an indisputably meritless legal theory."); *Walker v. City of Bogalusa*, 168 F.3d 237 (5th Cir. 1999) (claim is "frivolous" under [42 U.S.C. § 1988](#) if "it is 'so lacking in arguable merit as to be groundless or without foundation'" (quoting *Plemer v. Parsons-Gilbane*, 713 F.2d 1127, 1140 (5th Cir. 1983)) [\*\*275] (construing [42 U.S.C. §2000e-5\(k\)](#)) (quoting *Jones v. Texas Tech University*, 656 F.2d 1137, 1145 (5th Cir. 1981)); *Karam v. City of Burbank*, 352 F.3d 1188, 1195 (9th Cir. 2003) (complaint may be deemed "frivolous" under [42 U.S.C. § 1988](#) "only when the result is obvious or the ... arguments of error are wholly without merit" (quoting [\*1200] *McConnell v. Critchlow*, 661 F.2d 116, 118 (9th Cir. 1981))); *Davis v. Target Stores Div. of Dayton Hudson Corp.*, 87 F. Supp. 2d 492, 494 (D. Md. 2000) (claim is "frivolous" under Title VII ([42 U.S.C. § 2000e-5\(k\)](#)) "if a plaintiff presents no evidence to support his claim or if he has gone forward on the basis of no colorable legal theory"); see also Annotation, *Standards for determining whether proceedings in forma pauperis are frivolous and thus subject to dismissal under 28 U.S.C.A. sec. 1915(d)*, 52 A.L.R. Fed. 679 (1981 & Supp. 2004); Annotation, *Right of defendant in civil rights case to receive award of attorney's fees under Civil Rights Attorney's Fees Awards Act of 1976 (42 U.S.C.A. sec. 1988)*, 104 A.L.R. Fed. 14 (1991 & Supp. 2004); *Black's Law Dictionary* 601 (5th ed. 1979) ("A pleading is 'frivolous' when it is clearly insufficient in its face, [\*\*276] and does not controvert the material points of the opposite pleading, and is presumably interposed for mere purposes of delay or to embarrass the opponent.").

### **Pretrial Determination of the Part I Plaintiffs' Claims**

For the reasons explained in some detail above, the Final Pretrial Conference concluded with a bench ruling dismissing the Part I Plaintiffs' remaining federal claims on the grounds that they did not have an arguable basis in law and lacked sufficient support in plaintiffs' factual allegations to raise a triable issue, even where those allegations are taken as true and viewed in the light most favorable to the plaintiffs. (See [\*\*278] Tr. 11/15/02, at 113:9-118:7 (the court); [Fed. R. Civ. P. 16\(c\)\(1\)](#).)

Plaintiffs' counsel subsequently objected to the dismissal of the Part I Plaintiffs' claims at the Final Pretrial Conference on the grounds that (1) no summary judgment motion was pending at the time of the Final Pretrial Conference, and plaintiffs did not receive ten days' notice that summary judgment would be considered; (2) no notice was given to the plaintiffs that the pretrial hearing was in actuality a hearing of dismissal of all of their claims; (3) several issues of material fact were raised in the pretrial conference; and (4) dismissal with prejudice, without leave to amend, operates as a "severe sanction" that should only be imposed in extraordinary cases. According to plaintiffs' counsel, there are "two types of dismissal" under the Federal Rules: [Rule 12\(b\)](#) dismissal and [Rule 56](#) summary judgment--or three, viz., as a discovery sanction ([Rule 37\(b\)\(2\)\(C\)](#))--a view that fails to take into account [Rule 16\(c\)\(1\)](#) and the function of the final pretrial conference. (See *supra* at 4-7 ("The Final Pretrial Conference ([Fed. R. Civ. P. 16\(c\)](#)").))

The court's expectations concerning the proposed pretrial order and the [\*\*279] final pretrial conference were spelled out for counsel in explicit terms at the hearing on August 22, 2002:

THE COURT: A pretrial order is a joint product. *I'm interested in isolating the genuinely disputed factual issues. I'm interested in isolating the genuinely disputed legal issues if any.* I want a roster of all your witnesses on all sides. I want a roster of all your exhibits for your cases in chief.

MS. ROSE: Roster of exhibits and witnesses.

THE COURT: I'm interested in having the attorneys sign off on the suggested form of pretrial order so that I know that you've agreed to it even if you agree to disagree as to the identified issues, and I'm interested as I said in giving you a little more time here.

\*\*\*\*

We're interested in *identifying the issues, identifying both legal propositions* [\*1201] *and factual propositions, the witnesses, the exhibits.*

And then at pretrial *I'm interested in counsel being prepared to talk theory, that is legal theory, legal authority, statutory authority or case authority and be able to talk facts*, this is what this witness is going to tell us Judge. That way we can try to screen what's here and see what's genuinely disputed and what genuinely deserves a [\*280] fact finder trial.

(Transcript of Hearing, dated August 22, 2002, at 31:23-32:9, 32:25-33:9 (the court) (emphasis added).) And this was not the only occasion in which the court expressed its expectations concerning pretrial to counsel in open court, and on the record. (See Minute Entry, dated July 2, 2002 (dkt. no. 386); Minute Entry, dated October 8, 2002 (dkt. no. 427).) These expressed expectations comport with both the purpose and function of [Rule 16\(c\)](#) and the requirements of the court's Local Rules, particularly [DUCivR 16-1\(d\)](#): [HN92](#)↑ "Preparation for this final pretrial conference should proceed pursuant to [Fed. R. Civ. P. 16](#) and should include (i) preparation by plaintiffs counsel of a recommended pretrial order..., and (ii) preparation for resolution of unresolved issues in the case." (Emphasis added.)

As explained in some detail herein, this court addressed these plaintiffs' claims in the context of the Final Pretrial Conference, and did so pursuant to [Rule 16\(c\)\(1\)](#), applying [Rule 16\(c\)\(1\)](#) standards, using the parties' Proposed Pretrial Order as a guide--not pursuant to [Rule 56](#), applying [Rule 56\(c\)](#) standards; not pursuant to [Rule 12\(b\)\(6\)](#), working solely within the confines of the [\*281] written pleadings; and not in the context of the imposition of discovery sanctions against the plaintiffs pursuant to [Rule 37\(b\)\(2\)](#).<sup>121</sup>

## Claims Against San Juan County and the SJHSD

As explained above, the pretrial examination of the Part I Plaintiffs' causes of action leads to the conclusion that these plaintiffs have no viable federal causes of action against either San Juan County or the San Juan Health Services District. The remaining state tort law claims involve intentional torts allegedly committed by one or more individual defendants.

## Claims Against the Individual Defendants

The colloquy at the Final Pretrial Conference confirmed that as against the individual defendants--Commissioner Tyron Lewis, Commissioner Bill Redd, County Attorney Craig Halls, Reid [\*282] Wood, Cleal Bradford, Roger Atcity, John Lewis, John Housekeeper, Karen Adams, Patsy Shumway, Dr. Lloyd Val Jones, Dr. Manfred Nelson, Rick Bailey, Marilee Bailey, Ora Lee Black, Gary Holliday, Carla Grimshaw, Gloria Yanito, and Julie Bronson--the Part I Plaintiffs have failed to allege legally viable [§ 1983](#) claims against these defendants, even taking plaintiffs' factual allegations as true and treating them in the light most favorable to the plaintiffs. Plaintiffs' federal antitrust claims fail as against these defendants as well.

As against County Attorney Craig Halls, the Part I Plaintiffs have alleged no wrongful conduct whatsoever. Essentially the same may be said for defendant Carla Grimshaw. Defendants Ora Lee Black and Gloria Yanito are alleged to have communicated [\*1202] directions concerning Ms. Lyman's staff privileges that purportedly originated with Dr. Redd, the SJHSD medical director, or Ms. Schafer, the patient care director. By themselves, these allegations do not state an arguable legal claim under the plaintiffs' remaining state tort law theories. Nor

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<sup>121</sup> See, e.g., [Ehrenhaus v. Reynolds](#), 965 F.2d 916, 921 (10th Cir. 1992) (district court acted within its discretion under [Fed. R. Civ. P. 37\(b\)\(2\)\(C\)](#) in dismissing complaint with prejudice as sanction for violation of discovery order when securities fraud plaintiff failed to appear for scheduled deposition notwithstanding court's order and warning that court would dismiss complaint if plaintiff did not comply with order).

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does it appear that any remaining state law claim was pleaded against defendant Lori Wallace. (See Proposed Pretrial [**\*\*283**] Order at 5-6 PP(20)-(25).)

Likewise, the Part I Plaintiffs complain of the County Commissioners and SJHSD Board members *inaction* on their behalf, but allege no intentionally tortious acts by any of these defendants that establish any of the elements of the remaining state law causes of action for interference with contract, interference with prospective business relations, defamation and intentional infliction of emotional distress.

### **Dr. MacArthur's State Law Tort Claims**

As against defendant Julie Bronson (and possibly Marilee Bailey, Laurie Schafer and Cleal Bradford, ( see Proposed Pretrial Order at 25 P 96)), Dr. MacArthur alleges facts that, when taken in the light most favorable to him, may support a state law defamation claim. Whether he alleged a non-frivolous claim of interference with contract or interference with prospective business relations against those few individual defendants who were directly involved with his request for full provisional staff privileges appears more doubtful. He did not allege facts that would support a claim for intentional infliction of emotional distress against any defendant.

Dr. MacArthur's federal claims having been dismissed pursuant to [Fed. R. Civ. P. 16\(c\)\(1\)](#), [**\*\*284**] this court declines to exercise supplemental jurisdiction pursuant to [28 U.S.C. § 1367\(a\)](#) (2000) over his remaining state law tort claims of defamation against Ms. Bronson (or others), and interference with contract/prospective business relations against Dr. Redd, Mr. Bradford or others who had direct involvement with Dr. MacArthur's December 1999 request for full one-year provisional privileges pursuant to the SJHSD medical staff bylaws. See [28 U.S.C. § 1367\(c\)\(3\)](#) (2000). Dr. MacArthur has pleaded no other non-frivolous state tort claims against any other defendant.

### **Ms. Lyman's State Law Tort Claims**

From an examination of the Proposed Amended Complaint, the Proposed Pretrial Order and through the colloquy at the Final Pretrial Conference, it became increasingly apparent that Ms. Lyman was not claiming a *denial* of practice privileges as much as she was alleging intentional interference by some defendants with the *exercise* of practice privileges which Ms. Lyman understood she had already been granted by the SJHSD and which remained in effect until December 22, 1999. She alleges a series of incidents in which her orders for laboratory tests, heart monitors, injections, x-rays and other [**\*\*285**] routine procedures would be refused or ignored, often at the instance or direction of Dr. Redd. ( See *supra* n.69 and accompanying text.)

While such incidents may not amount to a constitutional deprivation actionable under [§ 1983](#) and subject to claims of qualified immunity--they may constitute at least a colorable state tort claim. An excluded practitioner may be able to avoid the qualified privilege barrier to [§ 1983](#) claims by pleading and proving that an individual defendant's actions were taken to satisfy a personal grudge, not in the best interests of the hospital, and therefore constituted an intentional tort, such as interference with contractual relations. See, e.g., [Straube v Emanuel Lutheran Charity Bd.](#), 287 Or. 375, <sup>A</sup>12031 600 P.2d 381 (1979), cert. denied, 445 U.S. 996, 100 S. Ct. 1657, 64 L. Ed. 2d 242 (1980). In addition, non-tort theories such as breach of contract may be available to remedy discrepancies between reasonable expectations as to practice privileges and restrictions imposed upon their actual exercise.

**HN93** [↑] Because the Hospital bylaws constitute "a contract between the hospital and the physician," [Rees, 808 P.2d at 1076](#), the Hospital must comply with those bylaws when [**\*\*286**] taking actions which effect its staff. Moreover, we agree with the weight of authority which grants deference to hospital officials' professional judgment. Under this authority, courts require that a hospital only "substantially comply" with its bylaws. See, e.g., [Hosp. Owens v. New Britain Gen. , 32 Conn. App. 56, 627 A.2d 1373, 1379-80 \(Conn. App. 1993\)](#)aff'd,229 Conn. 592, 643 A.2d 233 (Conn. 1994); [Friedman v. Memorial Hosp.](#), 523 N.E.2d 252, 253 (Ind. App. 1988); [Smith v. Our Lady of the Lake Hosp.](#), 639 So. 2d 730, 755 (La. 1994); [Mahmoodian v. United Hosp. Ctr., Inc.](#), 185 W. Va. 59, 404 S.E.2d 750, 755 (W. Va.), cert. denied, 502 U.S. 863, 112 S. Ct. 185, 116 L. Ed. 2d 146 (1991); see also [Piacitelli v. Southern Utah State College](#), 636 P.2d 1063, 1066-67 (Utah 1981)

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(finding substantial compliance with policies in college personnel manual sufficient to withstand due process attack); see generally Kathleen M. Dorr, Annotation, *Exclusion of, or Discrimination Against, Physician or Surgeon by Hospital*, 28 A.L.R. 5th 107, § 3, at 152-67 (1995 & Supp. 1996) (collecting cases). Substantial compliance with the bylaws adequately serves their primary purpose, which is to ensure fair procedures [\*\*287] for staffing decisions. See, e.g., [Owens, 627 A.2d at 1379-80](#).

[Houston v. Intermountain Health Care, Inc., 933 P.2d 403, 408 \(Utah Ct. App. 1997\)](#).<sup>122</sup>

Plaintiff Lyman may also have viable state tort claims against Dr. Redd for defamation and intentional infliction of emotional distress. Defamation claims under Utah law are constrained by the one-year limitations statute, but claims for intentional infliction of emotional distress have a much longer temporal reach:

Utah Code section 78-12-25(3) permits an action for intentional infliction of emotional distress to be brought within four years of actionability. See Utah Code Ann. § 78-12-25(3) (2002) ("An action may be brought within four years ... for relief not otherwise provided by law."); see also [Rutherford, 844 P.2d at 975](#) (applying section 78-12-25(3) to determine the statute of limitations for the plaintiff's intentional infliction of emotional distress claim).

In *Rutherford*, the Utah Supreme Court noted that "because [\*\*288] of the nature of [an intentional infliction of emotional distress] cause of action, it can be difficult to determine when all its elements--intentional, outrageous conduct proximately causing extreme distress--have come into being. Of particular difficulty is the element of injury--extreme emotional distress. " [844 P.2d at 975](#). However, the difficulty in determining when the emotional distress occurred is generally limited to situations "where a defendant subjects a plaintiff not to a single outrageous act, but to a pattern or practice of acts." *Id.*

[Christensen v. Drossos, 2005 UT App 170, 2005 WL 851700, \\*1](#). Furthermore, "When conduct that [\*1204] would give rise to a claim of intentional infliction of emotional distress is continuous and ongoing, and it is unclear when the plaintiff suffered severe emotional distress, the statute of limitations begins to run from the time the last injury is suffered or the tortious conduct ceases." [Hatch v. Davis, 102 P.3d 774, 2004 UT App 378, P 44, 102 P.3d 774, 785](#) (footnote omitted).

Ms. Lyman's federal claims having been dismissed at the conclusion of the Final Pretrial Conference, this court declines to exercise supplemental jurisdiction under [28 U.S.C. § 1367\(a\)](#) [\*\*289] over her remaining state law tort claims. See [28 U.S.C. § 1367\(c\)\(3\)](#). Those claims, therefore, will be dismissed *without* prejudice.

### **Summary re: the Final Pretrial Conference**

As the court explained at the conclusion of the Final Pretrial Conference, "The effort is again to sort out as best we can what the contentions are and the footings for those contentions," a process "resulting in the orders that the court has indicated." Tr. 11/15/02, at 228:8-10 (the court.).

In revisiting that sorting process in the process of preparing this more formal written disposition of the issues presented, the court has elaborated upon the legal and factual bases for its bench ruling in somewhat greater detail. The court has also taken this opportunity to clarify the jurisdictional disposition of the plaintiffs' few remaining state law claims in the interest of avoiding at least some confusion concerning those matters.

Initially, the court had called upon counsel for the prevailing parties to prepare proposed forms of order memorializing the court's bench ruling at the pretrial conference, consistent with this court's local rule, [DUCivR 54-1\(a\) & \(b\)](#):

<sup>122</sup> In dealing with the enforcement of the terms of written hospital bylaws, presumably the Utah six-year limitations statute for actions based upon written contracts would apply. See Utah Code Ann. § 78-12-23(2) (2002).

**HN94** [↑] **(a) Orders in Open Court.** Unless otherwise determined [\*\*290] by the court, orders announced in open court in civil cases must be prepared in writing by the prevailing party, served within five (5) days of the court's action on opposing counsel, and submitted to the court for signature pursuant to the provisions of section (b) of this rule.

**(b) Orders and Judgments.** Unless otherwise determined by the court, proposed orders and judgments prepared by an attorney must be served upon opposing counsel for review and approval as to form prior to being submitted to the court for review and signature. Approval will be deemed waived if no objections are filed within five (5) days after personal service or eight (8) days after service by mail.

The preparation of proposed forms of order led to another series of objections, revisions, hearings, and supplemental memoranda on the same. ( See Plaintiff's Formal Objection to the Court assigning the drafting of the Final Dismissal Order to the Defense Counsel, filed November 20, 2002 (dkt. no. 458); Proposed Final Order of Dismissal with Prejudice, received November 22, 2002; Proposed Order Denying Plaintiffs' [Rule 15](#) Motion to Amend, received November 26, 2002; Plaintiffs' Objection to the Form of the Proposed [\*\*291] Dismissal Order, filed November 27, 2002 (dkt. no. 465); Plaintiffs' Objection to the Defendants' Proposed Order Denying the Plaintiffs' Motion to Amend the Complaint, filed December 27, 2002 (dkt. no. 477); Transcript of Hearing, dated February 24, 2003, at 26:17-31:15, 71:8-12; Proposed Order of Dismissal With Prejudice, received March 4, 2003; Objection to the Defendants' Proposed Order of Dismissal With Prejudice, filed March 10, 2003 (dkt. no. 511); Transcript of Hearing, dated December 19, 2003; Supplemental Objections to the Final Orders of Dismissal of Federal and State Law Claims, filed December 29, 2003 (dkt. no. 585).

[\*1205] In preparing this written disposition of the Part I Plaintiffs' claims, the court has also taken the opportunity to address several of the objections raised by the plaintiffs to the proposed forms of order earlier submitted by counsel,<sup>123</sup> particularly where those objections were directed against the substance of the court's bench ruling or the conduct of the pretrial conference, as opposed to the *form* of the proposed orders reflecting that ruling. Cf. [DUCivR54-1\(b\)](#).

## PLAINTIFFS' MOTION FOR LEAVE TO FILE AN AMENDED COMPLAINT

It has long been understood that **HN95** [↑] "the Federal Rules encourage litigants to plead only a simple statement, in sequence, of the events which have transpired, coupled with a direct claim by way of demand for judgment." [Meadow Gold Products Co. v. Wright, 108 U.S. App. D.C. 33, 278 F.2d 867, 869 \(D.C. Cir. 1960\)](#) (citing [Gins v. Mauser Plumbing Supply Co., 148 F.2d 974 \(2d Cir. 1941\)](#)). From the commencement of this litigation, plaintiffs' counsel has taken a dramatically different approach to pleading the Part I Plaintiffs' claims, at times shuffling each plaintiff's factual allegations and legal assertions together as one would a deck of playing cards, sacrificing narrative [\*\*293] sequence in favor of argumentative characterizations and conclusory assertions.

Plaintiffs' Proposed Amended Complaint was no exception. Filed a week before the Final Pretrial Conference, "Plaintiffs' [Rule 15](#) Motion to Amend and Supplement Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," and "Memorandum of Fact and Law in Support," filed November 6, 2002 (dkt. no. 438), sought leave to file the Proposed Amended Complaint in order to correct any deficiencies in the plaintiffs' pleadings referred to by the Tenth Circuit in [MacArthur v. San Juan County, 309 F.3d 1216 \(10th Cir. 2002\)](#), and to amend plaintiffs' pleadings to conform to the evidence and clarify the remaining issues. See [Fed. R. Civ. P. 15\(b\)](#). The defendants did not have an opportunity to respond to that motion before the Final Pretrial Conference began on November 14, 2002.

<sup>123</sup> ( See, e.g., Plaintiffs' Objection to the Form of the Proposed Dismissal Order, filed [\*\*292] November 27, 2002 (dkt. no. 465), at 3, 5 ("the Plaintiffs should be allowed to know what legal theories and facts and rules the Court was relying upon for dismissing each Plaintiffs' claim in the pretrial setting. Plaintiffs should not be forced to ferret out by intuition what the Court meant, was thinking at the time, or intended .... Plaintiffs respectfully request the Court itself to identify the claims of the Plaintiffs and the reasons for their dismissal." ).)

At the conclusion of the Final Pretrial Conference on February 15, 2002, the court made a bench ruling denying the motion for leave to amend:

MS. ROSE: I've put in a motion to amend the complaint and I drafted it in 2 parts. Since these plaintiffs have been dismissed is there any way of procedurally just looking at amending the **[\*\*294]** complaint for the second part?

THE COURT: Well I dealt with the important aspect of the amended complaint, namely the emergency room problem and I've dealt with that and I'll simply deny the motion to amend.

MS. ROSE: No, no, I meant no, Your Honor, I'm sorry, I didn't mean for these 3 plaintiffs that have been dismissed, I understand they are gone. What I'm talking about is I amended the complaint that I originally filed for Singer, Riggs and Dickson and is that motion for amending that part of the complaint still viable?

THE COURT: No, the motion is denied.

**[\*1206]** Tr. 11/15/02, at 119:8-23.) The court again addressed the matter at the February 24, 2003 hearing on all pending motions. ( See Transcript of Hearing, dated February 24, 2003, at 36:21-23 ("We dealt with the question of amendments and I have indicated to you that as an amendment the answer is no." (the court).) A proposed form of order denying the motion was submitted to the court, as were objections thereto, and the proposed order has not been entered.

Having reviewed the record in this matter in preparing this written disposition, the court has again examined the motion for leave to amend as well as the Proposed Amended Complaint. **[\*\*295]** The allegations of the Proposed Amended Complaint, prolix and circuitous as they are, correspond far more closely to the issues as framed by counsel in the Proposed Pretrial Order than do the even more prolix and partially obsolete allegations of the original Complaint, as earlier amended. ( See Complaint (Verified), filed July 25, 2000 (dkt. no. 1); "Amendments to the Complaint; Correction of Errors," filed August 1, 2000 (dkt. no. 3).)

**HN96** While generally, motions to amend a complaint to conform to the evidence "are made at trial or in the immediate aftermath of trial," Steven Baicker-McKee, et al., *Federal Civil Rules Handbook* 337 (2000 ed.), the express language of Rule 15(b) does not limit such motions to that context.

Viewing the Proposed Amended Complaint as the best statement of plaintiffs' claims as of the time of pretrial, and given the close relationship between the proposed pleading and the Proposed Pretrial Order, it likely would serve the interests of clarity of the record to grant the leave to amend as requested, and direct the filing of the Proposed Amended Complaint *nunc pro tunc* to November 14, 2002, the date of the Final Pretrial Conference. Granting leave to amend **[\*\*296]** on that basis avoids confusion between the Part I Plaintiffs' claims as pleaded in the original Complaint and their claims as addressed in the context of pretrial, and does so without reviving any claims that were disposed of in the course of the Final Pretrial Conference. Granting leave to amend also serves to clarify the remaining plaintiffs' claims as pleaded in Part II of the Proposed Amended Complaint, concerning the enforcement of certain orders of the Navajo Tribal Court. Therefore, the court concludes that its earlier bench ruling concerning the "Plaintiffs' Rule 15 Motion to Amend and Supplement Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," filed November 6, 2002 (dkt. no. 438), should be vacated and the motion should be granted *nunc pro tunc* to November 14, 2002.

## THE PART I PLAINTIFFS' MOTIONS FOR RECONSIDERATION

In the months since the November 2002 pretrial conference, court and counsel have addressed matters concerning the claims of the remaining three plaintiffs, Singer, Riggs and Dickson, and the questions of Navajo Tribal Court jurisdiction they have raised. In addition, the court has heard, considered and ruled upon a series of motions **[\*\*297]** filed by the parties, including a request for a settlement conference, which was granted, ( see Minute Entry, dated July 6, 2004.(dkt. no. 657)), but apparently to no avail. ( See Minute Entry, dated September 28, 2004 (dkt. no. 663).)

Shortly after the reported failure of the settlement conference, the Part I Plaintiffs' filed a series of motions for reconsideration of the court's bench rulings at the Final Pretrial Conference, coupled with motions for summary judgment in favor of the Part I Plaintiffs pursuant to [Fed. R. Civ. P. 56](#). ( See Plaintiff Valdez's Motion for the Court to Reconsider its Motion to [\[\\*1207\]](#) Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 664); Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670); Plaintiff Lyman's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' [sic] Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed December 28, 2004 (dkt. no. 695).) Responsive memoranda were filed by the defendants, [\[\\*\\*298\]](#) followed by the plaintiffs' reply memoranda and several additional motions.<sup>124</sup>

**[HN97](#)** Except to the extent that a motion under [Fed. R. Civ. P. 60\(b\)](#) or [Fed. R. Civ. P. 59\(e\)](#) is deemed a "motion for reconsideration," the Federal Rules do not expressly provide for such motions. Nevertheless, in this circuit, a "motion for reconsideration" may be made on one or more specific grounds:

Grounds warranting a motion to reconsider include (1) an intervening change in the controlling law, (2) new evidence previously unavailable, and (3) the need to correct clear error or prevent manifest injustice. See [Brumark Corp. v. Samson Resources Corp.](#), 57 F.3d 941, 948 (10th Cir. 1995). Thus, a motion for reconsideration is appropriate where the court has misapprehended the facts, a party's position, or the controlling law.

[Servants of the Paraclete v. Doe, 204 F.3d 1005, 1012 \(10th Cir. 2000\).](#)

Here, the Part I Plaintiffs urge reconsideration [\[\\*\\*300\]](#) of this court's November 15, 2002 bench ruling on most, if not all of the available grounds. ( See Memorandum of Points and Authorities Supporting Plaintiff Valdez's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 665), *passim*; Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), *passim*; Memorandum in Support of Plaintiff Lyman's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' [sic] Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed December 28, 2004 (dkt. no. 696), *passim*.) They also raise additional issues *not* addressed at pretrial, particularly as to the nature of the relationships between [\[\\*1208\]](#) various defendants, their liability insurers and their counsel of record.

The court has reviewed and considered the Part I Plaintiffs' motions for reconsideration and supporting memoranda and exhibits as part of the process of preparing this written embodiment of that bench [\[\\*\\*301\]](#) ruling, and has referred to them more than once in the foregoing analysis of the plaintiffs' various claims. The Part I Plaintiffs' "new evidence previously unavailable" consists largely of deposition testimony of a SJHSD officer obtained in another federal lawsuit relating conversations about non-parties, or evidence of collateral matters concerning the background and credibility of one or more of the individual defendants, ( e.g., unrelated prior criminal convictions).

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<sup>124</sup> ( See "Plaintiffs' MacArthur, Lyman, Valdez' Motion for Sanctions," filed January 25, 2005 (dkt. no. 703); San Juan County Defendants' Combined (1) Memorandum in Opposition to Plaintiff Valdez' Motion to Reconsider and (2) Motion for an Extension of Time to Respond to Motion for Summary Judgment, filed November 29, 2004 (dkt. no. 673); San Juan County Defendants' Combined (1) Memorandum in Opposition to Plaintiff MacArthur's Motion to Reconsider and (2) Motion for an Extension of Time to Respond to Cross-Motion for Summary Judgment, filed December 13, 2004 (dkt. no. 682); Motion for an Extension of Time to Respond to MacArthur's November 29, 2004 Motion for Summary Judgment (Health District), filed December 14, 2004 (dkt. no. 684); Health District Defendants' Joinder in Motion, filed December 21, 2004 (dkt. no. 690); Motion for an Extension of Time to Respond to Lyman's December 26, 2004 Motion for Summary Judgment (Health District), filed January 14, 2005 (dkt. no. 699); San Juan County Defendants' Combined (1) Memorandum in Opposition to Plaintiff Lyman's Motion to Reconsider and (2) Motion for an [\[\\*\\*299\]](#) Extension of Time to Respond to Cross-Motion for Summary Judgment, filed January 18, 2005 (dkt. no. 701); Joinder in San Juan County Defendants' Combined (1) Memorandum in Opposition to Plaintiff Lyman's Motion to Reconsider and (2) Motion for an Extension of Time to Respond to Cross-Motion for Summary Judgment, filed February 3, 2005 (dkt. no. 706).)

The plaintiffs also complain of materials not produced by the defendants in discovery in this action. They also use these motions as an opportunity to adjust their legal contentions and theories of liability.

In large part, however, the Part I Plaintiffs' motions for reconsideration simply reargue the same legal claims grounded upon the same factual allegations as were set forth in the Proposed Amended Complaint and the Proposed Pretrial Order, and discussed in some detail at the Final Pretrial Conference.

Having examined the motions for reconsideration, the court concludes that in each instance, the motion presents no exceptional circumstances justifying relief from the court's prior bench ruling as it has been further [<sup>\*\*302</sup>] explicated herein. Cf. *Bud Brooks Trucking, Inc. v. Bill Hodges Trucking Co.*, 909 F.2d 1437, 1440 (10th Cir. 1990) [HN98↑](#) ("Relief under Rule 60(b) is extraordinary and may only be granted in exceptional circumstances."). The Part I Plaintiffs have failed to point to "new evidence previously unavailable" that materially alters the existing factual footing for their claims; nor have they established a "need to correct clear error or prevent manifest injustice" as to any claim that has been dismissed on its merits, as detailed above.

Therefore, the Part I Plaintiffs' motions for reconsideration should in each instance be denied in all respects.<sup>125</sup>

## CONCLUSION

With the determination of the Part I Plaintiffs' motions for reconsideration and for sanctions, this court's consideration of these plaintiffs' [<sup>\*\*303</sup>] claims against the remaining defendants draws to a close. Based upon detailed examination in the context of the Final Pretrial Conference, the Part I Plaintiffs' claims have been dismissed pursuant to Fed. R. Civ. P. 16(c)(1), on the merits and with prejudice, with the exception of the remaining state tort law claims of plaintiffs MacArthur and Lyman for interference with contract, interference with prospective business relations, defamation and/or intentional infliction of emotional distress as against defendants Redd, Jones, Schafer, Nelson, and Bradford, as well as defendants Bronson and Marilee Bailey (defamation only), over which this court declines to exercise supplemental jurisdiction, see 28 U.S.C. § 1367(c); those claims shall be dismissed without prejudice.

The claims asserted and issues raised by the remaining plaintiffs, Singer, Riggs and Dickson, and the defenses and issues [<sup>\*1209</sup>] raised by the remaining defendants in response to those plaintiffs' claims, currently remain under advisement, and will be addressed in a separate written disposition to be issued in due course. The claims of plaintiffs Singer, Riggs and Dickson having already been submitted for decision, the remaining [<sup>\*\*304</sup>] defendants need not answer or otherwise respond to the plaintiffs' Amended Complaint, which has been directed to be filed herein, *nunc pro tunc* to November 14, 2002.

Good cause thus appearing therefor,

**IT IS ORDERED** that the "Plaintiffs' Rule 15 Motion to Amend and Supplement Complaint to Conform to the Evidence & the 10th Cir. Court 10-7-02 Opinion," and "Memorandum of Fact and Law in Support," filed November 6, 2002 (dkt. no. 438), shall be and hereby is GRANTED *nunc pro tunc* to November 14, 2002; the Clerk of the Court is directed to file the proposed Amended Complaint annexed thereto in the record in this action (Civil No. 2:00-CV-584BSJ)<sup>126</sup> and enter the same upon the docket forthwith;

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<sup>125</sup> The denial of plaintiffs' motions for reconsideration renders moot their accompanying motions for summary judgment. Thus, no further response by the defendants to the latter motions is required. ( See Order re: Pending Motions, filed March 30, 2005 (dkt. no. 7]8), at 5-6.)

"Plaintiffs' MacArthur, Lyman, Valdez' Motion for Sanctions," filed January 25, 2005 (dkt. no. 703), shall likewise be denied.

<sup>126</sup> The caption of the Proposed Amended Complaint erroneously refers to "civil no. 92-C-1071TS," a case currently assigned to Chief Judge Benson.

**IT IS FURTHER ORDERED** that the claims of plaintiff Dr. Steven MacArthur shall be and hereby are DISMISSED with prejudice as against all of the defendants named herein, except that the court declines to exercise supplemental jurisdiction over his claims for intentional interference with contract, intentional interference with prospective business relations **[\*\*305]** and defamation as against defendants Dr. James Redd, Dr. L. Val Jones, Laurie Schafer, Dr. Manfred Nelson, and Cleal Bradford, Julie Bronson and Marilee Bailey, see 28 U.S.C. § 1367(c); those claims are hereby DISMISSED without prejudice;

**IT IS FURTHER ORDERED** that the claims of plaintiff Michele Lyman shall be and hereby are DISMISSED with prejudice as against all of the defendants named herein, except that the court declines to exercise supplemental jurisdiction over her claims for intentional interference with contract, intentional interference with prospective business relations, defamation and intentional infliction of emotional distress as against defendants Dr. James Redd, Dr. L. Val Jones, Laurie Schafer, Dr. Manfred Nelson, and Cleal Bradford, see 28 U.S.C. § 1367(c); those claims are hereby DISMISSED without prejudice;

**IT IS FURTHER ORDERED** that the claims of plaintiff Helen Valdez shall be and hereby are DISMISSED with prejudice as against the defendants named herein, and in particular defendants Lori Wallace and the San Juan Health Services District;

**IT IS FURTHER ORDERED** that Plaintiff Valdez's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' **[\*\*306]** Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed October 26, 2004 (dkt. no. 664), is hereby DENIED;

**IT IS FURTHER ORDERED** that Plaintiff MacArthur's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed November 23, 2004 (dkt. no. 670), is hereby DENIED;

**IT IS HEREBY ORDERED** that Plaintiff Lyman's Motion for the Court to Reconsider its Motion to Dismiss Plaintiff's Valdez' [sic] Discrimination Claims and Plaintiffs' Cross-Motion for Summary Judgment, filed December 28, 2004 (dkt. no. 695), is hereby DENIED;

**IT IS FURTHER ORDERED** that "Plaintiffs' MacArthur, Lyman, Valdez' **[\*1210]** Motion for Sanctions," filed January 25, 2005 (dkt. no. 703), is hereby DENIED; and

**IT IS FURTHER ORDERED** that a printed copy of the Proposed Pretrial Order, received by the court on November 12, 2002, shall be lodged by the Clerk of the Court in the file as part of the record in this action, and that an electronic (.pdf format) copy of the Proposed Pretrial Order shall be appended by the Clerk of the Court to the electronic (.pdf format) copy of this Memorandum Decision & Order and be made available as part **[\*\*307]** of the permanent CM/ECF case record in this action.

DATED this 13 day of June, 2005.

BY THE COURT:

BRUCE S. JENKINS

United States Senior District Judge



## *Freeman v. Lasky, Haas & Cohler*

United States Court of Appeals for the Ninth Circuit

February 16, 2005, Argued and Submitted, Pasadena, California ; June 14, 2005, Filed

No. 03-56588

### **Reporter**

410 F.3d 1180 \*; 2005 U.S. App. LEXIS 11132 \*\*; 2005-1 Trade Cas. (CCH) P74,827

ARLEEN FREEMAN, individually and on behalf of all others similarly situated; JAMES ALEXANDER, individually and on behalf of all others similarly situated, Plaintiffs-Appellants, v. LASKY, HAAS & COHLER, a professional corporation; CHARLES B. COHLER; LUCE, FORWARD, HAMILTON & SCRIPPS; CHRISTOPHER J. HEALEY; WHITE AND BRIGHT, a professional corporation; DAVID S. BRIGHT; MUSICK, PEELER & GARRETT LLP; MICHAEL J. HICKMAN; JON F. MCKINLEY; CALIFORNIA ASSOCIATION OF REALTORS, INC.; JOHN LOMAC; MARK MARCHAND; DIANNE MCMILLAN; SHARE JACKSON; SCOTT HUBAL; JUNE BARLOW, Defendants-Appellees.

**Prior History:** [\*\*1] Appeal from the United States District Court for the Southern District of California. D.C. No. CV-03-00715 MJL/JAH. M. James Lorenz, District Judge, Presiding.

**Disposition:** AFFIRMED.

## **Core Terms**

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sham, lawsuit, antitrust, discovery, Sherman Act, misconduct, immunity, incidental, petitions, realtors'

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

### **HN1** [blue icon] **Exemptions & Immunities, Noerr-Pennington Doctrine**

The Noerr-Pennington doctrine extends to all three branches of government, and thus exempts bringing a lawsuit--that is, petitioning a court--from antitrust liability.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

### **HN2** [blue icon] **Noerr-Pennington Doctrine, Sham Exception**

While Noerr-Pennington immunity is broad, it is not so broad as to cover all litigation: "Sham" petitions don't fall within the protection of the doctrine. There are three circumstances when litigation might be sham: First, if the alleged anticompetitive behavior consists of bringing a single sham lawsuit (or a small number of such suits), the antitrust plaintiff must demonstrate that the lawsuit was (1) objectively baseless, and (2) a concealed attempt to interfere with the plaintiff's business relationships. Second, if the alleged anticompetitive behavior is the filing of a series of lawsuits, the question is not whether any one of them has merit--some may turn out to, just as a matter of chance--but whether they are brought pursuant to a policy of starting legal proceedings without regard to the merits and for the purpose of injuring a market rival. Finally, in the context of a judicial proceeding, if the alleged anticompetitive behavior consists of making intentional misrepresentations to the court, litigation can be deemed a sham if a party's knowing fraud upon, or its intentional misrepresentations to, the court deprive the litigation of its legitimacy.

[Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope](#)

[Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception](#)

### **HN3 Exemptions & Immunities, Noerr-Pennington Doctrine**

Noerr-Pennington immunity from antitrust liability, and the sham exception, also apply to defensive pleadings, because asking a court to deny one's opponent's petition is also a form of petition; thus, the courts speak of a "sham defense" as well as a "sham lawsuit."

[Antitrust & Trade Law > Sherman Act > Scope > Exemptions](#)

[Civil Procedure > ... > Pleadings > Counterclaims > General Overview](#)

[Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom to Petition](#)

[Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity](#)

### **HN4 Scope, Exemptions**

Because the Noerr-Pennington doctrine grows out of the Petition Clause, its reach extends only so far as necessary to steer the Sherman Act, [15 U.S.C.S. §§ 1 to 3](#), clear of violating the [First Amendment](#). Immunity thus applies only to what may fairly be described as petitions, not to litigation conduct generally. A complaint, an answer, a counterclaim and other assorted documents and pleadings, in which plaintiffs or defendants make representations and present arguments to support their request that the court do or not do something, can be described as petitions without doing violence to the concept. But discovery is merely communication between parties as an aid to litigation. It is not in any sense a communication to the court and is therefore not a petition. Nevertheless, conduct incidental to a petition is protected by Noerr-Pennington if the petition itself is protected.

[Antitrust & Trade Law > Sherman Act > Defenses](#)

[Antitrust & Trade Law > Clayton Act > Defenses](#)

410 F.3d 1180, \*1180L<sup>2005 U.S. App. LEXIS 11132, \*\*1</sup>

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity

## **HN5** Sherman Act, Defenses

Discovery, like settlement talks, is conduct incidental to a petition for purposes of the Noerr-Pennington exception to antitrust liability. Thus, whether discovery misconduct violates the Sherman Act, [15 U.S.C.S. §§ 1 to 3](#), depends on whether the defense as a whole would be actionable.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Civil Procedure > Sanctions > General Overview

Real Property Law > Torts > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

## **HN6** Noerr-Pennington Doctrine, Sham Exception

To apply the sham exception to Noerr-Pennington immunity in the context of a defense, courts look to the test for a sham lawsuit spelled out in the first Kottle exception. This two-part test contains both an objective and a subjective component. On the first prong, the issue is whether the defense is or is not objectively baseless. The existence of probable cause to institute legal proceedings--a notion drawn from the common-law tort of wrongful civil proceedings--precludes a finding that an antitrust defendant has engaged in sham litigation.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

## **HN7** Noerr-Pennington Doctrine, Sham Exception

Under the second part of a definition of sham litigation as an exception to Noerr-Pennington immunity, the court should focus on whether the baseless lawsuit conceals an attempt to interfere directly with the business relationships of a competitor through the use of the governmental process--as opposed to the outcome of that process--as an anticompetitive weapon.

Antitrust & Trade Law > Clayton Act > Defenses

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

## **HN8** Clayton Act, Defenses

For a defense of a lawsuit to be a sham for purposes of the first Kottle sham litigation exception to Noerr-Pennington immunity, plaintiffs would have to show that the defense was not merely baseless, but aimed at interfering with their business by, for example, sapping their financial resources or distracting their attention.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

## **[HN9](#) [+] Exemptions & Immunities, Noerr-Pennington Doctrine**

Noerr-Pennington immunity from antitrust liability is not limited to lawyers. A Noerr-Pennington case need not involve claims against lawyers at all.

**Counsel:** David Barry, Barry & Associates, San Francisco, California, for the plaintiffs-appellants.

Jeffrey M. Shohet and Stanley J. Panikowski, Gray Cary Ware & Freidenrich LLP, San Diego, California; Charles A. Bird, Luce, Forward, Hamilton & Scripps LLP, San Diego, California; Robert F. Semmer, Coughlan, Semmer & Lipman, LLP, San Diego, California; Cheryl A. Orr, Musick, Peeler & Garrett LLP, Los Angeles, California, for the defendants-appellees.

**Judges:** Before: Alex Kozinski, Stephen S. Trott and Richard R. Clifton, Circuit Judges. Opinion by Judge Kozinski.

**Opinion by:** Alex Kozinski

## **Opinion**

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[\*1182] KOZINSKI, Circuit Judge:

We consider the applicability of *Noerr-Pennington* immunity to discovery misconduct.

### **Facts**

Realtor Arleen Freeman subscribes to a regional real-estate Multiple Listing [\*1183] Service (MLS) run by Sandicor, a corporation owned and managed by various local realtors' associations. Charging that Sandicor's MLS subscription fees were fixed at artificially high levels, Freeman sued Sandicor, the realtors' [\*2] associations, and some of their officers and directors under the Sherman Act, [15 U.S.C. §§ 1, 2](#). The defendants in that litigation wrongfully withheld information in discovery. After the misconduct came to light, the district court granted new discovery and sanctioned the defendants, but it nonetheless granted their motion for summary judgment. On appeal, we affirmed in part and reversed in part. [\*Freeman v. San Diego Ass'n of Realtors\*, 322 F.3d 1133 \(9th Cir. 2003\)](#).

Freeman now brings a new antitrust action against some of the executives, lawyers and law firms of the associations involved in the previous litigation, and against the state realtors' association directly, based on the discovery misconduct that, she claims, involved subornation of perjury and intimidation of witnesses. Freeman argues that, by stretching out the litigation, the discovery misconduct postponed the day of judgment and thus

extended Sandicor's price fixing. The district court dismissed the complaint with prejudice for failure to state a claim, based (among other grounds) on the *Noerr-Pennington* doctrine. Freeman appeals.<sup>1</sup>

### [\*\*3] Analysis

1. The *First Amendment* aspect of *antitrust law*, the *Noerr-Pennington* doctrine, was first announced in *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 5 L. Ed. 2d 464, 81 S. Ct. 523 (1961), where the Supreme Court interpreted the Sherman Act, in view of "the right of the people . . . to petition the Government for a redress of grievances," *U.S. Const. amend. I*, to not cover political lobbying:

To hold that the government retains the power to act in [its] representative capacity [to make laws that operate to restrain trade] and yet hold, at the same time, that the people cannot freely inform the government of their wishes would impute to the Sherman Act a purpose to regulate, not business activity, but political activity, a purpose which would have no basis whatever in the legislative history of that Act. . . . Such a construction of the Sherman Act would [also] raise important constitutional questions. The right of petition is one of the freedoms protected by the *Bill of Rights*, and we cannot, of course, lightly impute to Congress an intent to invade these freedoms.

365 U.S. at 137-38 [\*\*4] (footnote omitted); see also *United Mine Workers v. Pennington*, 381 U.S. 657, 669-70, 14 L. Ed. 2d 626, 85 S. Ct. 1585 (1965). **HN1** [↑] The doctrine extends to all three branches of government, and thus also exempts bringing a lawsuit--that is, petitioning a court--from antitrust liability. See *Cal. Motor Transp. Co. v. Trucking Unlimited*, 404 U.S. 508, 510, 30 L. Ed. 2d 642, 92 S. Ct. 609 (1972).

**HN2** [↑] While *Noerr-Pennington* immunity is broad, it is not so broad as to cover all litigation: "Sham" petitions don't fall within [\*1184] the protection of the doctrine. See *Noerr*, 365 U.S. at 144; *Cal. Motor Transp.*, 404 U.S. at 511; *Prof'l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49, 56-57, 123 L. Ed. 2d 611, 113 S. Ct. 1920 (1993). We have recognized three circumstances when litigation might be sham:

First, if the alleged anticompetitive behavior consists of bringing a single sham lawsuit (or a small number of such suits), the antitrust plaintiff must demonstrate that the lawsuit was (1) objectively baseless, and (2) a concealed attempt to interfere with the plaintiff's business relationships.

Second, if the alleged [\*\*5] anticompetitive behavior is the filing of a series of lawsuits, "the question is not whether any one of them has merit--some may turn out to, just as a matter of chance--but whether they are brought pursuant to a policy of starting legal proceedings without regard to the merits and for the purpose of injuring a market rival."

Finally, in the context of a judicial proceeding, if the alleged anticompetitive behavior consists of making intentional misrepresentations to the court, litigation can be deemed a sham if "a party's knowing fraud upon, or its intentional misrepresentations to, the court deprive the litigation of its legitimacy."

*Kottle v. Northwest Kidney Ctrs.*, 146 F.3d 1056, 1060 (9th Cir. 1998) (citations omitted) (quoting *USS-POSCO Indus. v. Contra Costa County Bldg. & Constr. Trades Council*, 31 F.3d 800, 811 (9th Cir. 1994); *Liberty Lake Invs., Inc. v. Magnuson*, 12 F.3d 155, 159 (9th Cir. 1993)).

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<sup>1</sup> The complaint was filed as a separate action because the statute of limitations was about to run out and our mandate in the original case, which would have officially remanded the action, hadn't yet issued. Freeman requested that the district court classify the complaint as supplemental to the original case when it regained jurisdiction. The district court, however, did not consolidate the action with the original lawsuit, but continued to treat it as a separate lawsuit. Its dismissal is therefore a final judgment subject to appeal pursuant to *28 U.S.C. § 1291*.

[HN3](#) <sup>↑</sup> *Noerr-Pennington* immunity, and the sham exception, also apply to defensive pleadings, see [In re Burlington N., Inc.](#), 822 F.2d 518, 532-33 (5th Cir. 1987), because asking a court to [\*\*6] deny one's opponent's petition is also a form of petition; thus, we may speak of a "sham defense" as well as a "sham lawsuit."

2. [HN4](#) <sup>↑</sup> Because the *Noerr-Pennington* doctrine grows out of the [Petition Clause](#), its reach extends only so far as necessary to steer the Sherman Act clear of violating the [First Amendment](#). Immunity thus applies only to what may fairly be described as *petitions*, not to litigation conduct generally. A complaint, an answer, a counterclaim and other assorted documents and pleadings, in which plaintiffs or defendants make representations and present arguments to support their request that the court do or not do something, can be described as petitions without doing violence to the concept. But discovery is merely communication between parties as an aid to litigation. It is not in any sense a communication to the court and is therefore not a petition. See *Theofel v. Farey-Jones*, 359 F.3d 1066, 1078-79 (9th Cir. 2004) (noting that "subpoenaing private parties in . . . private . . . litigation" is hardly petitioning). Nevertheless, "conduct incidental to" a petition is protected by *Noerr-Pennington* if the petition itself is [\*\*7] protected. *Id.* at 1078 (internal quotation mark omitted); cf. [Noerr](#), 365 U.S. at 143-44.

In [Columbia Pictures Industries, Inc. v. Professional Real Estate Investors, Inc.](#), 944 F.2d 1525 (9th Cir. 1991), aff'd on other grounds, 508 U.S. 49, 123 L. Ed. 2d 611, 113 S. Ct. 1920 (1993), we considered whether a refusal to settle a lawsuit could be actionable under the Sherman Act. We held:

A decision to accept or reject an offer of settlement is conduct incidental to the prosecution of the suit and not a separate and distinct activity which might form the basis for antitrust liability. Consequently, [defendant's] ability to establish that [plaintiffs'] refusal to [settle] violated the Sherman Act depends on its success or failure in showing that the [\*1185] [underlying lawsuit] is actionable under the federal antitrust laws.

*Id.* at 1528-29. Because the underlying lawsuit was not a sham, plaintiffs' refusal to settle could not support antitrust liability. [HN5](#) <sup>↑</sup> Discovery, like settlement talks, is "conduct incidental to" a petition--in this case, incidental to the realtors' associations' defense against Freeman's [\*\*8] lawsuit. Thus, whether this particular misconduct violates the Sherman Act depends on whether the defense as a whole would be actionable.

Discovery misconduct, subornation of perjury and witness intimidation are, of course, serious matters. Had they not been brought to light in time, it is entirely possible that they would so have infected the defense of the lawsuit as to make it a sham. But we need not decide that question today because it is clear that the defense here was not a sham.

[HN6](#) <sup>↑</sup> To apply the sham exception in the context of a defense, we look to the test for a sham lawsuit spelled out in the first [Kottle](#) exception. See page 7062 *supra*. This two-part test contains both an objective and a subjective component. On the first prong, the defense was not "objectively baseless." "The existence of probable cause to institute legal proceedings"--a notion drawn from the common-law tort of wrongful civil proceedings--"precludes a finding that an antitrust defendant has engaged in sham litigation." [Prof'l Real Estate Investors](#), 508 U.S. at 62. And here, there was probable cause, because defendants prevailed on their defense in the district court after the [\*\*9] discovery misconduct was discovered, undone and sanctioned. Cf. *Prosser and Keeton on the Law of Torts* 894 (W. Page Keeton ed., 5th ed. 1984) ("A recovery by the plaintiff in the original action usually is regarded as conclusive evidence of the existence of probable cause, even though it is subsequently reversed, unless it can be shown to have been obtained by fraud or other imposition upon the court." (footnotes omitted)).

On the second prong, there is no evidence that the defense as a whole was "a concealed attempt to interfere with the plaintiff's business relations." See also [Prof'l Real Estate Investors](#), 508 U.S. at 60-61 [HN7](#) <sup>↑</sup> ("Under this second part of our definition of sham, the court should focus on whether the baseless lawsuit conceals 'an attempt to interfere directly with the business relationships of a competitor,' through the 'use [of] the governmental process--as opposed to the outcome of that process--as an anticompetitive weapon.'" (quoting [Noerr](#), 365 U.S. at 144 (emphasis added); [City of Columbia v. Omni Outdoor Adver., Inc.](#), 499 U.S. 365, 380, 113 L. Ed. 2d 382, 111 S. Ct. 1344 (1991)) (alteration in original). [\*\*10] [HN8](#) <sup>↑</sup> For a defense of a lawsuit to be a sham for purposes of the first [Kottle](#) exception, plaintiffs would have to show that the defense was not merely baseless, but aimed at interfering with their business by, for example, sapping their financial resources or distracting their attention.

There was enough objective merit and subjective good faith in the defense of the original antitrust suit to cover it, and the conduct incidental to it, with the *Noerr-Pennington* cloak.<sup>2</sup>

[\*1186] [\*\*11] 3. The district court used *Noerr-Pennington* immunity (among other grounds) to dismiss the complaint as to the attorney defendants only; the complaint was dismissed as to the other defendants based on other theories. However, [HN9](#) Noerr-Pennington immunity is not limited to lawyers: The [\*First Amendment\*](#) petition right belongs to the defendants in the original case, though their employees, law firms and lawyers, as their agents in that litigation, get to benefit as well. Indeed, a *Noerr-Pennington* case, such as *Professional Real Estate Investors*, need not involve claims against lawyers at all. *Noerr-Pennington* immunity is a sufficient ground to dismiss the complaint as to all defendants. We therefore affirm the district court's ruling as to the non-lawyer defendants on this alternative ground. See [\*New Kids on the Block v. News Am. Publ'g\*, 971 F.2d 302, 305 \(9th Cir. 1992\)](#) (we may affirm the district court's judgment on any ground fairly presented by the record before us).

**AFFIRMED.**

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<sup>2</sup> Freeman further alleges that, on one occasion, the attorney defendants made false factual representations to the court. Compl. P 37. Unlike Freeman's other allegations, which concern out-of-court misconduct, this one falls within the third [\*Kotte\*](#) exception, under which misrepresentations to the court make a petition a sham if they "deprive the litigation of its legitimacy." See page 7063 *supra*. Our conclusion that the defense as a whole was not a sham also establishes that this isolated instance of litigation misconduct would not, if proven, deprive the defense as a whole of its legitimacy.



## *In re Enron Corp.*

United States Bankruptcy Court for the Southern District of New York

June 14, 2005, Decided

Chapter 11, Case No. 01 B 16034 (AJG) (Confirmed)

**Reporter**

327 B.R. 526 \*; 2005 Bankr. LEXIS 1065 \*\*; 44 Bankr. Ct. Dec. 249

In re: ENRON CORP., et al., Reorganized Debtors.

## Core Terms

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filed rate doctrine, electricity, energy, rates, wholesale, tariff, cases, state law claim, anti trust law, preemption, regulation, market-based, violations, markets, state law, preempted, refunds, sales, manipulation, interstate, courts, file a tariff, transactions, antitrust, remedies, reasons, argues, exclusive jurisdiction, unfair competition, field preemption

## LexisNexis® Headnotes

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Antitrust & Trade Law > Public Enforcement > State Civil Actions

### [HN1](#) [] **Public Enforcement, State Civil Actions**

The Cartwright Act prohibits agreements to limit or reduce the production, or increase the price of merchandise or of any commodity. [Cal. Bus. & Prof. Code § 16720\(b\)](#).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### [HN2](#) [] **Public Enforcement, State Civil Actions**

The Unfair Competition Law prohibits unlawful, unfair, or fraudulent business acts and practices. [Cal. Bus. & Prof. Code § 17200](#).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### [HN3](#) [] **Public Enforcement, State Civil Actions**

The California Commodity Law prohibits fraudulent acts or conduct in connection with the purchase or sale of a commodity. [Cal. Corp. Code §§ 29536-37](#).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **[HN4](#) [+] Public Enforcement, State Civil Actions**

Pursuant to [Cal. Bus. & Prof. Code § 17204](#); [Cal. Govt. Code § 12658](#); [Cal. Bus. & Prof. Code §§ 16750\(c\), 16754, 16760](#), the state can prosecute violations of these state laws on behalf of the people.

Constitutional Law > Supremacy Clause > Federal Preemption

Governments > Federal Government > US Congress

Constitutional Law > Supremacy Clause > General Overview

#### **[HN5](#) [+] Supremacy Clause, Federal Preemption**

Federal preemption of state law is rooted in the [Supremacy Clause, U.S. Const. art. VI, cl. 2](#). Where Congress manifests an intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. Federal courts have rarely identified legislation which has been found to completely preempt state jurisdiction.

Constitutional Law > Supremacy Clause > General Overview

#### **[HN6](#) [+] Constitutional Law, Supremacy Clause**

In the absence of an express preemption by Congress, state law is preempted: (1) when Congress intends that federal law occupy a given field; and (2) to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > Exclusive Jurisdiction

Constitutional Law > ... > Commerce Clause > Interstate Commerce > General Overview

Energy & Utilities Law > Administrative Proceedings > General Overview

Energy & Utilities Law > Administrative Proceedings > Preemption

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > ... > US Federal Energy Regulatory Commission > Civil Actions > Jurisdiction

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

327 B.R. 526, \*526L<sup>2005</sup> Bankr. LEXIS 1065, \*\*1065

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > General Overview

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Utility Companies > General Overview

Energy & Utilities Law > Utility Companies > Buying & Selling of Power

Transportation Law > Interstate Commerce > Federal Powers

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers

## **HN7** Pipelines & Transportation, Electricity Transmission

State actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by the Federal Power Act because the conduct the state sought to condemn was expressly governed by the California Independent System Operator tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to the Federal Energy Regulatory Commission (FERC), both to enforce and to seek remedy. FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the FERC exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states. Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states. Federal Power Act, [16 U.S.C.S. §§ 824-824m](#).

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Communications Law > Regulators > US Federal Communications Commission > Jurisdiction

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Utility Companies > Rates > General Overview

## **HN8** Electric Power Industry, Electricity Distribution & Transmission

[16 U.S.C.S. § 824e](#) provides that upon a determination by the Federal Energy Regulatory Commission (FERC) that any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the FERC, or that any rule, regulation, practice, or contract

affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the FERC shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order. Federal Power Act, [16 U.S.C.S. § 824e](#).

Administrative Law > Agency Adjudication > Informal Agency Action

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > US Federal Energy Regulatory Commission

Energy & Utilities Law > Oil, Gas & Mineral Interests > Purchase Contracts > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

Energy & Utilities Law > Electric Power Industry > Deregulation & Restructuring

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

## [HN9](#) [blue] Agency Adjudication, Informal Agency Action

The Federal Energy Regulatory Commission (FERC) possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, §§ 205, 206(a), [16 U.S.C.S. §§ 824d, 824e\(a\)](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.S. § 7173\(c\)](#).

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

## [HN10](#) [blue] US Federal Energy Regulatory Commission, Authorities & Powers

California entities that transact through the California Independent System Operator (ISO) or the California Power Exchange and engage in improper practices are in violation of filed tariffs. The Federal Energy Regulatory Commission (FERC) and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement.

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Energy & Utilities Law > Administrative Proceedings > General Overview](#)

[Energy & Utilities Law > Administrative Proceedings > Preemption](#)

[Energy & Utilities Law > Antitrust Issues > General Overview](#)

[Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators](#)

[Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview](#)

[Business & Corporate Compliance > ... > Electric Power Industry > State Regulation > Rate Setting & Tariffs](#)

[Business & Corporate Compliance > ... > Governments > State & Territorial Governments > Gaming & Lotteries](#)

## **[HN11](#)[] Regulators, US Federal Energy Regulatory Commission**

Since 1998, the California Independent System Operator and the California Power Exchange tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. "Anomalous market behavior" is: (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation; or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include: (1) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; (2) unexplained or unusual redeclarations of availability; (3) unusual trades or transactions; (4) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and (5) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

[Administrative Law > Separation of Powers > Legislative Controls > Implicit Delegation of Authority](#)

[Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview](#)

[Business & Corporate Law > Corporations > Dissolution & Receivership > Involuntary Dissolution](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers](#)

[Energy & Utilities Law > Antitrust Issues > General Overview](#)

## **[HN12](#)[] Legislative Controls, Implicit Delegation of Authority**

Implicit in Federal Energy Regulatory Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.

Administrative Law > Separation of Powers > Jurisdiction

Governments > Federal Government > Claims By & Against

Administrative Law > Separation of Powers > Primary Jurisdiction

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

#### **HN13** Separation of Powers, Jurisdiction

The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### **HN14** Exemptions & Immunities, Filed Rate Doctrine

While market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

#### **HN15** Energy & Utilities Law, Antitrust Issues

The reporting requirements are an integral part of a tariff, with Federal Energy Regulatory Commission's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates.

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Transportation Law > Carrier Duties & Liabilities > Damages

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > Restraints of Trade

## [HN16](#) [blue document icon] Common Carrier Duties & Liabilities, Rates & Tariffs

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the United States Supreme Court has stated that injury implies violation of a legal right. The Supreme Court concluded that the legal rights of a shipper as against a carrier in respect to a rate are measured by the published tariff. A rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Antitrust Act. What rates are legal is determined by the Act to Regulate Commerce. Under § 8 of the latter act, the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation.

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers](#)

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Energy & Utilities Law > Antitrust Issues > General Overview](#)

[Energy & Utilities Law > Utility Companies > General Overview](#)

[Energy & Utilities Law > Utility Companies > Liability](#)

## [HN17](#) [blue document icon] US Federal Energy Regulatory Commission, Authorities & Powers

When Congress has established an exclusive form of regulation, there can be no divided authority over interstate commerce. Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged.

[Contracts Law > Remedies > Equitable Relief > Injunctions](#)

[Energy & Utilities Law > Administrative Proceedings > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Energy & Utilities Law > Antitrust Issues > General Overview](#)

[Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine](#)

[Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview](#)

[Energy & Utilities Law > Oil, Gas & Mineral Interests > Purchase Contracts > Remedies for Breach](#)

## [HN18](#) [blue document icon] Equitable Relief, Injunctions

Remedies for breach and non-performance of operating agreements approved by the Federal Energy Regulatory Commission (FERC) in the interstate wholesale electricity market fall within the exclusive domain of FERC.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Ratemaking Procedures

## **HN19** Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

The filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that: (1) legislatively appointed regulatory bodies have institutional competence to address rate-making issues; (2) courts lack the competence to set utility rates; and (3) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime.

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People of the State of California: Steven H. Felderstein, Esq., Paul J. Pascuzzi, Esq., Christa K. McKimmy, Esq., FELDERSTEIN FITZGERALD WILLOUGHBY & PASCUZZI LLP, Sacramento, CA.

**Judges:** ARTHUR J. GONZALEZ, United States Bankruptcy Judge.

**Opinion by:** ARTHUR J. GONZALEZ

## **Opinion**

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### **[\*527] MEMORANDUM OPINION SUSTAINING DEBTORS' OBJECTION TO PROOFS OF CLAIM NOS. 12172-12174 AND 12252-12257 FILED BY BILL LOCKYER, ATTORNEY GENERAL OF THE STATE OF CALIFORNIA**

ARTHUR J. GONZALEZ, United States Bankruptcy Judge.

The Attorney General of the State of California (the "State") filed separate **[\*528]** proofs of claim in unliquidated amounts on behalf of the People of the State of California (the "People") against Enron Corporation ("Enron Corp.") and certain of its affiliated entities, (collectively, the "Debtors") in the following nine cases: Enron (Claim No. 12173); ENA **[\*\*2]** (Claim No. 12172); EPMI (Claim No. 12174); EESI (Claim No. 12255); Enron Energy Services, LLC (Claim No. 12254); Enron Energy Services Operations, Inc. (Claim No. 12257); Enron Energy Marketing Corp. (Claim No. 12256); and Enron Capital & Trade Resources International Corp. (Claim No. 12253) (collectively, the "Claims"). The Claims are based upon allegation that the Debtors improperly and illegally manipulated energy markets in California, overcharged for energy, and violated state and federal laws and regulations.

The issues before the Court are whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine. The Court finds that because the Federal Energy Regulatory Commission ("FERC") has exclusive jurisdiction over interstate sales of wholesale electricity, the state laws sought to be enforced by the State in the prosecution of the Claims are preempted by the FPA. Further, the filed rate doctrine precludes consideration of such Claims.

## **I. FACTUAL AND PROCEDURAL HISTORY**

## A. The Debtors

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under [\*\*3] chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the "Plan") in these cases. The Plan became effective on November 17, 2004.

## B. The Claims

This litigation arises out of the California energy crisis of 2000-01. Prior to the crisis, the California legislature had passed Assembly Bill 1890 <sup>1</sup> to create two non-governmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. [California v. Dynegy, Inc., 375 F.3d 831, 850 \(9th Cir. 2004\)](#). The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. Since August 2, 2000, FERC has commenced refund, partnership and gaming proceedings [\*\*4] to investigate certain of the Debtors. FERC found that they engaged in gaming <sup>2</sup> in the form of inappropriate trading strategies and engaged in the deliberate submission of false information or the deliberate omission of material information. [Enron Power Mktg., Inc., et al., 106 FERC P 61,024 \(2004\)](#). Both proceedings [\*529] are ongoing, including the determination of remedies by FERC.

On October 11, 2002, the State filed the Claims on behalf of the People, alleging that the Debtors have improperly and illegally manipulated energy markets in California, overcharged for energy, [\*\*5] and violated state and federal laws and regulations during the west coast power crisis of 2000 and 2001. The State maintains that the Debtors' alleged conduct in the electricity market constitutes a violation of state antitrust law, specifically, the Cartwright Act,<sup>3</sup> the Unfair Competition Law,<sup>4</sup> and the California Commodity Law.<sup>5</sup> As a result of the Debtors' misconduct, as set forth in the Claims, the State seeks disgorgement, restitution, damages, civil and criminal penalties, and other relief, in an undetermined and unliquidated amount.

[\*\*6] On March 4, 2005, the Debtors filed an objection to the Claims filed by the State, seeking to disallow the state claims on the ground that the FPA preempts state law and the filed rate doctrine precludes consideration of these claims.

On April 11, 2005, the State filed its response to the Debtors' objection, requesting the Court hold in abeyance the Debtors' objection to the Claims because FERC has not resolved and concluded many issues raised by the Debtors' objections in its refund, partnership and gaming proceedings. The State contends that it is authorized

<sup>1</sup> 1996 Cal. Stat. 854

<sup>2</sup> The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule . . . to the detriment of the efficiency of, and of consumers in, the ISO markets." [Am. Electric Power Service Corp., et al., 103 FERC P 61,346 \(2003\)](#).

<sup>3</sup> [HN1](#) The Cartwright Acts prohibits agreements "to limit or reduce the production, or increase the price of merchandise or of any commodity." [CAL. BUS. & PROF. CODE § 16720\(b\)](#).

<sup>4</sup> [HN2](#) The Unfair Competition Law prohibits unlawful, unfair, or fraudulent business acts and practices. [CAL. BUS. & PROF. CODE § 17200](#).

<sup>5</sup> [HN3](#) The California Commodity Law prohibits fraudulent acts or conduct in connection with the purchase or sale of a commodity. [CAL. CORP. CODE §§ 29536-37](#).

under state law<sup>6</sup> to act as the representative of the People in bringing such actions. The State argues that it does not intend to infringe on FERC's jurisdiction. Instead, the State maintains that it seeks the enforcement of state law, a determination of the Debtors' liability under that law, and whatever relief may be afforded under those statutes.

[\*\*7] A hearing on this matter was held before the Court on May 18, 2005 (the "Hearing"). At the Hearing, the State argued that the Court would not have to determine a rate. Rather, it contends that the Court can determine liability, and thereafter, can refer the matter to FERC for a determination of remedies.

## II. The Parties' Contentions

The Debtors argue that the state law claims in the electricity market are preempted by the FPA because through the FPA, Congress vested in FERC exclusive jurisdiction over the transmission and sale of wholesale electric energy and *a fortiori*, over whether market participants' conduct violates FERC approved tariffs. Further, the Debtors argue that the filed rate doctrine precludes the state law claims because under the doctrine, once FERC determines that a rate is "just and reasonable," neither the states nor courts can modify that rate. Moreover, the Debtors contend that the state law claims still require the Court to either determine a nonmanipulated rate or to adjudicate whether a tariff was violated.

The State counters that the FPA does not occupy the field completely. In supporting its assertion, the State cites to [\[\\*530\] California v. Federal Power Commission, 369 U.S. 482, 8 L. Ed. 2d 54, 82 S. Ct. 901 \(1962\)](#), [\*\*8] [Otter Tail Power Co. v. United States, 410 U.S. 366, 35 L. Ed. 2d 359, 93 S. Ct. 1022 \(1973\)](#), and [Public Util. Dist. No 1 v. IDACORP Inc., 379 F.3d 641 \(9th Cir. 2004\)](#) to contend that the FPA does not preclude operation of other laws, or judicial adjudication of certain issues relating to wholesale energy markets regulated by FERC. Accordingly, the State maintains that the Court may decide whether the Debtors' various fraudulent gaming and market manipulation activities violate the Unfair Competition Law, the California Commodity Law, and the Cartwright Act.

Additionally, the State challenges the Debtors' assertion that it is impossible for the Court to avoid the determination of a nonmanipulated rate or the adjudication of whether a tariff was violated, if the state law claims are allowed to proceed before the Court. The State maintains that the state law claims here are unrelated to the ISO tariff. Thus, the State argues that the Court would not have to determine a nonmanipulated rate because FERC has done so. The State further seeks to hold the Debtors accountable for violations of state anti-fraud and consumer protection laws resulting from employing fraudulent and deceptive schemes. The [\*\*9] State requests the Court to determine liability and then subsequently remand to FERC for a determination of remedies. According to the State, because the filed rates are not at issue before this Court, the filed rate doctrine should not preclude the state law claims. In addition, the State reasons that the filed rate doctrine applies only if rates are properly filed.

## III. DISCUSSION

### A. Legal Standard of Preemption

[HN5](#) [↑] "Federal preemption of state law is rooted in the [Supremacy Clause, Article VI, clause 2, of the United States Constitution](#)." *Transmission Agency of N. Cal. v. Sierra Pac. Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests an intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. [Metropolitan Life Ins. Co. v. Taylor, 481 U.S. 58, 63-64, 95 L. Ed. 2d 55, 107 S. Ct. 1542 \(1987\)](#). Federal courts have rarely identified legislation which has been found to completely preempt state jurisdiction. [Caterpillar, Inc. v. Williams, 482 U.S. 386, 96 L. Ed. 2d 318, 107 S. Ct. 2425 \(1987\)](#).

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<sup>6</sup> [HN4](#) [↑] Pursuant to [CAL. BUS. & PROF. CODE § 17204](#); [CAL. GOVT. CODE § 12658](#); [CAL. BUS. & PROF. CODE §§ 16750\(c\), 16754, 16760](#), the State can prosecute violations of these state laws on behalf of the People.

Here, neither party raises the argument that complete preemption is applicable, nor is there any evidence in the [\*\*10] record that would support the conclusion that Congress intended for complete preemption to apply in this case. [HN6](#)[<sup>↑</sup>] In the absence of an express preemption by Congress, state law is preempted (1) "when Congress intends that federal law occupy a given field." *Silkwood v. Kerr-McGee Corp.*, 464 U.S. 238, 248, 78 L. Ed. 2d 443, 104 S. Ct. 615 (1984) ("Field Preemption"), and (2) "to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* ("Conflict Preemption").

## B. Preemption

### 1) Field Preemption

The Debtors, in support of their position that the state law claims should be barred by FERC's exclusive jurisdiction, cite to *Grays Harbor*, *Dynegy*, and *Snohomish*. These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The state law claims in the instant [\*531] case, alleging violations of state antitrust and unfair competition law, are nearly identical to those involved in the cited cases, and for the reasons set forth in those cases, [\*\*11] field preemption is applicable here.

The *Dynegy* court ruled that [HN7](#)[<sup>↑</sup>] "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." [375 F.3d at 852](#).

The Court finds that the statute's framework under the FPA supports the conclusion in *Dynegy* that FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states. . . . Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states." Federal Power Act, [16 U.S.C. § 824-824m](#).

The State does not dispute that the transactions [\*\*12] at issue involved wholesale interstate sales. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute should be characterized as either retail sales of electricity or wholesale intrastate sales. [HN8](#)[<sup>↑</sup>] The statute provides that upon a determination by FERC that "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, *the Commission shall determine* the just and reasonable rate, charge, classification, rule, regulation, *practice, or contract* to be thereafter observed and in force, and shall fix the same by order." Federal Power Act, [16 U.S.C. § 824e](#) (emphasis added).

Moreover, pursuant to the statute, [HN9](#)[<sup>↑</sup>] FERC possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, [\*\*13] and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. *Federal Power Act*, §§ 205, 206(a), as amended, [16 U.S.C.A. §§ 824d, 824e\(a\)](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.A. § 7173\(c\)](#).

In addition, after the deregulation of California energy markets, the central transactions, the wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC jurisdictional ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded that "FERC is doing enough regulation to justify federal preemption of state laws under the market-based system of setting wholesale electricity rates." [Snohomish](#), 384 F.3d 756, 760-61. For instance,

(1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and the ISO. FERC approved [\*532] the market-based tariffs only upon a showing that the seller [\*14] lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under FPA § 205(c), [16 U.S.C. § 824d\(c\)](#). (3) FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, "each participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market." *Id.*

The Court also recognizes that [HN10](#)<sup>7</sup> "entities that transact through the ISO or [the] PX and engage in improper practices" are in violation of filed tariffs. . . . FERC and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement." [103 FERC P 61,346](#).

[\*\*15] The State does not contest FERC's jurisdiction in the electricity market. Rather, the State argues that field preemption is not applicable because courts have referred the state law claims related to filed tariffs to regulatory commissions. In supporting its assertion, the State cites the Supreme Court's decisions in [Otter Tail Power](#) and [California v. Federal Power Comm'n](#). In both cases, the Supreme Court found that Congress does not intend to bar the government from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions.

Having reviewed these cases, the Court disagrees with the State's argument and finds that two important differences exist. First, both cases discussed issues of the interaction between federal administrative law and federal **antitrust law**; thereby no state law preemption issue was presented in these cases. In *California v. Federal Power Commission*, a gas company filed a motion to dismiss the antitrust suit pursuant to the Clayton Act, § 7 as amended [15 U.S.C.A. § 18](#), or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's [\*16] assets pursuant to the Natural Gas Act (the "NGA"), § 7(c) as amended [15 U.S.C.A. § 717f\(c\)](#), before the Power Energy Commission. [369 U.S. at 483](#). In *Otter Tail Power*, the government brought an action against an electric power company to enjoin violations of the Sherman Act, [15 U.S.C.A. § 2](#). [410 U.S. at 368](#). In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws. The Court will not address whether Congress has left room for enforcement of state antitrust laws because the State does not argue that state **antitrust law** and federal **antitrust law** would be impacted the same way. Further, the Court notes that the Ninth Circuit in *Snohomish* and *Dynegy* did not discuss the issue of the similarity between California **antitrust law** and Sherman Act. In *Snohomish*, consumer utility in Washington sued generators and traders of wholesale electricity, for violations of California state antitrust and consumer protection laws. [384 F.3d 756](#). In *Dynegy*, Attorney General of the State of California brought state court actions against wholesale electricity suppliers for violations of California's unfair business practices law. [375 F.3d 831](#).

Second, and more importantly, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior [\*533] that has been entrusted to FERC. As the Court discussed above, the statute under [16 U.S.C.A. §§ 824d, 824e\(a\)](#) provides FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order" [\*17] disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund

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[HN11](#)<sup>7</sup> Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. "Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges." [103 FERC P 61,346 \(2003\)](#).

Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." [103 FERC P 61,346](#). Further, [HN12](#) [↑] "implicit in Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority." [106 FERC P 61,024](#).

In contrast, the court in *California v. Federal Power Commission* concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the Clayton Act. [369 U.S. at 485](#). "The Commission's standard, set forth in [§ 7 of the NGA](#), will serve the public convenience and necessity.' If existing natural gas companies violate the antitrust laws, the Commission is directed by [§ 20\(a\)](#) to transmit such evidence' to the Attorney [\*\*18] General." [Id. at 486](#). Similarly, the Court in *Otter Tail Power* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the Sherman Act. [410 U.S. at 375](#). Moreover, the Supreme Court in *Carnation Co. v. Pacific Westbound Conference*, [383 U.S. 213, 383 U.S. 932, 15 L. Ed. 2d 709, 86 S. Ct. 781 \(1966\)](#) declined to grant antitrust immunity to a shipping company because "the provisions of the Shipping Act, 46 U.S.C.A. § 801, can not reasonably be construed as an implied repeal of antitrust regulation of the shipping industry's rate-making activities." [Id. at 217](#). The Shipping Act does not give the Federal Maritime Commission (the "FMC") any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. [Square D Co. v. Niagara Frontier Tariff Bureau, 476 U.S. 409, 422, 90 L. Ed. 2d 413, 106 S. Ct. 1922 \(1986\)](#).

The State further argues that the state law claims related to wholesale energy have been allowed by courts in *Grays Harbor* and [Gulf States Utils. Co. v. Alabama Power Co., 824 F.2d 1465 \(5th Cir. 1987\)](#). The courts in both cases [\*\*19] concluded that the state claims concerning contractual disputes were not within the scope of FERC's jurisdiction. The viability of the State's comparison depends on the substantial similarity of facts between the case before the Court and those two cited cases. The Court finds that the facts here are distinguishable. First, the state law claims in the cited cases were related to contractual issues, which exclusively fall within a state's jurisdiction. The court in *Grays Harbor* granted the utility leave to amend its complaint to seek declaratory relief only as to issues of contract formation. [379 F.3d. at 652-53](#). Similarly, the court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. [824 F.2d at 1474](#). Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily intrude upon the [\*534] rate-setting jurisdiction of FERC. [Grays Harbor, 379 F.3d. at 653](#). Therefore, field preemption bars the State from pursuing its state law claims before [\*\*20] the Court.

## 2) Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court disagrees with the State that the FPA only provides FERC with authority to determine the "just and reasonable" rates for wholesale power. Instead, FERC has broad authority concerning anti-competitive activities related to the filed rate. Accordingly, conflict preemption also bars the State from pursuing its state law claims before the Court.

## C. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. [HN13](#) [↑] The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. *E. & J. Gallo Winery v. Encana Energy Servs., Inc.*, Case No.CV F 03-5412 AWILJO. at 15. The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates [\*\*21] for its service other than those properly filed with the appropriate federal regulatory authority." [Ark. L.A. Gas Co. v. Frank Hall, 453 U.S. 571, 577-78, 69 L. Ed. 2d 856, 101 S. Ct. 2925 \(1981\)](#). The Court also

acknowledges that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant." [\*Cleveland v. Federal Power Comm'n, 174 U.S. App. D.C. 1, 525 F.2d 845, 854 \(D.C. Cir. 1976\).\*](#)

The first argument made by the State is that the filed rate doctrine is inapplicable because no properly filed rates were on file during the period when the alleged conduct occurred. However, the State relied on the following finding in [\*California v. FERC, 383 F.3d 1006, 1016 \(9th Cir. 2004\)\*](#) to support its position "without the required filings, neither FERC nor any affected party may challenge the rate. Pragmatically, under such circumstances, there is no filed tariff in place at all." *Id.* This argument, however, inappropriately equates the Debtors' alleged violation of the filing requirements with no-filed tariffs. FERC required each seller to file [\*\*22] quarterly reports pursuant to FPA § 205(c) [16 U.S.C. § 824d\(c\)](#) on transaction-specific information about its sales and purchases at market-based rates. The court in *Grays Harbor* concluded [HN14](#) "while market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine." [379 F.3d at 651](#).

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that [HN15](#) "the reporting requirements are an integral part of a tariff, with FERC's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [383 F.3d at 1016](#). On August 13, 2002, FERC's Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.<sup>8</sup> Then, [\*535] FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales [\*\*23] at market-based rates. [106 FERC P 61,024](#). As noted by FERC,

implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market shares) that reflect a departure from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized [\*\*24] the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by [FERC. 383 F.3d at 1016](#). Without the availability of retroactive refunds, "parties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

The second argument made by the State is that the filed rate doctrine is not applicable because the issue presented before the Court is distinguishable from those in *Grays Harbor* and *Snohomish*. The plaintiff in *Snohomish* brought an action against a company that engaged in market manipulation during the energy crisis in violation of state antitrust and unfair competition law. The court confirmed that the filed rate doctrine applies because the court could not determine the rates that "would have been achieved in a competitive market." [384 F.3d at 761](#). Similarly, the court in *Grays Harbor* rejected the request from the plaintiff for [\*\*25] a determination of the "fair price." [379 F.3d at 645](#). Here, the State argues that it is not asserting a price which should be paid in a competitive market as the benchmark for a calculation of a remedy. Rather, the State maintains that the remedy would be unrelated to the ISO tariff and the Court would not have to determine a non-manipulated rate because FERC has done so. The State

<sup>8</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, as required under their market-based rate authorization. [106 FERC P 61,024](#).

argues that it is merely requesting the Court to determine liability, and thereafter, remand to FERC for a determination of remedies.

The Ninth Circuit in *California v. FERC* examined the substance of the law and remanded to FERC for the determination of remedies. The court there declined to order refunds to a state because the court reasoned it was more appropriate for FERC to consider its remedial options in the first instance. [383 F.3d at 1018](#). The substantive law examined by the court in *California v. FERC* concerned whether retroactive refunds were legally available. *Id.* As such, no liability issue was raised and determined by that court. However, the Court finds that determining the liability or the legal right of the State against the Debtors for violation of the [\[\\*\\*26\]](#) antitrust laws would have to be measured by the tariff. Therefore, the filed rate doctrine would be applicable.

[\[\\*536\] \*\*HN16\*\*\[!\[\]\(7196df618003dfe69225b54d4938115c\_img.jpg\)](#)

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in [Keogh v. Chicago & N.W.R. Y. Co., 260 U.S. 156, 67 L.Ed. 183, 43 S.Ct. 47 \(1922\)](#), stated that "injury implies violation of a legal right." [Id. at 163](#). The Supreme Court concluded that "the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff." [Id. at 163](#). Justice Brandeis explained "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the [Anti-Trust Act](#). What rates are legal is determined by the Act to Regulate Commerce. Under Section 8 of the latter act . . . the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation." [Id. at 162](#). Thus, the finding of liability in antitrust laws would be integral to the Court's determination of whether the Debtors [\[\\*\\*27\]](#) are liable due to their violations of state [antitrust law](#) and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. "In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company." [453 U.S. at 579](#). The Supreme Court rejected this argument by reasoning that "the mere fact that respondents brought this suit under state law would not rescue it, for [HN17](#)[ when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce. . . . Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged." [Id. at 580-84](#).

Moreover, to award monetary relief, [\[\\*\\*28\]](#) the Court would have to determine a "fair price." Thus, the filed rate doctrine bars the Court from awarding monetary damages sought by the State. Nonetheless, the Court finds that injunctive relief would also be unavailable to the State. The Court agrees with the Ninth Circuit's decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. [384 F.3d at 762](#). [HN18](#)[ "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC." [Dynegy, 375 F.3d at 836](#).

The decisions from the Second Circuit in [Sun City Taxpayers' Association v. Citizens Utilities Co., 45 F.3d 58 \(2d Cir. 1995\)](#) and [Wegoland Ltd. v. NYNEX Corp., 27 F.3d 17 \(2d Cir. 1994\)](#), provide an additional basis for dismissal of the Claims sought by the State. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In determining whether [\[\\*\\*29\]](#) the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. [Sun City Taxpayers' Ass'n v. Citizens Utils. Co., 847 F.Supp.281, 291 \(D. Conn. 1994\)](#). The Second Circuit in *Wegoland* recognized that [HN19](#)[ the filed rate doctrine exists [\[\\*537\]](#) for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. [27 F.3d at 21](#).

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects the State's challenge to the application of the filed rate doctrine. Accordingly, the **[\*\*30]** filed rate doctrine bars the relief sought by the State.

#### **V. Conclusion**

For the foregoing reasons, the Court concludes that the state electricity market manipulation claims are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims filed by the State.

Counsel for the Debtors is directed to settle an order consistent with this Court's Memorandum Opinion.

Dated: New York, New York

June 14, 2005

Arthur J. Gonzalez

UNITED STATES BANKRUPTCY JUDGE

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## **Stand Energy Corp. v. Columbia Gas Transmission Corp.**

United States District Court for the Southern District of West Virginia, Charleston Division

June 14, 2005, Filed; June 14, 2005, Entered

CIVIL ACTION NO. 2:04-0867, consolidated with civil action nos: 2:04-0868; 2:04-0869; 2:04-0870; 2:04-0871; 2:04-0872; 2:04-0873; 2:04-0874

### **Reporter**

373 F. Supp. 2d 631 \*; 2005 U.S. Dist. LEXIS 11776 \*\*; 2005-1 Trade Cas. (CCH) P74,859; 166 Oil & Gas Rep. 147

STAND ENERGY CORPORATION, Plaintiff v. COLUMBIA GAS TRANSMISSION CORPORATION, et al., Defendants.

**Subsequent History:** [\[\\*\\*1\]](#) As Amended September 15, 2005.

Motion granted by, Dismissed by, in part [Stand Energy Corp. v. Columbia Gas Transmission Corp., 2005 U.S. Dist. LEXIS 20865 \(S.D. W. Va., July 5, 2005\)](#)

**Prior History:** Case 2:04-cv-00867.

[Stand Energy Corp. v. Columbia Gas Transmission Corp., 2005 U.S. Dist. LEXIS 64477 \(S.D. W. Va., Jan. 6, 2005\)](#)

## **Core Terms**

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rates, Shippers, tariff, Select, Pipeline, anti trust law, natural gas, damages, filed rate doctrine, motion to dismiss, transportation, preempted, regulated, output, violations, Energy, field preemption, antitrust claim, antitrust, failure to state a claim, preemption, prices, cases, plaintiff's claim, fair dealing, good faith, preferential, customers, independent cause of action, pipeline system

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

### [HN1](#) Motions to Dismiss, Failure to State Claim

Under [Fed. R. Civ. P. 12\(b\)\(6\)](#), a defending party may move to dismiss if the pleading party has failed to state a claim for which relief may be granted. A [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion tests the sufficiency of the pleading. It does not resolve factual disputes, the merits of a claim, or the applicability of defenses.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

### [HN2](#) Motions to Dismiss, Failure to State Claim

373 F. Supp. 2d 631, \*631L<sup>A</sup>2005 U.S. Dist. LEXIS 11776, \*\*1

In considering a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss, the claims must be viewed in the light most favorable to the non-moving party and all allegations accepted as true. Dismissal is appropriate only when it appears beyond a doubt that no set of facts would entitle the pleader to relief.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### [HN3](#) [] Motions to Dismiss, Failure to State Claim

The [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss for failure to state a claim is viewed with disfavor and rarely granted.

Energy & Utilities Law > Natural Gas Industry > Distribution & Sale

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Common Carriers

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Natural Gas Industry > General Overview

Energy & Utilities Law > Natural Gas Industry > Exports & Imports

Energy & Utilities Law > Natural Gas Industry > Marketing & Transportation > General Overview

Energy & Utilities Law > Natural Gas Industry > Natural Gas Act > General Overview

Energy & Utilities Law > Pipelines & Transportation > Natural Gas Transportation

Transportation Law > Interstate Commerce > Federal Powers

### [HN4](#) [] Natural Gas Industry, Distribution & Sale

Under [§ 717b](#) of the Natural Gas Act, transporters and sellers of natural gas in interstate commerce are regulated by the Federal Energy Regulatory Commission. [15 U.S.C.S. § 717b](#). They must file their rates with the Commission and may charge only such rates as found by the Commission to be "just and reasonable." [15 U.S.C.S. § 717c\(a\)](#). They may not grant any "undue preference or advantage," and they must file any change in their rates or services with the Commission in advance. [15 U.S.C.S. §§ 717c\(b\)](#) and [717c\(d\)](#). The Commission retains broad regulatory authority to determine the reasonableness of any rates or services. At its core, the filed rate doctrine recognizes the authority extended to the Commission, and not the courts, to determine the reasonableness of the rates stated in the filing. The doctrine achieves two goals - restricting the regulated entity to charging only the approved rates and preserving the regulatory agency's authority to determine those rates.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Energy & Utilities Law > Natural Gas Industry > Natural Gas Act > Certificates of Need

#### **HN5** [down] Exemptions & Immunities, Filed Rate Doctrine

The filed rate doctrine applies to more than just rates; it extends to the services, classifications, charges, and practices included in the rate filing. [15 U.S.C.S. § 717c\(c\)](#). Similar statutory provisions have been found to support applying the doctrine to services that may not literally involve rates or rate-setting. Rates, however, do not exist in isolation. They have meaning only when one knows the services to which they are attached. Any claim for excessive rates can be couched as a claim for inadequate services and vice versa. In addition to barring suits challenging filed rates and suits seeking to enforce rates that differ from the filed rates, the filed-rate doctrine also bars suits challenging services, billing, or other practices when such challenges, if successful, would have the effect of changing the filed tariff.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

#### **HN6** [down] Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

A claim for compensatory damages may implicate the filed rate doctrine where it has the effect of challenging the filed rate. Even though the complaint may not explicitly challenge the filed rate, the court must consider whether the damages sought would effectively provide plaintiffs with a different rate than the one contained in the tariff. Courts therefore cannot permit any claim to go forward that, if successful, would require an award of damages that would have the effect of imposing different rates upon different consumers. Similarly, authorizing a court to award damages that would effectively impose a rate different from that dictated by the tariff would usurp the Federal Communications Commission's authority to determine what rate is reasonable.

Communications Law > Federal Acts > Federal Communications Act > Tariffs

Energy & Utilities Law > Natural Gas Industry > Natural Gas Act > General Overview

Transportation Law > Carrier Duties & Liabilities > Tariff Interpretation

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

#### **HN7** [down] Federal Communications Act, Tariffs

The filed-rate doctrine precludes courts from deciding whether a tariff is reasonable, reserving the evaluation of tariffs to the Federal Communications Commission, but it does not preclude courts from interpreting the provisions of a tariff and enforcing that tariff. If the filed-rate doctrine were to bar a court from interpreting and enforcing the provisions of a tariff, that doctrine would render meaningless the provisions of the Federal Communication Act allowing plaintiffs redress in federal court. The Natural Gas Act contains a similar provision allowing suits in federal court. [15 U.S.C.S. § 717u](#).

Constitutional Law > Supremacy Clause > General Overview

373 F. Supp. 2d 631, \*631L<sup>2005 U.S. Dist. LEXIS 11776, \*\*1</sup>

Energy & Utilities Law > Natural Gas Industry > Natural Gas Act > General Overview

Energy & Utilities Law > Administrative Proceedings > General Overview

Energy & Utilities Law > Administrative Proceedings > Preemption

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Natural Gas Industry > General Overview

Energy & Utilities Law > Natural Gas Industry > Distribution & Sale

Energy & Utilities Law > Natural Gas Industry > Marketing & Transportation > General Overview

Energy & Utilities Law > Pipelines & Transportation > Natural Gas Transportation

Energy & Utilities Law > Utility Companies > General Overview

Energy & Utilities Law > Utility Companies > Buying & Selling of Power

Energy & Utilities Law > Utility Companies > Rates > General Overview

#### **HN8** [blue icon] Constitutional Law, Supremacy Clause

Every state statute that has some indirect effect on rates and facilities of natural gas companies is not preempted. In determining whether the effect of a state claim results in preemption, the United States Supreme Court has articulated the following test: When a state regulation affects the ability of the Federal Energy Regulatory Commission to regulate comprehensively the transportation and sale of natural gas, and to achieve the uniformity of regulation which was an objective of the Natural Gas Act, [15 U.S.C.S. § 717](#), or presents the prospect of interference with the federal regulatory power, then the state law may be preempted even though collision between the state and federal regulation may not be an inevitable consequence.

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Mergers & Acquisitions Law > Antitrust > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

#### **HN9** [blue icon] Regulated Industries, Energy & Utilities

Immunity from the antitrust laws is not lightly implied.

Antitrust & Trade Law > Exemptions & Immunities > General Overview

#### **HN10** [blue icon] Antitrust & Trade Law, Exemptions & Immunities

The existence of a regulatory structure designed to deter and remedy anticompetitive harm significantly reduces the need to apply traditional antitrust principles.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## **HN11** [blue icon] Motions to Dismiss, Failure to State Claim

In ruling on a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss, the court must ascertain whether the complaint covers all of the elements that comprise the theory for relief.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **HN12** [blue icon] Private Actions, Standing

Injury to competition, is an essential element of every antitrust claim. An antitrust claim must assert that a defendant's conduct constitutes an unreasonable restraint of trade, not merely an economic injury to the plaintiff.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

## **HN13** [blue icon] Regulated Practices, Price Fixing & Restraints of Trade

Competitors are not injured by mere price fixing whether the conspiracy sets maximum or minimum prices. To this end, price-fixing agreements are illegal but do not cause injury to competitors.

**Counsel:** For Stand Energy Corporation, PLAINTIFF CLASS: Natural Gas Marketing Customers Of Columbia Gas Transmission Corporation ("TCO") That Were Damaged By An Illegal Gas Scheme Perpetrated By Defendants, Plaintiff: Joshua I. Barrett, Lonnie C. Simmons, Molly McGinley Han, Rudolph L. DiTrapano, DITRAPANO BARRETT & DIPIERO, Charleston, WV.; Robert C. Sanders, LAW OFFICE OF ROBERT C. SANDERS, Upper Marlboro, MD.

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For Cove Point LNG Limited Partnership, Williams Cove Point LNG Company, LLC, Dominion Resources, Inc., The Wholesale Power Group, Virginia Electric and Power Company, Defendants: Bryan A. Fratkin, Howard Feller, J. Brent Justus, MCGUIRE WOODS, Richmond, VA.; Jeffrey M. Wakefield, FLAHERTY SENSABAUGH & BONASSO, Charleston, WV.

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For Dominion Cove Point LNG LP, Dominion Cove Point LNG Company, LLC, DEFENDANT CLASS A: Three Federally Regulated Interstate Natural Gas Pipeline Companies (Columbia Gas Transmission Corporation, Columbia Gulf Transmission Company, And The Cove Point LNG Limited Partnership) That Participated In An

373 F. Supp. 2d 631, \*631L 2005 U.S. Dist. LEXIS 11776, \*\*2

Illegal Scheme, etc., Defendants: Bryan A. Fratkin, Howard Feller, J. Brent Justus, MCGUIRE WOODS, Richmond, VA.; Jeffrey M. [\*\*3] Wakefield, Erica M. Baumgras, FLAHERTY SENSABAUGH & BONASSO, Charleston, WV.

For Base Petroleum, Inc., Defendant: Johnny M. Knisely, II, Thomas R. Goodwin, GOODWIN & GOODWIN, Charleston, WV.

For Howard Energy Company, Inc., Defendant: Brian McAleenan, Ruchi Verma, Thomas K. Cauley, SIDLEY AUSTIN BROWN & WOOD, Chicago, IL.; Mark A. Glover, Stephen B. Farmer, FARMER CLINE & ARNOLD, Charleston, WV.

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For Semco Pipeline Company, Semco Energy Services, Inc., Defendants: Avery Gardiner, James W. Draughn, Jr., Michael S. Becker, Thomas M. McDermott, KIRKLAND & ELLIS, Washington, DC.; John H. Tinney, THE TINNEY LAW FIRM, Charleston, WV.

For El Paso Merchant Energy, L.P., Defendant: David K. Hendrickson, HENDRICKSON & LONG, Charleston, WV.; John L. Shoemaker, Murray J. Fogler, Paul J. Franzetti, MCDADE FOGLER MAINES, Houston, TX.

**Judges:** ROBERT C. CHAMBERS, UNITED STATES DISTRICT JUDGE.

**Opinion by:** ROBERT C. CHAMBERS

## Opinion

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### [\*633] AMENDED [\*\*4] MEMORANDUM OPINION AND ORDER

The Court entered an Order on June 14, 2005, on Defendants' Joint Motion to Dismiss. In that Order, for the reasons stated, the Court **DENIED** the motions to dismiss for failure to state a claim based on the filed rate doctrine and preemption, and **GRANTED IN PART** and **DENIED IN PART** the motion to dismiss based on failure to state a claim under antitrust law and common law claims. Following the entry of that Order, Defendants moved for the Court to amend the Order to certify the issues of filed rate doctrine and preemption for interlocutory appeal. For reasons stated in the concluding paragraph below, the Court **GRANTS** Defendants' motion [Docket No. 378] and amends this Order for the sole purpose of certifying the above issues for interlocutory appeal. The remainder of the Order remains unchanged.

#### I.

#### Standard of Review

**HN1** [↑] Under Rule 12(b)(6) of the Federal Rules of Civil Procedure, a defending party may move to dismiss if the pleading party has failed to state a claim for which relief may be granted. A Rule 12(b)(6) motion tests the sufficiency of the pleading. It does not resolve factual disputes, the merits of a claim, [\*\*5] or the applicability of defenses. Republican Party of North Carolina v. Martin, 980 F.2d 943, 952 (4th Cir. 1992). **HN2** [↑] In considering the motion, the claims must be viewed in the light most favorable to the non-moving party and all allegations accepted as true. *Id.* Dismissal is appropriate only when it appears beyond a doubt that no set of facts would entitle the pleader to relief. Conley v. Gibson, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957). **HN3** [↑] The motion to dismiss for failure to state a claim is viewed with disfavor and rarely granted. See Rogers v. Jefferson-Pilot Life Ins. Co., 883 F.2d 324, 325 (4th Cir. 1989) (reaffirmed in Mylan Laboratories, Inc. v. Matkari, 7 F.3d 1130, 1134 n.4

(*4th Cir. 1993*). See generally 5A Charles A. Wright & Arthur R. Miller, *Federal Practice & Procedure* §§ 1356 and 1357 (1990 and 1998 Supplement).

## II.

### Factual Allegations and Procedural Background

Plaintiffs are eight shippers, wholesalers, and marketers of natural gas who transported and stored gas on the interstate pipeline systems owned by Columbia Gas Transmission Corporation, Columbia Gulf [\*\*6] Transmission Company and Dominion Cove Point LNG, LP (Pipeline Defendants). Defendants fall into one of two groups. One group of defendants is the Pipeline Defendants who own pipelines used in the transportation and storage of natural gas. The other defendants are eight natural gas shippers (Select Shippers) whom Plaintiffs contend were given preferential treatment by the Pipeline Defendants.

Plaintiffs allege that the Pipeline Defendants granted preferential access to storage capacity and transportation on the interstate pipeline system to the Select Shippers in exchange for "kickback" payments. Specifically, Plaintiffs allege that the Pipeline Defendants allowed the Select Shippers to store gas on the pipeline system during the warmer months for resale during the colder months. This allowed [\*634] the Select Shippers to maintain a "positive imbalance" on the pipeline system. Along the same line, it is alleged that the Select Shippers were able to "borrow" gas off the pipeline system during the colder months for resale at a high price and replace the borrowed gas during the warmer months at a decreased price. Additionally, Plaintiffs contend that the Select Shippers were also [\*\*7] given preferential transportation services. Plaintiffs argue that the scheme allowed Defendants to monopolize the market and resulted in "diminished revenues from sales to existing end-user customers, obstruction to business expansion, loss of market share and loss of asset value" to Plaintiffs. (Pls.' Resp. to Defs.' Mot. to Dismiss at 5).

In the fall of 1998, Columbia Gas Transmission Company (TCO) filed an application with the Federal Energy Regulatory Commission (FERC or Commission), seeking approval to operate a parking and lending service (PAL). The PAL service would allow shippers to park gas on the pipeline system as well as borrow gas from the pipeline system on an interruptible basis, which means it would be subject to interruption by higher priority shipping contracts. FERC approved TCO's application. Plaintiffs allege that subsequent to FERC's approval of the PAL license, the Pipeline Defendants continued their preferential treatment of the Select Shippers. Plaintiffs contend that though the Select Shippers accessed the inexpensive PAL service, the Pipeline Defendants continued to interrupt the higher priority shipping and transportation agreements of the Plaintiffs in [\*\*8] favor of the interruptible agreements of the Select Shippers.

In February of 1999, TCO, Columbia Gulf Transmission Corp., and Columbia Energy Service Corp., voluntarily informed FERC of the gas imbalances which had occurred which Plaintiffs allege were a result of their preferential treatment of the Select Shipper Defendants prior to the 1998 PAL license. FERC instituted an investigation and in October, 2000, issued an Order approving a Stipulation and Consent Agreement with TCO, Columbia Gulf, and Columbia Energy Services. As a result of the Stipulation and Consent agreement, TCO, Columbia Gulf, and Columbia Energy Services agreed to refund the Storage in Transit (SIT) penalties and disgorgement of profits to the industry participants whom FERC found had been illegally excluded from the scheme, which included many of the plaintiffs.

Plaintiffs originally filed this action alleging violations of state antitrust laws and breach of contract arising out of the conduct of Defendants in the Circuit Court of Kanawha County, West Virginia. Defendants properly removed the action to this Court pursuant to [28 U.S.C. §§ 1441](#) and [1446](#). Plaintiffs amended their complaint, [\*\*9] after expedited discovery, to add the Select Shipper Defendants. Defendants subsequently filed the instant motion to dismiss Plaintiffs Second Amended Complaint (SAC) on numerous grounds. The Court will address each of Defendants arguments in turn.

### III.

## Analysis

### A. Filed Rate Doctrine

Defendants assert that Plaintiffs' claims are barred by the filed rate doctrine. [HN4](#) Under [§ 717b of the Natural Gas Act](#) (NGA), transporters and sellers of natural gas in interstate commerce are regulated by FERC. [15 U.S.C. § 717b](#). They must file their rates with the Commission and may charge only such rates as found by the Commission to be "just and reasonable." [15 U.S.C. § 717c\(a\)](#). They may not grant any "undue preference or advantage," [\*635] and they must file any change in their rates or services with the Commission in advance. [15 U.S.C. §§ 717c\(b\)](#) and [717c\(d\)](#). The Commission retains broad regulatory authority to determine the reasonableness of any rates or services. At its core, the filed rate doctrine recognizes the authority extended to the Commission, and not the courts, to determine the reasonableness [\*\*10] of the rates stated in the filing. [Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 577, 69 L. Ed. 2d 856, 101 S. Ct. 2925 \(1981\)](#). The doctrine achieves two goals - restricting the regulated entity to charging only the approved rates and preserving the regulatory agency's authority to determine those rates. [Id. at 577-78](#). See also [Bryan v. BellSouth Communications, Inc., 377 F.3d 424, 429 \(4th Cir. 2004\)](#) ("The doctrine's purpose is two-fold: to prevent discrimination among consumers and to preserve the rate-making authority of federal agencies"). "It would undermine the congressional scheme of uniform rate regulation to allow a state court to award as damages a rate never filed with the Commission and thus never found to be reasonable within the meaning of the Act." [Arkansas Louisiana Gas Co., 453 U.S. at 579](#).

[HN5](#) The doctrine applies to more than just rates; it extends to the services, classifications, charges, and practices included in the rate filing. See [15 U.S.C. § 717c\(c\)](#). Similar statutory provisions have been found to support applying the doctrine to services that may not literally [\*\*11] involve rates or rate-setting. [AT&T v. Central Office Telephone, Inc., 524 U.S. 214, 233, 141 L. Ed. 2d 222, 118 S. Ct. 1956 \(1998\)](#) (Stevens, J., dissenting). "Rates, however, do not exist in isolation. They have meaning only when one knows the services to which they are attached. Any claim for excessive rates can be couched as a claim for inadequate services and vice versa." [Id. at 223](#). "In addition to barring suits challenging filed rates and suits seeking to enforce rates that differ from the filed rates, the filed-rate doctrine also bars suits challenging services, billing, or other practices when such challenges, if successful, would have the effect of changing the filed tariff." [Brown, III v. MCI Worldcom Network Services, Inc., 277 F.3d 1166, 1170 \(9th Cir. 2002\)](#) (citing [AT&T v. Central Office, 524 U.S. at 223](#)).

The doctrine has been raised by Defendants as a bar to all of Plaintiffs' claims. They contend that Plaintiffs are attacking the tariff by claiming, first, that Defendants violated the tariff and its rate schedule and General Terms and Conditions, and, second, that the subsequently approved PAL [\*\*12] service as part of the tariff violates Plaintiffs' rights. The Court has examined the SAC and the relief Plaintiffs seek in each cause of action. Plaintiffs claim that they suffered diminished revenues from sales to their customers, obstruction to business expansion, loss of market share, and loss of asset value.<sup>1</sup> The suit does not directly challenge the rates contained in Defendants' tariffs but asserts that Plaintiffs have been wrongfully injured by the Pipeline Defendants and the Select Shippers' conduct, for which Plaintiffs seek compensatory damages.

[HN6](#) A claim for compensatory damages may implicate the filed rate doctrine where it has the effect of challenging the filed rate. [\*\*13] [Hill v. BellSouth Telecommunications, Inc., 364 F.3d 1308, 1315 \(11th Cir. 2004\)](#). Even though the complaint may not explicitly challenge the filed rate, the Court must consider whether the damages sought would effectively provide Plaintiffs with a different rate than the one contained in the tariff. "We

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<sup>1</sup> See SAC at PP 112, 170, 181, 206, 221, 234, 243, 251, 268, 278, 288, 299, and 309 for Counts One through Three and Five through Thirteen. Count Four, alleging unjust enrichment, seeks damages in the amount of profits earned by Defendants on sales Plaintiffs lost as a result of the alleged scheme.

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therefore cannot permit any claim to go forward that, if successful, would require an award of damages that would have the effect of imposing different rates upon different consumers.... Similarly, authorizing a court to award damages that would effectively impose a rate different from that dictated by the tariff would usurp the FCC's [Federal Communications Commission's] authority to determine what rate is reasonable." [Bryan v. BellSouth, 377 F.3d at 429-430.](#)

The distinguishing element in the cases where the doctrine has been applied is the damages sought. Where plaintiffs seek damages based on the rates, the claims have been prohibited. In [Arkansas Louisiana Gas Co. v. Hall, 453 U.S. 571, 69 L. Ed. 2d 856, 101 S. Ct. 2925 \(1981\)](#), the Supreme Court framed the issue, stating, "the question before us is whether that [\*\*14] doctrine forbids a state court to calculate damages in a breach-of-contract action based on an assumption that had a higher rate been filed, the Commission would have approved it." [Id. at 573.](#) The Court agreed with the characterization that plaintiff's damage claim was "nothing less than the award of a retroactive rate increase based on speculation about what the Commission might have done..." [Id. at 578-79.](#) Damages for the breach of contract action based on assumptions as to what rate the Commission might have approved infringed on the powers of the agency, violating the doctrine. *Id.*

The Fourth Circuit applied this rationale in *Bryan*. There, the Court approached the filed rate doctrine by first explaining its rationale - preventing discrimination and preserving agency rate-making. [Bryan, 377 F.3d at 429.](#) It noted that a damage award would effectively lower that plaintiff's rates below that of other customers or require a court to determine a rate different from the filed rate. [\[\\*\\*15\] Id. at 430.](#) Turning to the complaint before it, the Court concluded:

In our view, the Complaint--read in the light most favorable to the plaintiff--nowhere purports to seek any form of damages other than a refund of some portion of the FUSC [Federal Universal Service Charge]. And it pleads no facts that would put BellSouth on notice that Bryan intends to seek damages resulting from any injury other than paying the FUSC.

[Id. at 431.](#)

*Bryan* relied on *Hill v. BellSouth*, where the Eleventh Circuit decided a case arising in a similar context, the [Federal Communications Act](#) universal service fund charges. Finding the filed rate doctrine prohibited the state law claims, the Eleventh Circuit considered the two prongs of the doctrine: nondiscrimination and nonjusticiability, and how they applied to plaintiff's claims. [Hill, 364 F.3d at 1316.](#) The court in *Hill* found the plaintiff's claim would violate the nondiscrimination principle because a damage award for excessive charges would result in a discounted rate for the services. *Id.* Additionally, the nonjusticiability principle would be violated because the [\[\\*\\*16\]](#) court would be retroactively finding the filed rate unreasonable and ordering a new rate, an inappropriate judicial determination of the reasonableness of rates. [Id. at 1317.](#) Thus, claims seeking damages based on rates or services differing from those set in the tariff are barred by the doctrine.

The critical factor in the analysis is the nature of the damages sought by the plaintiff. With this understanding in mind, the Court comments on the cases cited by the [\[\\*637\]](#) parties to illustrate its analysis. Defendants rely on several cases which arose from the California energy crisis. In [Public Util. Dist. No. 1 v. Dynegy Power Mktg., Inc., 384 F.3d 756 \(2004\)](#), the Ninth Circuit applied the filed rate doctrine to dismiss state law claims. The consumer utility sued wholesale electricity generators and traders for market manipulation which caused the utility to pay higher rates than a competitive market would require. [Id. at 758.](#) The court reasoned that the claims would ask the district court to determine "fair price" rates. [\[\\*\\*17\] Id. at 761.](#) [Public Util. Dist. No 1 v. IDACORP Inc., 379 F.3d 641 \(9th Cir. 2004\)](#), reached a similar result, emphasizing that plaintiff's claims would depend on the district court's determination of what a fair price or rate should have been. [Id. at 648.](#) *Snohomish County* treats the antitrust claims in the same fashion that *Grays Harbor* handled contract claims. Whether antitrust, unfair practices, or breach of contract actions, the nature of the damages sought governs the application of the doctrine.

Defendants also rely on [Lockyer v. Dynegy, Inc., 375 F.3d 831 \(9th Cir. 2004\)](#), but its application of the doctrine arises in a different context. The State of California challenged the terms of the tariff by seeking to impose civil penalties, which the court declared was the province of FERC and would effect an alteration of the rates set by

FERC. *Id.* at 853. Defendants also submitted *In re W. States Wholesale Natural Gas Antitrust Litig.*, 368 F. Supp. 2d 1110, 2005 U.S. Dist. LEXIS 8906, No. MDL 1566, CVS031431PMP(PAL) (Base File) (D. Nev. Apr. 8, 2005) [\*\*18] , which applied the doctrine but only after finding "to calculate the necessary damages.... this Court would be required to make a determination as to what a just or reasonable rate would have been...." *Id.* In these cases the damages claimed by the plaintiffs implicated the filed rates and, for that reason, were precluded.

The cases cited by Plaintiffs underscore the proper application of the doctrine. In *Brown v. MCI Worldcom*, the plaintiffs brought an action in federal court alleging the defendants over-charged. [277 F.3d at 1169](#). Finding federal subject matter jurisdiction because the Federal Communications Act (FCA) permitted customers claiming violations of a filed tariff to bring an action in district court, the court then addressed the filed rate doctrine. [Id. at 1170](#). The plaintiff did not challenge the validity of the tariff. [Id. at 1171](#). Rather, he claimed it was being violated, and the FCA explicitly allows such actions in federal court. [Id. at 1171-1172](#).

**HN7** [↑] The filed-rate doctrine precludes courts from deciding whether a tariff is reasonable, reserving the evaluation of tariffs to the FCC, but [\*\*19] it does not preclude courts from interpreting the provisions of a tariff and enforcing that tariff. If the filed-rate doctrine were to bar a court from interpreting and enforcing the provisions of a tariff, that doctrine would render meaningless the provisions of the FCA allowing plaintiffs redress in federal court.

*Id.* The NGA contains a similar provision allowing suits in federal court. [15 U.S.C. § 717u](#). The plaintiff in *Brown* claimed he was improperly charged multiple fees not provided for in the tariff. [Brown, 277 F.3d at 1172](#).

*Brown* seeks merely to enforce the tariff. He does not claim that he was promised something outside the tariff and then denied it, as in *Central Office*. Nor does he claim that MCI had some obligation to him beyond the obligations set out in the tariff. Nor does he argue that the \$ 10 fee, if authorized by the tariff, is unreasonable.

*Id.* (citations omitted). The filed rate doctrine did not preclude the suit. *Id.* The [\*638] claims in [\*\*20] [Brown](#) are analogous to those of the Plaintiffs here.

[Gulf States Utilities Co. v. Alabama Power Co., 824 F.2d 1465 \(5th Cir. 1987\)](#), also illustrates the distinction based on the damages sought and their effect on the tariff rates. To the extent a claim is premised on a theory that different rates would have been charged but for a breach of contract or other duty, the claim is barred. [Id. at 1471](#). But claims which do not seek relief based on a rate different from that filed would not be precluded. [Id. at 1471-72](#).

For the purposes of discussion, Plaintiffs' claims may be divided chronologically: the "illegal 'parking and lending' service that TCO was not authorized to provide under its FERC-approved natural gas tariff" (SAC at P 76) and the later use of the tariff -approved PAL service in a manner that violates Plaintiffs' rights. (SAC at PP 113-126). They first complain that the Pipeline Defendants provided certain preferences to the Select Shippers that were illegal - a PAL service not included in the tariff. This illegal scheme, Plaintiffs aver, kept their natural gas out of the market and allowed the Select Shippers greater [\*\*21] access to the market, causing Plaintiffs to lose customers.

Plaintiffs do not claim that they were entitled to participate in these preferences. Had that been their claim, the filed rate doctrine would likely preclude it. They could not claim entitlement to services not included in the tariff any more than they could seek damages based on the rates they paid for the services received. Instead, they claim the off-tariff preferences displaced them from the market, resulting in the loss of revenue and business value.

After disclosure of these practices, Pipeline Defendants obtained approval from FERC to offer the PAL service but implemented it so as to perpetuate the advantage given the Select Shippers and the injury to Plaintiffs' business. As to this post-approval PAL service, their claim is even clearer. They argue that the Pipeline Defendants and Select Shippers have created a scheme to effectively deprive Plaintiffs of access to the transportation and storage services under their service agreements with the pipelines. In this regard, Plaintiffs seek to enforce the tariff. Plaintiffs make no complaint about the rates or services other than being denied the benefits of their service [\*\*22] agreements and being injured by the unfair advantage purportedly given to the Select Shippers. They do not seek

damages based on the rates they were charged or some hypothetical rate to be determined by the court. The filed rate doctrine does not bar their claims.

## B. Preemption

Defendants also argue that Plaintiffs' state law claims should be dismissed because the claims are governed exclusively by federal law and thus are preempted. In support of its assertion, Defendants rely on the NGA, stating that in enacting the NGA Congress gave exclusive control of the "transportation and sale of natural gas in interstate commerce" to the federal government, specifically FERC. [15 U.S.C. § 717\(b\)](#).

Generally, under the [Supremacy Clause](#) federal law can preempt state law in one of three ways. First, Congress can expressly state an intention to do so. [College Loan Corp. v. SLM Corp., 396 F.3d 588, 596 \(4th Cir. 2005\)](#). Secondly, "if Congress evidences an intent to occupy a given field, any state law falling within that field is preempted." [\*\*23] [Silkwood v. Kerr-McGee Corp., 464 U.S. 238, 248, 78 L. Ed. 2d 443, 104 S. Ct. 615 \(1984\)](#). Finally, if Congress has not expressed such an intent "state law is still preempted to the extent it [\*639] actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* This third type of preemption is known as conflict preemption. See [Lockyer, 375 F.3d at 849](#).

Defendants assert that in the present case Congress, through the NGA, has created a comprehensive scheme occupying the entire field of the sale and transportation of natural gas and thus the entire field is preempted. In support of its argument, Defendants again cite [Lockyer](#), a case which arose out of the California energy crisis and dealt with the [Federal Power Act](#) (FPA). *Id.* The *Lockyer* court found that because the FPA delegates "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce" to FERC and the plaintiff's claims would encroach on that authority, [\*\*24] the plaintiff's claims were preempted. [Id. at 849, 852](#) (quoting *Transmission Agency of California v. Sierra Pacific Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002)). The *Lockyer* court began its analysis by discussing the broader underpinnings of preemption, particularly field preemption, and looking to Supreme Court precedent in [Silkwood v. Kerr McGee. Lockyer, 375 F.3d 831 at 849](#). In *Silkwood*, the Court considered whether the [Atomic Energy Act](#) completely occupied the field of nuclear energy. In its analysis, the Court carefully considered the legislative history of the controlling statute and found that though Congress intended to completely occupy the nuclear safety field, it did not intend to preempt all state tort actions. See [Silkwood, 464 U.S. at 251-52](#). The Court further found that though the Nuclear Regulatory Commission has exclusive authority to regulate safety matters, "Congress assumed that state law remedies, in whatever form they might take, were available to those injured by nuclear incidents." [\*\*25] [Id. at 256](#). Therefore, the plaintiff's claims for state punitive damages were not preempted. *Id.*

The Supreme Court later discussed the test for field preemption as it relates to the natural gas industry in [Schneidewind v. ANR Pipeline Co., 485 U.S. 293, 99 L. Ed. 2d 316, 108 S. Ct. 1145 \(1988\)](#). Explaining the test for field preemption, the Supreme Court noted in *Schneidewind* that [HN8](#) "every state statute that has some indirect effect on rates and facilities of natural gas companies is not pre-empted." [485 U.S. at 308](#). In determining whether the effect of a state claim results in preemption, the Supreme Court articulated the following test:

When a state regulation "affect[s] the ability of [FERC] to regulate comprehensively...the transportation and sale of natural gas, and to achieve the uniformity of regulation which was an objective of the Natural Gas Act" or presents the "prospect of interference with the federal regulatory power," then the state law may be preempted even though "collision between the state and federal regulation may not be an inevitable consequence."

[\*\*26] [Id. at 310](#) (quoting *Northern Natural Gas Co. v. State Corp. Comm'n of Kansas, 372 U.S. 84, 91-92, 9 L. Ed. 2d 601, 83 S. Ct. 646 (1963)*). Defendants have not demonstrated that the relief sought for Plaintiffs' claims would interfere with FERC's regulatory authority. The consent decree and settlement do not purport to remedy Plaintiffs' claims, and there has been no showing that FERC is engaged in any proceedings that conflict with Plaintiffs' lawsuit.

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Additionally, in *California v. Federal Power Commission*, 369 U.S. 482, 8 L. Ed. 2d 54, 82 S. Ct. 901 (1962), the Supreme Court specifically addressed whether the [\*640] Federal Power Commission (FPC) should proceed with a decision on a merger where there was a pending state court antitrust action challenging the validity of that very merger. *Id. at 487*. The Court, stating that HN9<sup>1</sup> "immunity from the antitrust laws is not lightly implied," found that the FPC did not have exclusive authority over antitrust violations. [\*\*27] *Id. at 485, 487*. Defendants have not established that FERC has such exclusive authority now.

When *Lockyer* and the precedents on which it relies, *Duke Energy Trading and Marketing, L.L.C. v. Davis*, 267 F.3d 1042 (9th Cir. 2001) and *TANC v. Sierra Pacific Power Co.*, 295 F.3d 918 (9th Cir. 2002), are examined in the context laid out above, they are distinguishable from the case currently before the Court. In *Duke Energy* the Ninth Circuit Court of Appeals considered whether the California governor was able to commandeer an energy supplier's "contractual rights to deliver electricity to public utilities within the state." 267 F.3d at 1045. The court found that the California governor's actions "directly nullified" a portion of the FERC approved tariff which "constituted an impermissible intrusion into FERC's territory." *Id. at 1057*. Similarly in *TANC*, the Ninth Circuit found that because the damages TANC sought from its state tort and property claims depended on a finding regarding the validity of a specific system for the transportation of electricity which had been expressly approved by [\*28] FERC, the state claims were preempted. 295 F.3d at 928. Only FERC has the authority to modify the operation of the system which it approved. *Id.* Whether a state claim is preempted by field preemption hinges on the effect that claim will have on the authority of FERC over the industry.

Plaintiffs point out that the court in *Brown*, as discussed *supra*, allowed plaintiff's state breach of contract claims to go forward despite that the terms of the contract were dictated by the tariff. 277 F.3d 1166. The court in *Brown* focused its analysis on the filed-rate doctrine rather than field preemption; however, this Court finds it interesting that field preemption was not even addressed. The court in *Brown* allowed state claims to go forward in a field that was comprehensively regulated and in which the regulatory authority, the FCC, had the power to hear claims similar to those brought by the plaintiff. It is instructive that field preemption was not found to be a bar.

Plaintiffs in the present case do not make any state claims which directly affect FERC's authority to "regulate comprehensively" nor do they present "the prospect of interference [\*\*29] with the federal regulatory power." *Schneidewind*, 485 U.S. at 310. Instead, Plaintiffs simply seek damages for the business they contend they lost as a result of Defendants' actions. Taking all of Plaintiffs' allegations as true, the Court finds that Defendants did not provide a convincing argument that Plaintiffs' claims interfere with FERC's regulatory authority to support dismissal based on field preemption.

### C. Anti-Trust and Common Law Claims

Defendants also challenge the sufficiency of Plaintiffs' antitrust claims, asserting that Plaintiffs do not, and cannot, state facts necessary to support the elements of these claims. The SAC includes ten antitrust claims, Counts Four through Thirteen, which allege state and federal **antitrust law** violations. First, Defendants' motion to dismiss argues that Plaintiffs alleged only FERC violations, which are inadequate to state antitrust violations and failed to allege an "injury to competition." Second, Defendants argue that Plaintiffs lack standing as to some of their [\*641] claims. Last, Defendants argue that Plaintiffs' horizontal conspiracy claims in Counts Eleven and Thirteen contain insufficient conclusory [\*\*30] allegations.

Defendants attack the Plaintiffs reliance on violations of FERC regulations alleged throughout the SAC. Citing *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP*, 540 U.S. 398, 157 L. Ed. 2d 823, 124 S. Ct. 872 (2004), Defendants contend that Plaintiffs' "refusal to deal" claims cannot survive. In *Trinko* the Supreme Court noted that the 1996 Telecommunications Act imposed new duties requiring a regulated company to deal with its competition. *Id. at 401*. Generally, a refusal to cooperate with rivals is a matter of right, but there are limited exceptions. *Id. at 408*. Where that refusal to cooperate is predicated on anticompetitive goals, **antitrust law** may restrict the right. *Id.* In determining whether the exception applied in *Trinko*, the Court reviewed several factors considered in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 86 L. Ed. 2d 467, 105 S. Ct. 2847 (1985) and *Otter Tail Power Co. v. United States*, 410 U.S. 366, 35 L. Ed. 2d 359, 93 S. Ct. 1022 (1973). HN10<sup>1</sup>

The "existence of a regulatory structure designed to deter and remedy anticompetitive [\*\*31] harm" significantly reduces the need to apply traditional antitrust principles. [Trinko, 540 U.S. at 412](#). The Court explained at some length the regulatory framework imposed by the FCC to provide competition access in that setting, in new wholesale market created by the regulatory scheme pursuant to an act "more ambitious than the antitrust laws... 'to eliminate the monopolies.'" [Id. at 415](#) (quoting [Verizon Communications Inc. v. FCC, 535 U.S. 467, 476, 152 L. Ed. 2d 701, 122 S. Ct. 1646 \(2002\)](#)). *Trinko* reaffirms *Otter Tail* and *Aspen Skiing*, even though it acknowledged the limits of antitrust liability. Though FERC regulates the rates for transporting and selling natural gas in interstate commerce, Defendants have not demonstrated that this case involves the same level of regulatory overlay and unique market found in *Trinko*.

The Court finds *Otter Tail* more closely on point. There, the Supreme Court applied antitrust laws despite the authority of the Federal Power Commission. [\*\*32] [Otter Tail, 410 U.S. at 374-75](#). "Repeals of antitrust law by implication is disfavored." [Id. at 372](#) (quoting [United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 350-51, 10 L. Ed. 2d 915, 83 S. Ct. 1715 \(1963\)](#)). There, the regulatory scheme did not explicitly take into account antitrust considerations. The Court found *Otter Tail*'s use of its monopoly power violated antitrust law. [Id. at 377](#). Here, FERC's authority to remedy anti-competitive behavior is decidedly less than the regulatory authority in *Trinko*. FERC's order provided relief limited to disgorging the Pipeline Defendants' ill-gotten profits and a small rebate of SIT fees, neither of which purported to address any anticompetitive results of the scheme.

Further, the SAC joins the Pipeline Defendants and Select Shippers as actors in concert claiming an "illegal agreement" (SAC at PP 40-42) between them to violate antitrust laws and FERC regulations. Characterizing the Select Shippers as their competitors, Plaintiffs, nonselect shippers, contend that the scheme falls within the "concerted action" cases noted by Footnote 3 in *Trinko* as presenting [\*\*33] "greater anticompetitive concerns." [Trinko, 540 U.S. at 410](#). *Trinko* does not alter the applicability of traditional antitrust principles to the Defendants in this case.

Next, Defendants argue that the SAC fails to allege an "injury to competition." They contend that any antitrust claim [\*642] must allege a restriction in the output of some good or service. In Defendants' view, Plaintiffs allege only a loss of market share due to the preferential treatment afforded the Select Shippers in return for the "kickback" payment made to the pipelines.

[HN11](#) [↑] In ruling on a motion to dismiss, the Court must ascertain whether the complaint covers all of the elements that comprise the theory for relief. [Estate Construction Co. v. Miller & Smith Holding Co., 14 F.3d 213 \(4th Cir. 1994\)](#). [HN12](#) [↑] "Injury to competition," is an essential element of every antitrust claim. An antitrust claim must assert that a defendant's conduct constitutes an unreasonable restraint of trade, not merely an economic injury to the plaintiff. [\*\*34] [Continental Airlines, Inc. v. United Airlines, Inc., 277 F.3d 499, 508 \(4th Cir. 2002\)](#). Defendants argue that the SAC fails to allege injury to competition because Plaintiffs do not allege and cannot show that Defendants' conduct resulted in a reduction in output. Defendants posit that Plaintiffs cannot demonstrate that the conduct alleged caused any reduction in natural gas flowing into the market. In fact, Defendants point out, the SAC alleges that the Pipeline Defendants increased their storage capacity to accommodate greater quantities of gas from the Select Shippers. A shift in the market shares between the nonselect and select shippers, alone, would support only a finding of injury to a competitor. Plaintiffs respond by disputing whether a reduction in output is the test for injury to competition, but also argue that the SAC sufficiently alleges an injury to competition anyway.

A fair reading of the SAC supports the denial of Defendants' motion. Plaintiffs allege that Defendants' manipulation of the parking and lending service blocked the nonselect shippers from access to the pipelines. Excluding the nonselect shippers from the marketplace allowed the Select [\*\*35] Shippers, acting in concert with the Pipelines, to take over the market and led to higher prices to retail customers. Plaintiffs assert that more than simply units of natural gas were blocked from the pipelines; their services and other attributes were also prevented from reaching their customers and others in the market. At this stage, the Court is reluctant to require more. Finding a restriction in output is a complex matter which requires a determination of the relevant market and a means of measuring output. See VII Phillip Areeda & Herbert Hovenkamp, [Antitrust Law](#) P 1503 (2003); XI Phillip Areeda & Herbert Hovenkamp, [Antitrust Law](#) P 1901(d) (2005). Here,

... it is enough to note that "output" is not always a clear concept. Even when we define it readily, it is usually difficult to observe. Many alleged restraints are examined before they have had time to work their results. And the longer a restraint has been in effect, the greater is the impact of changes in supply, demand, and other market forces. We are often unable to disentangle the effects of challenged conduct. That is the reason we are so often forced to turn to surrogate for actual effects.

VII Phillip [\*\*36] Areeda & Herbert Hovenkamp, *Antitrust Law* P 1503 (2003).

The Fourth Circuit applied the "rule of reason" test in *Continental* and *Dickson v. Microsoft Corp.*, 309 F.3d 193 (4th Cir. 2002), and each case is relied upon by the parties to support their divergent analyses. Assuming that test applies to Plaintiffs' claims, the Court cannot conclude that Plaintiffs' SAC fails to state a claim.<sup>2</sup> The [\*643] discussion in *Continental* does not support Defendants' argument that a reduction in overall output, as opposed to an increase in price, is necessary to prove injury to competition. In *Continental* the competing airlines at Dulles Airport disputed the effects of templates used to control carry-on baggage. 277 F.3d at 502. Applying the "rule of reason" analysis, the Fourth Circuit discussed that if the template program restricted Continental's passengers from bringing carry-on baggage to the gates then a reduction in output, and therefore a restraint on trade, would be established. Id. at 515. The Court did not require a showing that fewer passengers departed at Dulles or even that fewer passengers chose Continental. Id. [\*\*37] The Court noted that "Continental unquestionably incurred costs" in its effort to provide, as an alternative, a means of bypassing the templates. Id. The Court did not elaborate in its discussion of a restraint in trade based on restraining output but went on to state, "if Continental cannot show any effect on price or output, then it has shown only that it incurred costs in hiring people to lift templates." Id.

The Court also finds the discussion in *Dickson*, although limited, to be of help. 309 F.3d 193 (4th Cir. 2002). In *Dickson* the Fourth Circuit stated that, "aiding the maintenance of a monopoly theoretically could harm competition by affecting price and/or output in various ways." Id. at 206 [\*\*38]. The Court theorized that potential harm to consumers would occur if rivals were foreclosed from access to consumers, denying competitive choices and allowing higher prices by the monopolist. Id. Increased prices and decreased access to consumers for rivals in the market are exactly what Plaintiffs allege here. To the extent that the "rule of reason" test applies to Plaintiffs' claims, the Court cannot conclude that Plaintiffs' SAC fails to state a claim.

Defendants next challenge Plaintiffs' standing to assert antitrust claims based on price fixing. In the SAC Plaintiffs allege that the Select Shipper Defendants, utilizing the advantages they obtained from their preferential deal with the Pipeline Defendants, fixed their prices at just below Plaintiffs' to maximize their profits and avoid detection. Plaintiffs do not allege predatory pricing. Citing *Atlantic Richfield Co. v. USA Petroleum Co.*, 495 U.S. 328, 109 L. Ed. 2d 333, 110 S. Ct. 1884 (1990), Defendants assert that competitors do not have standing to raise price-fixing antitrust claims. HN13[] Competitors are not injured by mere price fixing whether the conspiracy sets maximum or minimum prices. [\*\*39] *Matsushita Electric Industrial Co., LTD., et al. v. Zenith Radio Corp.*, 475 U.S. 574, 584 n.8, 89 L. Ed. 2d 538, 106 S. Ct. 1348 (1986) ("Respondents therefore may not complain of conspiracies that, for example, set maximum price above market levels, or that set minimum prices at any level."); See also *Atlantic Richfield Co.*, 495 U.S. at 336 (finding maximum price-fixing agreements illegal but not causing injury to competitors). Plaintiffs respond that their claims assert that Defendants' price-fixing was accompanied by exclusionary conduct. Even so, the alleged exclusionary conduct does not alter the requirements for standing to claim price fixing. To the extent Plaintiffs' antitrust claims rely on the allegation that Defendants set a price below Plaintiffs' prices, Plaintiffs lack standing as to that aspect of the claims. Insofar as any violation of antitrust laws is based on price-fixing, the Court **GRANTS IN PART** Defendants' motion to dismiss Counts Four, Five, Six, Nine, Ten, and Eleven.

The final objection to the SAC is that the state common law contractual counts fail to state a claim. Defendants argue that the breach of contract [\*\*40] count fails to identify sufficiently any particular contract. [\*644] However,

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<sup>2</sup> Defendants suggested application of the rule of reason test in footnote 21 to their Joint Reply in Support of Defendants' Joint Motion to Dismiss for Failure to State a Claim, and Plaintiffs rely on *Continental* and *Dickson*, both of which applied the test.

Plaintiffs refer explicitly to the tariff's General Terms and Conditions and the service agreements between them and the Pipeline Defendants.

Defendants argue that West Virginia law does not recognize an independent cause of action for a breach of duty of good faith and fair dealing separate and apart from a breach of contract claim. Although this Court cannot find any cases in West Virginia directly on point with the present case, this Court held in *Hoffmaster v. Guiffrida*, 630 F. Supp. 1289 (S.D. W. Va. 1986), that "the law . . . implies a covenant of good faith and fair dealing in every contract for purposes of evaluating a party's performance of that contract." *Id. at 1290*. In other jurisdictions, this implied covenant is subsumed in the contract claim and cannot be pled as an independent cause of action. See, e.g., *Estrin v. Natural Answers, Inc.*, 103 Fed. Appx. 702, 705, 2004 W.L. 1444956 at \*3 (4th Cir. 2004) (unpublished) (finding the district court did not err in dismissing a counterclaim for a breach of good faith and fair dealing because [\*\*41] a separate claim is not recognized under Maryland law); *Harte-Hanks Direct Marketing/Baltimore, Inc. v. Varilease Tech. Fin. Group, Inc.*, 299 F. Supp.2d 505, 518 (D. Md. 2004) (finding that under Michigan law a plaintiff may state a claim for breach of contract based upon an implied duty of good faith and fair dealing, but a breach of that "duty does not supply an independent cause of action where the plaintiff already is alleging breach of contract"); *Rotec Servs. v. Encompass Servs.* 359 S.C. 467, 597 S.E.2d 881, 883-84 (S.C. App. 2004) (agreeing with courts interpreting Georgia, Illinois, New York, and South Dakota laws that state an implied covenant of good faith and fair dealing does not provide an independent cause of action that is separate and apart from a breach of contract claim). Given these cases and this Court's prior consistent pronouncement in *Hoffmaster*, the Court agrees with Defendants and **DISMISSES** Plaintiffs' independent cause of action for good faith and fair dealing.

Defendants also question how Plaintiffs can allege breach of contract and unjust enrichment, a form of restitution arising from implied contracts and generally [\*\*42] precluded by an express contract. Plaintiffs insist this count is in the alternative and permitted despite the inconsistency. At this stage, the Court has not determined whether the contracts identified by Plaintiffs apply to the course of dealing alleged by the SAC. Plaintiffs are entitled to claim alternative theories. Further, while no implied contract may conflict with terms of an express contract, where the express contract between parties does not apply or subsequent conduct not covered by the express contract may support an implied agreement, unjust enrichment may be asserted. *66 Am Jur 2d, Restitution and Implied Contracts*, §§ 6 and 7 (1973).

#### IV.

#### Conclusion

For the reasons stated, the Court **DENIES** Defendants' Joint Motion to Dismiss for failure to state a claim based on the filed rate doctrine and field preemption; **DENIES IN PART** Defendants' Joint Motion to Dismiss for failure to state a claim under antitrust law; **GRANTS IN PART** Defendants' Joint Motion to Dismiss for failure to state a claim under antitrust law to the extent Plaintiffs' claim is based upon price-fixing; **DENIES** Defendants' Joint Motion to Dismiss for failure to state a [\*\*43] claim under common law breach of contract and unjust enrichment; and **GRANTS** Defendants' Joint Motion to Dismiss for failure to state a claim as it relates to Plaintiffs' independent cause of action for good faith and fair dealing.

[\*645] The Court finds that its ruling on the filed-rate doctrine and preemption in sections III(A) and III(B) respectively involves a controlling question of law as to which there is substantial ground for difference of opinion. See 28 U.S.C. § 1292(b). Furthermore, the Court finds that an immediate appeal on these issues may materially advance the ultimate termination of the litigation. *Id.* As such, the Court **CERTIFIES** the issues found in sections III(A) and III(B) for immediate interlocutory appeal pursuant to 28 U.S.C. § 1292(b). In addition, the Court does not stay the proceedings while such an appeal is pursued. The parties are to adhere to the Order and Notice previously entered in this case on August 11, 2005.

373 F. Supp. 2d 631, \*645L 2005 U.S. Dist. LEXIS 11776, \*\*43

The Court **DIRECTS** the Clerk to send a copy of this written opinion and order to counsel of record and any unrepresented parties.

ENTER: September 15, 2005

ROBERT [\*\*44] C. CHAMBERS

UNITED STATES DISTRICT JUDGE

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End of Document

## **United States v. Gosselin World Wide Moving, N.V.**

United States Court of Appeals for the Fourth Circuit

March 18, 2005, Argued ; June 14, 2005, Decided

No. 04-4752, No. 04-4876, No. 04-4877

**Reporter**

411 F.3d 502 \*; 2005 U.S. App. LEXIS 11144 \*\*; 2005-1 Trade Cas. (CCH) P74,829; 2005 AMC 1594

UNITED STATES OF AMERICA, Plaintiff-Appellant, v. GOSSELIN WORLD WIDE MOVING, N.V.; THE PASHA GROUP, Defendants-Appellees. UNITED STATES OF AMERICA, Plaintiff-Appellee, v. GOSSELIN WORLDWIDE MOVING, N.V., Defendant-Appellant, and THE PASHA GROUP, Defendant. UNITED STATES OF AMERICA, Plaintiff-Appellee, v. THE PASHA GROUP, Defendant-Appellant, and GOSSELIN WORLD WIDE MOVING, N.V., Defendant.

**Subsequent History:** US Supreme Court certiorari denied by *Gosselin World Wide Moving, N.V. v. United States*, 547 U.S. 1002, 126 S. Ct. 1464, 164 L. Ed. 2d 246, 2006 U.S. LEXIS 2035 (Mar. 6, 2006)

**Prior History:** [\*\*1] Appeals from the United States District Court for the Eastern District of Virginia, at Alexandria. (CR-03-551). Gerald Bruce Lee, District Judge.

[United States v. Gosselin World Wide Moving N.V., 333 F. Supp. 2d 497, 2004 U.S. Dist. LEXIS 17008 \(E.D. Va., Aug. 16, 2004\)](#)

**Disposition:** AFFIRMED IN PART, REVERSED IN PART, AND REMANDED FOR RESENTENCING.

## **Core Terms**

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bids, immunity, exemption, transportation, forwarders, defendants', Shipping, channels, conspiracy to defraud, segment, inland, sentencing, district court, antitrust, freight, rates, anti trust law, provisions, tariff, firms, antitrust liability, conspiracy, antitrust immunity, plea agreement, effects, counts, me-too, ports, Sherman Act, anticompetitive

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Sherman Act > Remedies > Injunctions

Antitrust & Trade Law > Sherman Act > General Overview

### [HN1](#) Remedies, Injunctions

Price fixing is contrary to the policy of competition underlying the Sherman Act, [15 U.S.C.S. § 1](#). A bid rigging agreement is price-fixing agreement of the simplest kind.

Antitrust & Trade Law > Exemptions & Immunities > Collectives & Cooperatives > General Overview

Governments > Legislation > Interpretation

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > McCarran-Ferguson Act Exemption

## **HN2** [down] Exemptions & Immunities, Collectives & Cooperatives

The United States Supreme Court has consistently construed the reach of exemptions from antitrust laws narrowly, even when Congress confers these exemptions in terms. This narrow construction of antitrust immunity is appropriate because the robust marketplace competition that antitrust laws protect is a fundamental national economic policy. This canon of construction has been employed by the Supreme Court to defeat antitrust exemptions claimed under provisions of the McCarran-Ferguson Act, the Miller-Tydings and McGuire Acts, and the Agricultural Marketing Agreement Act.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Governments > Legislation > Interpretation

Antitrust & Trade Law > Exemptions & Immunities > General Overview

## **HN3** [down] Regulations & Statutes, Shipping Act

Although the Shipping Act of 1984, 46 U.S.C.S. app. §§ 1701-1719, contains several new grants of antitrust immunity, 46 U.S.C.S. app. § 1706(a), nowhere in the 1984 Act did Congress indicate an intention to override the principle of narrow construction for antitrust exemptions that the United States Supreme Court had long applied to the Shipping Act 1916, 46 U.S.C.S. §§ 801-842. Moreover, this interpretive maxim has informed the construction of every other grant of antitrust immunity in federal legislation.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Regulated Industries > Transportation > Common Carriers

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Antitrust & Trade Law > Regulated Industries > General Overview

Antitrust & Trade Law > Regulated Industries > Transportation > General Overview

International Trade Law > General Overview

## **HN4** [down] Regulations & Statutes, Shipping Act

46 U.S.C.S. app. § 1706(a)(4) exempts from antitrust liability any agreement or activity concerning the foreign inland segment of through transportation that is part of transportation provided in a United States import or export trade.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Governments > Legislation > Interpretation

#### **HN5** [+] **Regulations & Statutes, Shipping Act**

For an agreement or activity to "concern the foreign inland segment" under 46 U.S.C.S. app. § 1706(a)(4), the parties undertaking the agreement or participating in the activity must have in mind some consequence for the foreign inland segment that they intend their behavior to have. "Concerning" is essentially a connecting term, the scope and meaning of which is defined in part by the terms it modifies.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

#### **HN6** [+] **Regulations & Statutes, Shipping Act**

See 46 U.S.C.S. app. § 1706(a)(2).

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

International Trade Law > International Commerce & Trade > Exports & Imports > General Overview

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Business & Corporate Compliance > ... > Transportation Law > Water Transportation > Rates & Tariffs

Business & Corporate Compliance > ... > Transportation Law > Water Transportation > US Federal Maritime Commission

#### **HN7** [+] **Common Carrier Duties & Liabilities, Rates & Tariffs**

There is a tariff filing exemption that the Federal Maritime Commission granted to non-vessel operating common carriers for the transportation of used military household goods and personal effects by ocean transportation intermediaries. [46 C.F.R. § 520.13\(c\) \(2004\)](#).

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

#### **HN8** [+] **Regulations & Statutes, Shipping Act**

The touchstone of 46 U.S.C.S. app. § 1706(a)(2)(B) is reasonableness.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Business & Corporate Compliance > ... > Transportation Law > Water Transportation > Rates & Tariffs

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Business & Corporate Compliance > ... > Transportation Law > Water Transportation > US Federal Maritime Commission

#### **HN9**[] **Regulations & Statutes, Shipping Act**

46 U.S.C.S. app. § 1715 conditions exemption from the disclosure requirements of the Shipping Act of 1984, 46 U.S.C.S. app. §§ 1701-1719, on a finding by the Federal Maritime Commission that the exemption will not result in substantial reduction in competition or be detrimental to commerce. Section 1715 is quite clear in laying out the criteria for the granting of filing exemptions: no substantial reduction in competition nor a detriment to commerce may result from the exemption.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

#### **HN10**[] **Regulations & Statutes, Shipping Act**

The statutory phrase "with a reasonable basis to conclude" in 46 U.S.C.S. app. § 1706(a)(2) clearly contemplates an inquiry into the propriety of a party's belief in light of the circumstances. And one of those circumstances is surely the terms of the statute governing the exemption. Sophisticated businesses operating in a regulatory regime are properly charged with knowledge of the statute that applies to their behavior.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

#### **HN11**[] **Regulations & Statutes, Shipping Act**

46 U.S.C.S. app. § 1706(a)(2)(B) may well extend to behavior taken pursuant to an Federal Maritime Commission filing or exemption whose anti-competitive effects are inadvertent, tangential, or debatable. But when the anticompetitive effects are intentional, direct, and palpable, reading § 1706(a)(2)(B) to insulate these effects from liability would encourage gross violations of the antitrust laws and vitiate the canon of construction that aims to protect the operation of these laws.

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Antitrust & Trade Law > Exemptions & Immunities > General Overview

## [\*\*HN12\*\*](#) [blue document icon] **Regulations & Statutes, Shipping Act**

See 46 U.S.C.S. app. § 1706(c)(1).

Admiralty & Maritime Law > Shipping > Regulations & Statutes > Shipping Act

Contracts Law > Contract Conditions & Provisions > General Overview

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Antitrust & Trade Law > Exemptions & Immunities > Export Trade

Business & Corporate Compliance > ... > Transportation Law > Water Transportation > Rates & Tariffs

## [\*\*HN13\*\*](#) [blue document icon] **Regulations & Statutes, Shipping Act**

46 U.S.C.S. app. § 1706(c)(1) was designed for those instances in which a firm has been operating under a clearly established statutory immunity, whose validity or scope is subsequently called into doubt -- for instance because of a changed circumstance or because of some discrete action on the part of the firm that the statute prohibits. When such an event occurs and immunity is abrogated, § 1706(c)(1) ensures that subsequent legal or administrative proceedings will not impose liability for the period between the event and the proceedings. The provision thus affords the regulated firm some time to re-engage the administrative process or otherwise render itself compliant. Under this interpretation, § 1706(c)(1) promotes beneficial reliance by the regulated industry on the regulatory process, particularly when the event that abrogates immunity is the invalidation of a filed tariff or operating agreement. Congress was evidently mindful of this end in passing this provision. To qualify for relief under § 1706(c)(1), a party must therefore identify a discrete event that triggers the provision's grace period. Obviously, that event cannot be the denial of immunity under another statutory provision of the Shipping Act of 1984, 46 U.S.C.S. app. §§ 1701-1719.

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > General Overview

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > Appeals

Criminal Law & Procedure > ... > Entry of Pleas > Role of Court > Factual Basis

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > Knowing & Intelligent Requirement

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > Voluntariness

Criminal Law & Procedure > ... > Guilty Pleas > Allocution & Colloquy > Waiver of Defenses

## [\*\*HN14\*\*](#) [blue document icon] **Entry of Pleas, Guilty Pleas**

Challenges to the factual basis for an adjudication of guilt following a guilty plea are severely circumscribed. A voluntary and intelligent plea of guilty is an admission of all the elements of a formal criminal charge. A defendant who pleads guilty therefore admits all of the factual allegations made in the indictment and waives all non-jurisdictional defects, including the right to contest the factual merits of the charges. In these circumstances, courts have permitted a defendant to challenge an adjudication of guilt only with the argument that the facts underlying the charge are insufficient to constitute a crime.

Criminal Law & Procedure > ... > Fraud Against the Government > Conspiracy to Defraud > Elements

Criminal Law & Procedure > ... > Fraud > Fraud Against the Government > General Overview

Criminal Law & Procedure > ... > Fraud Against the Government > Conspiracy to Defraud > General Overview

Criminal Law & Procedure > ... > Fraud Against the Government > False Claims > General Overview

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > General Overview

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

Criminal Law & Procedure > ... > Entry of Pleas > Guilty Pleas > General Overview

## HN15 [blue icon] Conspiracy to Defraud, Elements

Conspiracy to defraud under [18 U.S.C.S. § 371](#) requires three elements: (1) the existence of an agreement, (2) an overt act by one of the conspirators in furtherance of the objectives, and (3) an intent on the part of the conspirators to agree as well as to defraud the United States. The statute covers not only conspiracies intended to involve the loss of government funds but also any conspiracy for the purpose of impairing, obstructing, or defeating the lawful function of any department of government.

**Counsel:** ARGUED: John J. Powers, III, UNITED STATES DEPARTMENT OF JUSTICE, Antitrust Division, Appellate Section, Washington, D.C., for the United States. Charles Frederick Rule, FRIED, FRANK, HARRIS, SHRIVER & JACOBSON, L.L.P., Washington, D.C., for Gosselin World Wide Moving, N.V., and The Pasha Group.

ON BRIEF: R. Hewitt Pate, Assistant Attorney General, Makan Delrahim, Deputy Assistant Attorney General, James M. Griffin, Deputy Assistant Attorney General, Andrea Limmer, Hays Gorey, Jr., Mark W. Pletcher, Craig Y. Lee, UNITED STATES DEPARTMENT OF JUSTICE, Antitrust Division, Appellate Section, Washington, D.C., for the United States. Henry W. Asbill, COZEN O'CONNOR, P.C., Washington, D.C.; C. Allen Foster, Joe R. Reeder, Shirley Z. Johnson, GREENBERG TRAURIG, L.L.P., Washington, D.C., for Gosselin World Wide Moving, N.V. Anthony V. Nanni, Tommy P. Beaudreau, Michael J. Anstett, Franklin M. Rubinstein, FRIED, FRANK, HARRIS, SHRIVER & JACOBSON, L.L.P., Washington, D.C. [\[\\*\\*2\]](#), for The Pasha Group.

**Judges:** Before WILKINSON and GREGORY, Circuit Judges, and Frederick P. STAMP, Jr., United States District Judge for the Northern District of West Virginia, sitting by designation. Judge Wilkinson wrote the opinion, in which Judge Gregory and Judge Stamp joined.

**Opinion by:** WILKINSON

## Opinion

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[\*505] WILKINSON, Circuit Judge:

In this case, we must decide whether defendants are criminally liable for a scheme that raised the prices the Department of Defense ("DOD") pays to transport its personnel's belongings overseas. Defendants have admitted to orchestrating this scheme and have agreed to accept liability under the Sherman Act, [15 U.S.C. § 1 \(2000\)](#), and the federal anti-fraud statute, [18 U.S.C. § 371 \(2000\)](#), if we determine that their behavior is not immune from such liability under the Shipping Act, 46 U.S.C. app. §§ 1701-1719 (2000). We hold that the Shipping Act's immunity provisions afford defendants no relief from liability for the antitrust violation and conspiracy to defraud they have admitted. We therefore affirm in part, reverse in part, and remand for resentencing.

I.

A.

When personnel of the DOD are [\*\*3] posted to foreign countries, the International Through Government Bill of Lading program ("ITGBL") covers their moving expenses. The DOD contracts with private companies to provide this service. Under the Military Traffic Management Command ("MTMC"), bids are solicited for "through rates" from U.S. freight forwarding companies. A through rate is a payment encompassing all the costs involved in a door-to-door move of DOD personnel's household effects. Bidding for through rates occurs biannually and involves a two step process.

In the first step, or "initial filing," the freight forwarders file a bid for a through rate associated with a particular route, or channel. The low bid that emerges is referred to as the "prime through rate." MTMC publishes this bid and the next four lowest bids. The company that bids the prime is entitled to a set percentage of DOD freight business for the associated channel.

In the second step, other freight forwarders resubmit bids in light of the published prime. The remaining companies may match, or "me-too," the prime for each channel, or they may bid a higher rate. When the channel at issue operates [\*506] in a competitive market, a forwarder must typically [\*\*4] me-too the prime to receive any DOD business. Forwarders that me-too the prime are also entitled to a set portion of DOD business for the cycle and channel for which they have bid.

Because through rates are unitary, they encompass many costs, all of which the U.S. forwarders become responsible for when the DOD accepts their bids. Some of these costs relate to moving services undertaken by other firms along the channel. Costs of this sort cover five general categories of service: the carriage of goods between inland U.S. cities and U.S. ports, services performed at U.S. ports, ocean transportation between U.S. and foreign ports, foreign port services, and carriage of goods between foreign ports and foreign inland points. U.S. freight forwarders must naturally consider these costs in setting their bids.

B.

Defendant Gosselin World Wide Moving N.V. ("Gosselin"), a Belgian corporation, and defendant The Pasha Group ("Pasha"), a U.S. corporation, operate in the channels between the United States and Germany. Both companies provide a package covering local German moving agent services, European port services, and ocean transport services in this market. Defendants thus deal with goods [\*\*5] shipments between German points of origin (the households of DOD personnel abroad) and U.S. ports of destination. Gosselin and Pasha offer a "landed rate," which is a fee that covers all the moving costs involved in the portion of the channels they service.

Defendants also act as the exclusive agents of the International Shippers' Association ("ISA"), a conference of freight forwarders organized to negotiate collectively with shippers operating in the through transportation market. Many of the U.S. freight forwarders who place bids in the MTMC are also ISA members. In their capacity as ISA agents, Gosselin and Pasha negotiate service contracts with the Trans Atlantic American Flag Line Operators ("TAAFLO"), a group of U.S. ocean carriers. TAAFLO's service contract with the ISA entitles all ISA members to ocean transportation with TAAFLO member-carriers at a predetermined rate.

In late 2001, initial filings for the summer bidding cycle of 2002 occurred. A U.S. freight forwarder ("FF1") filed prime through rates with the MTMC for twenty-six of the channels between Germany and the U.S. FF1 did not use the landed rate offered by either defendant. Instead, by negotiating separately with [\*\*6] each service provider at every step of the transportation chain, FF1 was able to undercut its competitors by three dollars per hundredweight in twelve of the twenty-six channels. In December 2001, DOD published FF1's prime bid along with the next four lowest. The remaining forwarders then had until January 12, 2002 to file their second round bids.

Gosselin was evidently alarmed that FF1 had been able to low-bid for the twelve channels without using Gosselin's landed rate. Later in December, Gosselin's managing director sent an email to another landed rate provider, inviting the provider to collude with Gosselin to prevent the me-too rates for the twelve routes at issue from converging to the prime. Such convergence was likely, as we have noted, because of the competitiveness of the US-Germany through transportation market. The Gosselin managing director observed that by "not taking [FF1's bid] into

consideration we would increase the rate level with an average of [\$ 3.63]." The director opined that "this is the only thing that in my mind can happen." In a reply email sent the same day, an executive [\*507] at the competitor concurred, noting that "if we do not react and give [the] industry [\*7] a clear message which rate to base the [me-too bids] on, then everyone will use the low rate and later expect us to reduce our rates so those carriers can work under their [me-too] rates."

Shortly after this exchange, Gosselin's managing director forwarded the emails to the president of Pasha. The Gosselin executive identified the twelve channels, which had "quite some money on the table," and inquired "what rate levels would you be able to support if those [channels] would go to second level?" The director stressed that "it is important we []move rather quickly now." Pasha later indicated its willingness to cooperate.

Defendants faced a difficult task in preventing the imminent me-too bids from converging to the prime. FF1 had already demonstrated that defendants' landed rates could be undercut by contracting separately for each transportation segment along the twelve channels. Defendants therefore had to take preemptive action to prevent the remaining U.S. forwarders from following FF1's lead. In early January 2002, the managing director of Gosselin agreed in writing to pay twelve of the largest German moving agents a specified fee. The German agents, for their part, agreed [\*8] not to handle business from freight forwarders in those channels unless the forwarders submitted me-too bids at the second lowest level (the "second low") or above. Gosselin thereafter arranged a telefax to U.S. freight forwarders who were finalizing their second-step bids advising them of the German agents' undertaking.

Not content with securing their share of the DOD business designated for the second-round bids, defendants set about eliminating FF1's prime rate in the twelve channels at issue. First, they persuaded FF1 to cancel its bid with the MTMC if the remaining freight forwarders would file second-step bids at or above the second-low level. Defendants then secured such an agreement from the remaining forwarders. The forwarders overwhelmingly honored this agreement, and those who strayed below the second-low level were persuaded to withdraw their competitive bids.

As a result of defendants' scheme, a good deal of household goods shipments during the 2002 summer cycle in the twelve channels occurred at or above the second-low rate. The net financial effect of the conspiracy was to cause the DOD to pay substantially more than if FF1's original prime rate had prevailed.

#### C.

[\*\*9] The Department of Justice ("DOJ") charged defendants by information with two counts. The first count alleged a conspiracy to restrain trade in violation of the Sherman Act. [15 U.S.C. § 1 \(2000\)](#). The second count alleged a conspiracy to defraud the United States under [18 U.S.C. § 371 \(2000\)](#).

Defendants agreed to conditional pleas. They stipulated to a statement of facts on the basis of which they would move the district court to dismiss both counts. Gosselin and Pasha agreed in their pleas to make only one argument in support of their motion to dismiss: that the conduct set forth in the statement of facts "is immune from prosecution under the [Shipping Act]." If the district court found such immunity with respect to "both counts," and this finding was affirmed on appeal, defendants would not enter a guilty plea. If the district court denied the motion "as to either or both counts," however, the defendant would plead guilty on the "remaining counts" subject to withdrawal if a higher court overturned the district court's [\*508] finding. The plea agreements also indicated that the parties would recommend to the district court specified sentences [\*10] in the form of financial penalties depending on which count or counts survived the motion to dismiss.

Pursuant to the plea agreement, defendants filed a motion to dismiss on the basis of immunity under the Shipping Act, 46 U.S.C. app. §§ 1701-1719 (2000). The district court granted the motion with respect to the antitrust count, but denied it with respect to the conspiracy to defraud count. Following the arrangement set out in the plea agreements, Gosselin and Pasha pled guilty to the conspiracy to defraud count. Again pursuant to the pleas, the district court imposed on each defendant a criminal fine of \$ 4.6 million. After the final sentencing order, the DOJ appealed the dismissal on immunity grounds of the antitrust count and defendants cross-appealed their convictions

on the conspiracy to defraud count. We now address these appeals, beginning with the issue of immunity under the Shipping Act.

## II.

Defendants' collusion with each other and with other firms operating in the twelve transportation channels clearly violated the Sherman Act's injunction on combinations "in restraint of trade." [15 U.S.C. § 1 \(2000\)](#). "It has been held too often [\*\*11] to require elaboration []that [HN1](#)[<sup>↑</sup>] price fixing is contrary to the policy of competition underlying the Sherman Act . . ." [United States v. McKesson & Robbins, Inc., 351 U.S. 305, 309, 100 L. Ed. 1209, 76 S. Ct. 937 \(1956\)](#). Defendants' scheme, which prevented second round bids from converging to the prime and even erased FF1's first round prime bid, amounted to naked bid rigging. And "bid rigging agreement is price-fixing agreement of the simplest kind." [United States v. Portsmouth Paving Co., 694 F.2d 312, 318 \(4th Cir. 1982\)](#) (quoting [United States v. Bensinger Co., 430 F.2d 584, 589 \(8th Cir. 1970\)](#)); see also [United States v. W.F. Brinkley & Son Constr. Co., Inc., 783 F.2d 1157, 1160 \(4th Cir. 1986\)](#). Criminal antitrust liability is therefore appropriate unless defendants enjoy immunity under another federal law.

[HN2](#)[<sup>↑</sup>] The Supreme Court has consistently construed the reach of exemptions from antitrust laws narrowly, even when Congress confers these exemptions in terms. See, e.g., [Union Labor Life Ins. Co. v. Pireno, 458 U.S. 119, 126, 73 L. Ed. 2d 647, 102 S. Ct. 3002 \(1982\)](#). This narrow construction of antitrust immunity is appropriate [\*\*12] because the robust marketplace competition that antitrust laws protect is a "fundamental national economic policy." [Carnation Co. v. Pac. Westbound Conference, 383 U.S. 213, 218, 383 U.S. 932, 15 L. Ed. 2d 709, 86 S. Ct. 781 \(1966\)](#); see also [Otter Tail Power Co. v. United States, 410 U.S. 366, 374, 35 L. Ed. 2d 359, 93 S. Ct. 1022 \(1973\)](#). This canon of construction has been employed by the Supreme Court to defeat antitrust exemptions claimed under provisions of the [McCarran-Ferguson Act](#), see [Group Life & Health Ins. Co. v. Royal Drug Co., 440 U.S. 205, 231-32, 59 L. Ed. 2d 261, 99 S. Ct. 1067 \(1979\)](#), the [Miller-Tydings and McGuire Acts](#), see [McKesson, 351 U.S. at 316](#), and the [Agricultural Marketing Agreement Act](#), see [United States v. Borden Co., 308 U.S. 188, 198-200, 84 L. Ed. 181, 60 S. Ct. 182 \(1939\)](#).

Defendants here claim exemption from [antitrust law](#) under a federal maritime statute, the Shipping Act of 1984. 46 U.S.C. app. §§ 1701-1719 (2000). The Act modified an earlier law enacted in 1916. See 46 U.S.C. §§ 801-842 (1982). The earlier enactment grew out of the difficulties faced by the U.S. shipping industry in [\*509] the early [\*\*13] part of the last century. See generally [Puerto Rico Ports Auth. v. FMC, 919 F.2d 799, 806-807 \(1st Cir. 1990\)](#); [Plaquemines Port, Harbor and Terminal Dist. v. FMC, 267 U.S. App. D.C. 238, 838 F.2d 536, 542-43 \(D.C. Cir. 1988\)](#). To set U.S. shippers on an equal footing with foreign competitors, who operated outside of U.S. antitrust strictures, Congress granted them limited antitrust immunity. See 46 U.S.C. § 814 (1982).

This immunity, however, came with regulatory strings attached. See *id.* § 804. The regulatory requirements of the 1916 Act were designed to prevent the maritime transportation industry from monopolistically abusing its newly conferred grant of immunity. See [Puerto Rico Ports, 919 F.2d at 807](#). Regulation under the 1916 Act thus preserved some anti-competitive prohibitions. See *id.*; [A & E Pacific Constr. Co. v. Saipan Stevedore Co., Inc., 888 F.2d 68, 71 \(9th Cir. 1989\)](#); [Plaquemines, 838 F.2d at 542-43](#). Nonetheless, regulated firms did enjoy the real benefit of operating outside the full strictures of federal antitrust laws. Mindful of this benefit, the Supreme [\*\*14] Court concluded that the traditional canon of narrow construction, applicable to antitrust exemptions generally, applied with full force to the coverage provisions of the 1916 Act. See [FMC v. Seatrain Lines, Inc., 411 U.S. 726, 732-33, 36 L. Ed. 2d 620, 93 S. Ct. 1773 \(1973\)](#); [Carnation, 383 U.S. at 217-218](#).

The 1916 Act was supplemented by the Shipping Act of 1984, 46 U.S.C. app. §§ 1701-1719 (2000). [HN3](#)[<sup>↑</sup>] Although the 1984 Act contained several new grants of antitrust immunity, see *id.* § 1706(a), nowhere in the 1984 Act did Congress indicate an intention to override the principle of narrow construction for antitrust exemptions that the Supreme Court had long applied to the 1916 Act. Moreover, this interpretive maxim has informed the construction of every other grant of antitrust immunity in federal legislation. We therefore see no reason to depart from ordinary practice in construing the 1984 Act.

## III.

With the foregoing interpretive framework in mind, we turn to defendants' particular contentions. The district court found antitrust immunity for Gosselin and Pasha in three distinct statutory provisions of the Shipping Act. We address immunity [\*\*15] under each statutory provision separately.<sup>1</sup>

#### A.

Defendants first claim immunity under [HN4](#) [46 U.S.C. app. § 1706(a)(4) (2000)], which exempts from antitrust liability "any agreement or activity concerning the foreign inland segment of through transportation that is part of transportation provided in a United States import or export trade."

Defendants argue that this provision covers all [\*\*16] aspects of their scheme to rig bids. The first step in this scheme, defendants emphasize, was the agreement with twelve large German local agents to handle no business from forwarders who filed bids below the second low level. This agreement, defendants claim, is covered by § 1706(a)(4) because the German agents [\*510] provide only services between German ports and destinations in the interior -- a "foreign inland segment." Gosselin and Pasha had market leverage only in this segment; in the other segment they service, ocean transportation, they were constrained by their status as ISA agents and the strict terms of the TAAFLO service contract. Thus the success of the remainder of their scheme depended entirely on the continued viability of the arrangement defendants had reached with the local German firms. For this reason, defendants conclude, the scheme in its entirety should be covered by the immunity provision of § 1706(a)(4).

We do not believe that the statutory exemption extends as far as Gosselin and Pasha would have it. To begin with, the statutory language does not support defendants' position. [HN5](#) [For an agreement or activity to "[concern] the foreign inland segment," § 1706(a)(4) [\*\*17] (emphasis added), as the statute requires, the parties undertaking the agreement or participating in the activity must have in mind some consequence for the foreign inland segment that they intend their behavior to have. *Accord Hileman v. Pittsburgh & Lake Erie Props., Inc.*, 290 F.3d 516, 519 (3d Cir. 2002) ("Concerning . . . is essentially a connecting term, the scope and meaning of which is defined in part by the terms it modifies."); [Commerford v. Thompson](#), 2 Flip. 611, 1 F. 417, 420 (C.C. Ky. 1880) (observing that the "broadest sense" of the term "concerning" is "pertaining to or relative to"). Because defendants' collusive effort was aimed at the entire through transportation market, rather than just the foreign inland segment, we do not think that they can claim exemption from antitrust liability under § 1706(a)(4). Indeed, defendants fixed bids for through transportation rates, i.e. door-to-door rates, not just rates for the "foreign inland segment" of the routes. § 1706(a)(4).

It is true that defendants' original agreement with the German local agents may have had the relationship to a "foreign inland segment" that the statute requires. [\*\*18] *Id.* Indeed, [United States v. Tucor Int'l, Inc.](#), 35 F. Supp. 2d 1172 (N.D. Cal. 1998), aff'd, [189 F.3d 834 \(9th Cir. 1999\)](#), the case upon which Gosselin and Pasha chiefly rely, awarded immunity under the Shipping Act. In *Tucor*, several Philippine firms, operating in a through transportation market "packed, picked up, and trucked household shipments [of U.S. military personnel] from Subic Naval Base and Clark Air Force Base . . . to a Philippine seaport." [189 F.3d at 836](#). The firms were indicted under the Sherman Act for conspiring amongst each other "to suppress competition by fixing prices." [Tucor](#), 35 F. Supp. 2d at 1175. Defendants pled guilty, but the district court later dismissed the indictments on the basis of immunity under § 1706(a)(4). The Ninth Circuit affirmed, finding that § 1706(a)(4)'s reference to a "foreign inland segment," "unambiguously exempts the activities of [defendants]," [Tucor](#), 189 F.3d at 836, occurring as they did between points "entirely within a foreign country." [Id. at 835](#).

There is an argument to be made that the agreement defendants made with [\*\*19] the local German firms fits under the immunity announced in *Tucor*. And if defendants' scheme had ended there, we would have to decide

<sup>1</sup> Defendants note that when parties enter into a conditional plea agreement designed to permit defendants to challenge the prosecution theory on a particular basis, any ambiguities in the stipulated facts must be resolved in defendants' favor and the government may not rely in its prosecution on facts beyond those stipulated. See [United States v. Harvey](#), 791 F.2d 294, 300 (4th Cir. 1986). Accordingly, in resolving the contentions that defendants press on appeal, we take care not to rely on allegations that were not admitted in the plea agreements and the incorporated statement of facts.

whether the agreement did so qualify and whether *Tucor* should be adopted in this circuit. But the scheme did not stop there. Rather, Gosselin and Pasha took additional steps to perfect their bid-rigging plan. And we are not persuaded that these additional steps "[concerned] the foreign inland segment," in the manner the statute requires. § 1706(a)(4).

[\*511] Gosselin and Pasha's contacts with FF1, for instance, related not to foreign inland services, but to defendants' desire that FF1 withdraw the prime through rate bid it had filed with MTMC. Similarly, the agreement defendants secured from other U.S. freight forwarders to file bids at or above the second low level had little to do with the German inland segment of the through services these forwarders offered. Rather, the agreement was a precommitment mechanism to ensure that none of the freight forwarders defected from the anticompetitive cartel that defendants were assembling. When some of these forwarders later broke ranks, defendants instituted measures to reign them in. But these measures [\*20] were designed only to secure withdrawal of the competitive through rate bids the forwarders had filed in the second round, not to have consequences for the foreign inland segment.

In short, none of the additional steps Gosselin and Pasha took beyond their agreement with the German local agents had intended effects for any aspect of the German inland part of the through transportation market. It is unclear, therefore, how these steps "[concerned]" this foreign inland segment, as they must for immunity to attach under § 1706(a)(4).

Moreover, a broad immunity of the sort that Gosselin and Pasha seek would threaten to excise antitrust liability from the through transportation market completely. If § 1706(a)(4) exempted from anti-trust all stages of a conspiracy that involves in some manner a foreign inland segment, then any firm operating in any segment of any through transportation channel need only execute an agreement with a local moving agent to shield itself from the antitrust laws entirely. It does not take much to imagine how sophisticated transportation firms, intent on reaping larger gains, might abuse the immunity of such a rule. The incentives for opportunistic associations [\*21] with companies operating in foreign inland segments would simply be too great. And without the constraint of anticipated antitrust liability, the prices charged by companies in the through transportation market would escalate. Further, the agreements and activity for which defendants seek immunity here were not regulated by the FMC. Lack of regulatory oversight might only exacerbate the upward pressure on prices for through transportation engendered by the absence of antitrust liability.

The upshot of defendants' interpretation of § 1706(a)(4) would therefore be a through transportation market beset with collusive and artificially inflated bids, detrimental to consumers and non-cooperating competitors alike. The government, as a repeat purchaser, would stand to lose much, and the extra money it would have to pay would come from the fisc and thus taxpayers.

It is unlikely that Congress intended such dismaying effects, but if there is any doubt over whether § 1706(a)(4) affords defendants relief, it is settled by the maxim that exceptions to the antitrust laws should be construed narrowly. See *Seatrain*, 411 U.S. at 732-33. The Supreme Court has relied on this principle [\*22] to render agreements subject to the antitrust laws rather than the lesser anticompetitive protections of FMC regulation. See *id.* Here defendants seek exemption from legal enforcement by the DOJ for agreements that have not been regulated by the FMC. We hold for reasons earlier expressed that § 1706(a)(4) does not immunize defendants' scheme to raise through rate bids in the twelve channels at issue.

## B.

Defendants next claim immunity under § 1706(a)(2). That section exempts from antitrust laws

**HN6** [↑] [\*512] any activity or agreement within the scope of this chapter . . . undertaken or entered into with a reasonable basis to conclude that (A) it is pursuant to an agreement on file with the [FMC] and in effect when the activity took place, or (B) it is exempted by the FMC under § 1715 from any filing or publication requirement of this chapter.

Defendants do not claim that their "activity or agreements" were undertaken "pursuant to an agreement on file with the" FMC. Rather, they point to [HN7](#) a tariff filing exemption that the FMC granted to non-vessel operating common carriers, like defendants, for the "transportation of used military household goods and personal effects by [\[\\*\\*23\]](#) ocean transportation intermediaries." [46 C.F.R. § 520.13\(c\) \(2004\)](#). Gosselin and Pasha argue that they reasonably believed their collusive "activities and agreements" to be exempt from the filing requirements of the Shipping Act under this regulation, and thus beyond the antitrust laws under § 1706(a)(2)(B).

[HN8](#) The touchstone of § 1706(a)(2)(B) is reasonableness. Yet the terms of the exemption on which defendants rely, and other features of the regulatory framework in which defendants operate, demonstrate that their reliance was, if anything, unreasonable.

To begin with, the exemption facially covers only "tariffs," see [46 C.F.R. § 520.1\(a\) \(2004\)](#), not the kind of agreements and activities involved in defendants' bid rigging scheme. Yet a distinction between tariffs on the one hand and operating agreements on the other pervades the Shipping Act. Compare § 1703(a) (cataloguing the "agreements by or among ocean common carriers" to which the "chapter applies," including agreements to "discuss, fix, or regulate transportation rates"), with § 1707 (describing "tariffs" that "each common carrier and conference shall keep open [\[\\*\\*24\]](#) to public inspection"). This statutory distinction makes implausible defendants' claim that they understood the reference to tariffs in the exemption to cover the collusive agreements they secured during the course of their scheme.<sup>2</sup>

[\[\\*\\*25\]](#) The terms of § 1715, the Shipping Act provision mentioned in § 1706(a)(2)(B) which governs the FMC's exemption procedures, further erodes Gosselin and Pasha's claim of immunity under § 1706(a)(2)(B). [HN9](#) Section 1715 conditions exemption from the disclosure requirements of the Act on a finding by the FMC "that the exemption will not result in substantial reduction in competition or be detrimental to commerce." The FMC was thus required to make such a finding before passing the tariff filing dispensation on which defendants claim to have relied.

Section 1715 is quite clear in laying out the criteria for the granting of filing exemptions: [\[\\*513\]](#) no "substantial reduction in competition" nor a "[detriment] to commerce" may result from the exemption. The agreements that defendants secured during their bid rigging scheme, however, accomplished just those ends: indeed, it was precisely by a "reduction in competition" that Gosselin and Pasha succeeded in inflating bids above the prime level, and this result was clearly "[detrimental] to commerce." The incongruence between the conditions that § 1715 sets forth and the effects of defendants' bid-rigging scheme erodes defendants' claim that [\[\\*\\*26\]](#) they reasonably understood the tariff filing exemption to permit such activity.

Pasha and Gosselin complain that the ex ante judgment of the FMC under § 1715 should not apply ex post to our interpretation of the reasonableness standard under § 1706(a)(2)(B). But [HN10](#) the statutory phrase "with a reasonable basis to conclude," § 1706 (a)(2), clearly contemplates an inquiry into the propriety of a party's belief in light of the circumstances. And one of those circumstances is surely the terms of the statute governing the exemption. As sophisticated businesses operating in a regulatory regime, defendants are properly charged with knowledge of the statute that applies to their behavior. Accord [Hal Roach Studios, Inc. v. Richard Feiner & Co., Inc., 896 F.2d 1542, 1548 \(9th Cir. 1989\)](#) (citing [Kansas Power & Light v. Burlington N. R.R. Co., 544 F. Supp. 1336, 1347 \(D. Kan. 1982\)](#)) (indicating that "specialized knowledge" including of "statutory . . . law" may properly be presumed of parties according to their "experience"). Thus aware of the criteria set forth in § 1715, Gosselin and

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<sup>2</sup>Indeed, it would appear that the reach of the immunity in § 1706(a)(2)(B) is not as broad as defendants assume. Gosselin and Pasha focus on the tariff disclosure dispensation they received, but the statutory provision clearly requires a reasonable belief in an exemption from "any filing or publication requirement of" the Shipping Act. § 1706(a)(2)(B) (emphasis added). Section 1706(a)(2)(B) thus refers not only to § 1707 -- the tariff disclosure provision -- but also § 1704, which governs disclosure of "agreements." And § 1704(a), by its terms, extends to agreements that "control, regulate, or prevent competition in international ocean transportation." § 1703(a)(6). The agreements secured during the course of defendants' scheme would qualify under this definition, making them subject to a "filing or publication requirement of" the Act under § 1706(a)(2)(B). But if this is so, defendants' would hardly have a "reasonable basis to conclude that" their "activity or agreements" were exempt from "any" disclosure provision of the statute, as they must to be immunized under § 1706(a)(2)(B).

Pasha can hardly claim a "reasonable basis to conclude that" their behavior **[\*\*27]** was covered by the tariff filing exemption. § 1706(a)(2). An exemption conditioned upon no "substantial reduction in competition" simply should not be read to sanction, in any manner, behavior intended to accomplish just such a reduction. § 1715.

Moreover, defendants' position flies once again in the face of the maxim that exceptions to antitrust liability should be narrowly construed. Gosselin and Pasha's claim that the scope of the tariff filing exemption somehow applies to the stark anticompetitive agreements here is simply not persuasive. **HN11**<sup>[↑]</sup> Section 1706(a)(2)(B) may well extend to behavior taken pursuant to an FMC filing or exemption whose anti-competitive effects are inadvertent, tangential, or debatable. But when, as here, the anticompetitive effects are intentional, direct, and palpable, reading § 1706(a)(2)(B) to insulate these effects from liability would encourage gross violations of the antitrust laws and vitiate the canon of construction that aims to protect the operation of these laws.

For the foregoing reasons, we do not believe that Congress intended § 1706(a)(2)(B) to confer immunity on the kind of conduct for which defendants are being prosecuted. We therefore **[\*\*28]** find that defendants' scheme to rig bids is not exempt from antitrust under § 1706(a)(2)(B).

C.

The final part of the Shipping Act under which defendants claim immunity is § 1706(c)(1). This provision states that **HN12**<sup>[↑]</sup> "any determination by an agency or court that results in the denial or removal of the immunity to the antitrust laws set forth in [§ 1706(a)] shall not remove or alter the antitrust immunity for the period before the determination." Defendants contend that an adverse decision on one of the two other statutory immunities they seek -- § 1706(a)(4) and § 1706(a)(2)(B) -- constitutes a "denial or removal," and that § 1706(c)(1) thus requires that any penalty be imposed only prospectively.

**[\*514] HN13**<sup>[↑]</sup> Section 1706(c)(1) was designed for those instances in which a firm has been operating under a clearly established statutory immunity, whose validity or scope is subsequently called into doubt -- for instance because of a changed circumstance or because of some discrete action on the part of the firm that the statute prohibits. See, e.g., § 1709 (listing a variety of prohibited actions for firms operating under filed tariffs or agreements). When such an event occurs and immunity **[\*\*29]** is abrogated, § 1706(c)(1) ensures that subsequent legal or administrative proceedings will not impose liability for the period between the event and the proceedings. The provision thus affords the regulated firm some time to re-engage the administrative process or otherwise render itself compliant. Under this interpretation, § 1706(c)(1) promotes beneficial reliance by the regulated industry on the regulatory process, particularly when the event that abrogates immunity is the invalidation of a filed tariff or operating agreement. Congress was evidently mindful of this end in passing this provision. See, e.g., *H.R. Rep. No. 98-53, pt. 1, at 33 (1983)* ("[Section 1706(c)] is needed to provide a degree of stability and certainty to an agreement filed in good faith and valid on its face.")

To qualify for relief under § 1706(c)(1), defendants must therefore identify a discrete event that triggers the provision's grace period. Obviously, that event cannot be our present denial of immunity under another statutory provision of the Shipping Act, as defendants would have it. Were we to countenance such an argument, a maritime firm wishing to avoid full antitrust liability would simply **[\*\*30]** invent a series of spurious immunity arguments and remain perpetually one step ahead of the judicial or administrative proceedings invalidating them. Such a state of affairs would be the antithesis of the antitrust protections that the maxim requiring narrow construction of exemptions therefrom contemplates. See *Seatrain*, 411 U.S. at 732-33. We therefore reject defendants' interpretation of § 1706(c)(1).

D.

In short, we hold that defendants' scheme to rig bids does not qualify for immunity under any of the three provisions Gosselin and Pasha rely on -- § 1706(a)(4), § 1706(a)(2), and § 1706(c)(1).<sup>3</sup> [\*\*31] We therefore conclude that defendants enjoy no immunity from antitrust prosecution under the Shipping Act.<sup>4</sup>

[\*\*32] [\*515] IV.

The charging information also contained a conspiracy to defraud count. See [18 U.S.C. § 371 \(2000\)](#). Defendants argued in their motion to dismiss that the immunity provisions of the Shipping Act were broad enough to insulate them from liability under a conspiracy to defraud theory. Despite the district court's conclusion that defendants were indeed immunized from antitrust liability by the Shipping Act, the court found that this immunity did not extend to conspiracy to defraud. Employing the test set forth in [Blockburger v. United States, 284 U.S. 299, 76 L. Ed. 306, 52 S. Ct. 180 \(1932\)](#), the district court further determined that the elements of the antitrust claim did not subsume those of the conspiracy to defraud claim. The district court thus concluded that defendants could properly be prosecuted for the same behavior under both counts. See [United States v. Ashley Transfer & Storage Co., Inc., 858 F.2d 221, 224-25 \(4th Cir. 1988\)](#) (finding that conduct may form basis for prosecution under [§ 371](#) following acquittal on Sherman Act count). As a result, the court rejected defendants' motion to dismiss the fraud count on Shipping Act [\*\*33] immunity grounds, and, following the terms of the plea agreements, Gosselin and Pasha pled guilty under [§ 371](#).

We have concluded that defendants enjoy no antitrust immunity under the Shipping Act. We therefore need not determine, as the district court did, whether immunity under the Shipping Act extends to anticompetitive behavior that is also actionable under a conspiracy to defraud theory. Furthermore, defendants concede on appeal that the district court's *Blockburger* analysis is "certainly correct" and that "simultaneous Sherman Act and [Section 371](#) prosecutions are not multiplicitous." Prosecution of defendants' particular course of action under both statutes is therefore permissible.

In reviewing the district court's disposition of the conspiracy to defraud counts, it remains only to address the contention, raised on appeal, that there is insufficient factual support in the plea agreements and incorporated statement of facts for an adjudication of guilt under [§ 371](#).

**HN14** [↑] Challenges to the factual basis for an adjudication of guilt following a guilty plea are severely circumscribed. "A voluntary and intelligent plea of guilty is an admission of all the elements of a formal [\*\*34] criminal charge." [United States v. Willis, 992 F.2d 489, 490 \(4th Cir. 1993\)](#) (quoting [McCarthy v. United States, 394 U.S. 459, 466, 22 L. Ed. 2d 418, 89 S. Ct. 1166 \(1969\)](#)). A defendant who pleads guilty therefore "admits all of the factual allegations made in the indictment," [O'Leary v. United States, 856 F.2d 1142, 1143 \(8th Cir. 1988\)](#) (per curiam), and waives "all non-jurisdictional defects, including the right to contest the factual merits of the charges." [Willis, 992 F.2d at 490](#) (internal citations omitted); see also [United States v. Wiggins, 905 F.2d 51, 52 \(4th Cir.](#)

<sup>3</sup> Because we reach this conclusion on the substance of defendants' immunity arguments, we need not address the government's alternative contention that the agreements for which Gosselin and Pasha seek immunity are beyond the coverage provisions of the Shipping Act and likewise beyond the FMC's jurisdiction. See § 1703; see also [Tucor, 189 F.3d 834](#) (discussing a similar argument made in that case).

<sup>4</sup> One of the factors on which the district court rested its contrary determination was the "rule of lenity." Under this principle of interpretation, the application of ambiguous criminal statutes should be resolved in favor of a defendant. See, e.g., [Rewis v. United States, 401 U.S. 808, 812, 28 L. Ed. 2d 493, 91 S. Ct. 1056 \(1971\)](#). The Supreme Court has counseled, however, that there must be a "genuine ambiguity" before lenity will apply, [Perrin v. United States, 444 U.S. 37, 49 n.13, 62 L. Ed. 2d 199, 100 S. Ct. 311 \(1979\)](#), and has warned that no such ambiguity exists when "the ambiguous reading relied on is an implausible reading of the congressional purpose." [Caron v. United States, 524 U.S. 308, 316, 141 L. Ed. 2d 303, 118 S. Ct. 2007 \(1998\)](#). The Court has also directed that "traditional tools of statutory construction" should be consulted before ambiguity is found. *Id.* (citing [United States v. Shabani, 513 U.S. 10, 17, 130 L. Ed. 2d 225, 115 S. Ct. 382 \(1994\)](#)). Finding, as we do, that such "traditional tools," including "congressional purpose" and ordinary canons of statutory construction, suffice to resolve the interpretive issues before us, we see no occasion for resort to the rule of lenity.

1990). In these circumstances, courts have permitted a defendant to challenge an adjudication of guilt only with the argument that "the facts underlying the charge" are insufficient "to constitute a crime." Stanback v. United States, 113 F.3d 651, 654 (7th Cir. 1997).

The most that Gosselin and Pasha may argue, therefore, is that the allegations in the plea agreements and the [\*516] incorporated statement of facts are so insubstantial that they could not constitute an offense under § 371. It is clear that the factual recitations in the [\*\*35] plea documents easily surmount this low hurdle. HN15 ↑ Conspiracy to defraud under § 371 requires three elements: "(1) the existence of an agreement, (2) an overt act by one of the conspirators in furtherance of the objectives, and (3) an intent on the part of the conspirators to agree as well as to defraud the United States." United States v. Tedder, 801 F.2d 1437, 1446 (4th Cir. 1986). The statute covers "not only conspiracies intended to involve the loss of government funds but also any conspiracy for the purpose of impairing, obstructing, or defeating the lawful function of any department of government." *Id.* The statement of facts laid out in some detail the course of defendants' conspiracy, including the discrete agreements Gosselin and Pasha secured with various firms engaged in the bidding cycle. The statement of facts also unequivocally recites that the foregoing actions "[increased] the rates paid by DOD for the transportation of military goods during the [cycle] to levels higher than would have prevailed in the absence of their conspiracy." The stipulation therefore contains an abundance of information to establish a conspiracy to "[impair] . . . the [\*\*36] lawful function of [a] department of government," *id.* -- namely the MTMC program.

## V.

The final contention that Gosselin and Pasha raise on appeal concerns their sentence. Following the adjudication of guilt on the conspiracy to defraud count, the district court considered the sentences that the parties had agreed to recommend in the event of this outcome. The district court settled on the figure recommended in the plea agreements -- a fine of \$ 4.6 million for each defendant for its part in the conspiracy to defraud. Gosselin and Pasha now argue that this fine exceeded the maximum permissible under the relevant sentencing statute, 18 U.S.C. § 3571 (2000). They assert that the "gross loss" to the government as a result of the conspiracy to defraud was only \$ 1 million, *id.* § 3571 (d), less than the \$ 2.3 million amount on which the plea agreements' sentencing recommendations for the § 371 count were predicated.

The sentencing arrangement that the parties agreed to is carefully set out in each plea document. In the event of an adjudication of guilt, "the United States and the defendant agree that the appropriate disposition of this case is, and [\*37] agree to recommend jointly, that the Court impose a sentence requiring the defendant to pay to the United States a criminal fine . . ." The agreements further provide that "Count 1 and Count 2 are [to be] grouped together" for sentencing purposes, "and thus, the total fine paid will be the greater of" two figures that each sentencing agreement recites. The first figure is derived by applying various listed Sentencing Guidelines factors to the penalty provisions governing Sherman Act violations. The second figure is derived by applying various listed Sentencing Guidelines factors to the penalty provisions governing § 371 violations.

Operating under the assumption that defendants were guilty only of conspiracy to defraud, the district court limited its attention during sentencing to the conspiracy to defraud part of each plea agreement's sentencing recommendation. We have found additionally that the Shipping Act affords defendants no immunity from the antitrust count. We therefore vacate the sentence and remand for resentencing in light of our immunity holding and the entirety of [\*517] each plea agreement's sentencing provisions.

## VI.

We have found that the three immunity provisions [\*\*38] of the Shipping Act under which Gosselin and Pasha claim antitrust immunity afford them no relief. We have also determined that there was no error in the district court's adjudication of guilt on the conspiracy to defraud count. Because the district court applied the sentencing provisions of the plea agreement under the assumption that defendants were only guilty of conspiracy to defraud, a remand for resentencing in light of our disposition of the antitrust issue is in order. The judgment of the district court is therefore

*AFFIRMED IN PART, REVERSED IN PART, AND REMANDED FOR RESENTENCING.*

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## **Tex. Commer. Energy v. TXU Energy, Inc.**

United States Court of Appeals for the Fifth Circuit

June 17, 2005, Filed

No. 04-40962

**Reporter**

413 F.3d 503 \*; 2005 U.S. App. LEXIS 11553 \*\*; 2005-1 Trade Cas. (CCH) P74,836

TEXAS COMMERCIAL ENERGY, A TEXAS LIMITED LIABILITY COMPANY, Plaintiff-Appellant versus TXU ENERGY, INC; ET AL, Defendants; TXU ENERGY INC; TXU GENERATION SERVICES COMPANY LP; TXU PORTFOLIO MANAGEMENT COMPANY LP, formerly known as TXU Energy Trading Company LP; TXU ENERGY SOLUTIONS MANAGEMENT COMPANY, formerly known as TXU Energy Services Co; AMERICAN ELECTRIC POWER INC; AEP TEXAS CENTRAL COMPANY; AEP TEXAS NORTH COMPANY; AMERICAN ELECTRIC POWER SERVICE CORP; AEP TEXAS COMMERCIAL INDUSTRIAL RETAIL LP; RELIANT ENERGY INC; RELIANT RESOURCES INC; RELIANT ENERGY ELECTRIC SOLUTIONS LLC; RELIANT ENERGY RETAIL SERVICES LLC; RELIANT ENERGY SOLUTIONS LLC; AUTOMATED POWER EXCHANGE INC; ELECTRIC RELIABILITY COUNSEL OF TEXAS; TEXAS GENCO LP; CENTERPOINT ENERGY INC; CENTERPOINT ENERGY HOUSTON ELECTRIC LLC; TEXAS INDEPENDENT ENERGY LP; ODESSA-ECTOR POWER PARTNERS LLP; GUADALUPE POWER PARTNERS LLP; TRACTEBEL ENERGY MARKETING, INC., Defendants-Appellees

**Subsequent History:** [\*\*1] As Revised June 30, 2005.

US Supreme Court certiorari denied by [Tex. Commer. Energy v. TXU Energy, Inc., 2006 U.S. LEXIS 52 \(U.S., Jan. 9, 2006\)](#)

**Prior History:** Appeal from the United States District Court for the Southern District of Texas.

[Tex. Commer. Energy v. TXU Energy, Inc., 2004 U.S. Dist. LEXIS 13908 \(S.D. Tex., June 24, 2004\)](#)

**Disposition:** AFFIRM.

### **Core Terms**

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filed rate doctrine, electricity, energy, rates, antitrust, competitor, anti trust law, district court, anticompetitive, generators, argues, antitrust claim, manipulation

### **LexisNexis® Headnotes**

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413 F.3d 503, \*503L<sup>2005 U.S. App. LEXIS 11553, \*\*1</sup>

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Utility Companies > General Overview

## **HN1[ Pipelines & Transportation, Electricity Transmission**

Texas has deregulated its energy market with the passage of Senate Bill 7. 1999 Tex. Gen. Laws 2543. Bill 7 has amended the Texas Public Utility Regulatory Act (PURA) and has split the state's integrated utilities into three groups: electric generation companies, transmission and distribution companies, and retail electric providers. [Tex. Util. Code Ann. § 39.051\(b\)](#). The statute also gives the Public Utility Commission of Texas (PUCT) authority to regulate the state's electric grids and to monitor and remedy market power abuses. Specifically, PUCT has broad power to maintain safe, reliable, and reasonably priced electricity and to ensure that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, discriminatory, predatory, or anticompetitive. [Tex. Util. Code Ann. §§ 39.101\(a\)\(1\), 35.004\(e\)](#). PUCT is also empowered to remedy market abuses by seeking an injunction or civil penalties as necessary to eliminate or to remedy the market power abuse or violation as authorized by Tex. Bus. & Com. Code Ann. ch. 15, by imposing an administrative penalty as authorized by Chapter 15, or by suspending, revoking, or amending a certificate or registration as authorized by [Tex. Util. Code Ann. § 39.356](#). [Tex. Util. Code Ann. § 39.157\(a\)](#).

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrers & Objections > Motions to Dismiss

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

## **HN2[ Standards of Review, De Novo Review**

An appellate court reviews a district court's grant of a motion to dismiss de novo. A complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Common Carriers

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

## **HN3[ Filed Rate Doctrine, Common Carriers**

The filed rate doctrine bars judicial recourse against a regulated entity based upon allegations that the entity's filed rate is too high, unfair, or unlawful. It is up to the respective governmental agency to determine whether the rates are discriminatory or unlawful, not the courts. The doctrine holds that any filed rate, that is, one approved by the governing regulatory agency, is per se reasonable and unassailable in judicial proceedings brought by ratepayers.

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN4** **Regulated Industries, Energy & Utilities**

See [Tex. Util. Code Ann. § 39.158\(b\)](#).

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

#### **HN5** **Exemptions & Immunities, Filed Rate Doctrine**

The application of the filed rate doctrine is far different from the creation of an antitrust immunity. Defendants who engage in anticompetitive activities based on filed rates are still subject to scrutiny under the antitrust laws by the government and to possible criminal sanctions or equitable relief. The filed rate doctrine is very much a part of current federal **antitrust law**. It has been consistently applied as a defense to antitrust actions by various circuits and by the United States Supreme Court for decades.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Antitrust Issues > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Regulated Industries > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > Utility Companies

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN6** **Filed Rate Doctrine, Public Utilities & Telecommunications Carriers**

Applying the filed rate doctrine, along with other common-law defenses that are normally part of the federal antitrust legal landscape, gives effect to the legislature's intent to have the Texas Public Utility Regulatory Act complement other state and federal antitrust provisions. [Tex. Util. Code Ann. § 39.158\(b\)](#).

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Governments > Legislation > Interpretation

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN7** Exemptions & Immunities, Filed Rate Doctrine

The rationales underlying the filed rate doctrine apply equally strongly to regulation by state agencies. Moreover, state antitrust claims do not need to be addressed separately because the Texas Free Enterprise and Antitrust Act explicitly mandates that its provisions be interpreted in harmony with federal **antitrust law**.

Energy & Utilities Law > Utility Companies > Contracts for Service

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > State Regulation

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > US Federal Energy Regulatory Commission

Energy & Utilities Law > Regulators > Public Utility Commissions > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Authorities & Powers

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > General Overview

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Energy & Utilities Law > Utility Companies > Rates > General Overview

## **HN8** Utility Companies, Contracts for Service

The filed rate doctrine applies to market-based energy rates because the Federal Energy Regulatory Commission is responsible for ensuring just and reasonable rates and, to that end, wholesale power rates continue to be filed and subject to agency review. Similarly, the Public Utility Commission of Texas (PUCT) is required to ensure safe, reliable, and reasonably priced electricity and that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, discriminatory, predatory, or anticompetitive. [Tex. Util. Code Ann. §§ 39.101\(a\)\(1\), 35.004\(e\)](#). PUCT also requires electricity generators to file detailed information to assess market power and even a market power mitigation plan for those generators that control more than 20 percent of the electricity market in a specific region. [Tex. Util. Code Ann. §§ 39.155-156](#). Accordingly, PUCT's oversight over the market is sufficient to conclude that the Balancing Energy Service energy rates are "filed" within the meaning of the filed rate doctrine.

**Counsel:** For TEXAS COMMERCIAL ENERGY, A TEXAS LIMITED LIABILITY COMPANY, Plaintiff - Appellant: Mikal C Watts, Gregory Lamar Gowan, Watts Law Firm, Corpus Christi, TX.

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For AUTOMATED POWER EXCHANGE INC, Defendant - Appellee: Osborne J Dykes, William Joseph Boyce, Lance R Bremer, Fulbright & Jaworski, Houston, TX.

For ELECTRIC RELIABILITY COUNSEL OF TEXAS, Defendant - Appellee: Judith R Blakeway, Strasburger & Price, San Antonio, TX.

For TEXAS GENCO LP, CENTERPOINT ENERGY INC, CENTERPOINT ENERGY HOUSTON ELECTRIC LLC, Defendants - Appellees: Daniel K Hedges, John A Irvine, Porter & Hedges, Houston, TX.

For TEXAS INDEPENDENT ENERGY LP, ODESSA-ECTOR POWER PARTNERS LLP, GUADALUPE POWER PARTNERS LLP, Defendants - Appellees: Lawrence A Gaydos, Kathleen McIntosh Beasley, Haynes & Boone, Dallas, TX.

For TRACTEBEL ENERGY MARKETING INC, Defendant - Appellee: Ernest L Edwards, B Richard Moore, Jr, Amy L Baird, Lemle & Kelleher, New Orleans, LA.

CIRRO ENERGY CORP, UTILITY CHOICE LP dba Utility Choice Electric, Amicus [\[\\*\\*3\]](#) Curiae: Robert S Potosky, Dallas, TX.

**Judges:** Before GARZA and BENAVIDES, Circuit Judges. \*

**Opinion by:** EMILIO M. GARZA

## **Opinion**

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\* Judge Garwood recused himself after oral argument in this case. As a result, this opinion is being entered by quorum pursuant to 28 U.S.C. § 46.

[\*506] EMILIO M. GARZA, Circuit Judge.

Texas Commercial Energy ("TCE"), an energy retailer, appeals the district court's dismissal of its lawsuit against TXU Energy, Inc. ("TXU"), a generator of electric power, and twenty-three other defendants. TCE argues that the district court erred by applying the filed rate doctrine to preclude it from recovering damages it sustained when TXU allegedly manipulated its market position to create substantial price increases in the short-term energy market.

I

**HN1** [↑] Texas deregulated its energy market in 1999 with the passage of Senate Bill 7. Act of May 27, 1999, 76th Leg., R.S., ch. 405, 1999 Tex. Gen. Laws 2543. Bill 7 amended the *Public Utility Regulatory Act* ("PURA") and split the state's integrated utilities into three groups: electric generation companies, transmission and distribution companies, and retail electric providers. [\*\*4] [TEX. UTIL. CODE ANN. § 39.051\(b\)](#). The statute also gives the Public Utility Commission of Texas ("PUCT") authority to regulate the state's electric grids and to monitor and remedy market power abuses.<sup>1</sup> Specifically, PUCT has broad power to maintain "safe, reliable, and reasonably priced electricity" and to "ensure that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, discriminatory, predatory, or anticompetitive." [TEX. UTIL. CODE ANN. §§ 39.101\(a\)\(1\), 35.004\(e\)](#). PUCT is also empowered to remedy market abuses by "seeking an injunction or civil penalties as necessary to eliminate or to remedy the market power abuse or violation as authorized by Chapter 15, by imposing an administrative penalty as authorized by Chapter 15, or by suspending, revoking, or amending a certificate or registration as authorized by [Section 39.356](#)." [TEX. UTIL. CODE ANN. § 39.157\(a\)](#).

[\*\*5] TCE is a retail electric provider that sells electricity to customers in Texas by entering into bilateral agreements with generators and by purchasing electricity through the ancillary Balancing Energy Service ("BES") market. The BES market is a bid-based wholesale market for short-term electricity power. PUCT contracted with a private organization, the Electric Reliability Council of Texas, Inc. ("ERCOT"), to administer the BES market. Under the terms of the contract, ERCOT was required to ensure system reliability, nondiscriminatory access to transmission and distribution systems, access to market information, and clearance of all market transactions. PUCT also created the Market Oversight Division ("MOD") to ensure general compliance with the requirements of PURA. In 2002, MOD required all participants in the Texas electricity market to file an affidavit with PUCT pledging that they would not engage in market manipulation.

In February 2003, during severe winter weather, the price for electricity on the BES market soared. As a result, TCE was forced to pay considerably higher sums for the energy it had to supply its customers. The resulting losses led TCE [\*507] to meet with [\*\*6] MOD and express their concern that the price spikes were the result of anti-competitive bids and market manipulation. TCE alleged that, at the time of the price fluctuations, TXU controlled anywhere from seventy-five to ninety-nine percent of the BES market and that it used its market strength to purposefully withhold energy from the market in order to increase the price. TCE argues that while ERCOT made some attempts to force TXU to rectify the situation, it failed to follow its own protocols. Due to the mounting losses, TCE was forced to file for Chapter 11 bankruptcy.

TCE filed suit against twenty-four market participants including TXU, its subsidiaries, and ERCOT. According to the complaint, TCE alleges that the defendants violated the federal *Sherman Antitrust Act* and the *Texas Free Enterprise and Antitrust Act ("TFEAA")*. TCE also alleges fraud, negligent misrepresentation, breach of contract, defamation, business disparagement, and civil conspiracy. The defendants filed motions to dismiss. After holding a hearing on the motions, the district court dismissed TCE's fraud, negligent misrepresentation, and state and federal antitrust claims on the basis of the filed rate doctrine. [\*\*7] The court also dismissed some of the breach of contract and civil conspiracy claims, and denied ERCOT's motion to dismiss the defamation and business

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<sup>1</sup> Texas' electrical system is independent from the rest of the United States' which is administered through the Federal Energy Regulatory Commission ("FERC"). PUCT fulfills a similar role as FERC.

disparagement claims. Having dismissed the federal claims, the district court dismissed the entire case, finding that there was no basis for diversity jurisdiction on the remaining state law claims. TCE now appeals the district court's dismissal of its antitrust claims.<sup>2</sup>

## II

**HN2**[<sup>↑</sup>] We review a district court's grant of a motion to dismiss *de novo*. [Martin K. Eby Const. Co. v. Dallas Area Rapid Transit](#), 369 F.3d 464, 467 (5th Cir. 2004). A complaint "should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." [\*\*8] [Conley v. Gibson](#), 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957).

The district court held that, even if the defendants had engaged in market manipulation, the filed rate doctrine precluded TCE from recovering for its losses under federal and state **antitrust law**. **HN3**[<sup>↑</sup>] The filed rate doctrine bars judicial recourse against a regulated entity based upon allegations that the entity's "filed rate" is too high, unfair or unlawful. See, e.g., [Square D Co. v. Niagara Frontier Tariff Bureau, Inc.](#), 476 U.S. 409, 90 L. Ed. 2d 413, 106 S. Ct. 1922 (1986) (filed rate doctrine bars damage action against motor carriers under antitrust laws even though carriers colluded to set artificially high filed rate). The Supreme Court established this doctrine in [Keogh v. Chicago & Northwestern Railway, Co.](#), 260 U.S. 156, 67 L. Ed. 183, 43 S. Ct. 47 (1922). In *Keogh*, the Supreme Court held that a shipper could not bring an antitrust action against carriers in connection with tariffs paid because those tariffs had been filed and approved by the Interstate Commerce Commission. [\*\*9] [Id. at 163](#). The Court reasoned that even if the carriers had conspired to eliminate competition, the shipper could not recover under **antitrust law** because it could receive a rebate that might give the shipper "preference over his trade competitors." *Id.* Furthermore, the Court held that it was up to the respective governmental agency to determine whether the [\*508] rates were discriminatory or unlawful, not the courts. [Id. at 164](#).

Since *Keogh*, courts have consistently applied the filed rate doctrine in a number of energy cases to preclude lawsuits against companies based on rates that were filed with a government agency. See, e.g., [Ark. La. Gas Co. v. Hall](#), 453 U.S. 571, 578, 69 L. Ed. 2d 856, 101 S. Ct. 2925 (1981) (filed rate doctrine prohibits seller of natural gas to collect a rate different than the one it filed with the Federal Power Commission.); [Tex. E. Transmission Corp. v. Fed. Energy Regulatory Comm'n](#), 102 F.3d 174, 189 (5th Cir. 1996) (natural gas pipeline precluded from retroactively assessing customer rates based on a new and different rate methodology because the prior rates had been filed with a federal agency). "Simply stated, [\*\*10] the doctrine holds that any 'filed rate'--that is, one approved by the governing regulatory agency--is per se reasonable and unassailable in judicial proceedings brought by ratepayers." [Wegoland, Ltd. v. NYNEX Corp.](#), 27 F.3d 17, 18 (2d Cir. 1994).

## III

TCE argues that the district court was erroneous in applying the doctrine because: 1) the legislature clearly intended for aggrieved parties to bring private claims under PURA; 2) wholesale energy rates in the BES market are not filed with PUCT; 3) antitrust exemptions should be narrowly construed; and 4) the filed rate doctrine cannot be applied because PURA does not create a substitute damages mechanism.

## A

TCE argues that, under Bill 7, the Texas state legislature expressly intended to allow private antitrust claims to be brought under PURA and that the district court's decision violates "the primary rule in statutory interpretation [--] that a court must give effect to legislative intent." [Zer-llan v. Frankford \(In re CPDC, Inc.\)](#), 337 F.3d 436, 442 (5th Cir. 2003) (quoting [\*\*11] [Crown Life Ins. Co. v. Casteel](#), 22 S.W.3d 378, 383, 43 Tex. Sup. Ct. J. 348 (Tex. 2000)). In support, TCE cites to PURA's savings clause which states that **HN4**[<sup>↑</sup>] "nothing in this chapter shall be construed to confer immunity from state or federal antitrust laws. This chapter is intended to complement other state and

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<sup>2</sup>TCE does not challenge the district court's decision to dismiss their negligent misrepresentation and fraud claims under the filed rate doctrine.

federal antitrust provisions. Therefore, antitrust remedies may also be sought in state or federal court to remedy anticompetitive activities." [TEX. UTIL. CODE ANN. § 39.158\(b\)](#).

TCE asserts that the application of the filed rate doctrine violates this provision of the statute by conferring immunity on the defendants. In *Square D Co.*, the Supreme Court rejected this position by explicitly stating that [HN5](#) the application of the filed rate doctrine "is far different from the creation of an antitrust immunity." [476 U.S. at 422](#); see also [Wegoland, 27 F.3d at 22](#) ("filed rate doctrine does not leave regulated industries immune from suit under the RICO or antitrust statutes."). Rather, as the Court noted, defendants who engage in anticompetitive activities based on filed rates are "still subject to scrutiny under the antitrust laws by the Government and to possible criminal [\*\*12] sanctions or equitable relief." [Square D Co., 476 U.S. at 422](#). Moreover, contrary to TCE's assertions, the filed rate doctrine is very much a part of current federal **antitrust law**. It has been consistently applied as a defense to antitrust actions by various circuits and by the Supreme Court for decades. [Id. at 423](#) ("the Keogh rule has been an established guidepost at the intersection of the antitrust and interstate commerce statutory regimes for 6 1/2 decades . . . [and is] an essential element of the settled legal context in which Congress has [\*509] repeatedly acted in this area"). Thus, we find that [HN6](#) applying the filed rate doctrine, along with other common-law defenses that are normally part of the federal antitrust legal landscape, gives effect to the legislature's intent to have PURA "complement other state and federal antitrust provisions." [TEX. UTIL. CODE ANN. § 39.158\(b\)](#).

Similarly, TCE's state antitrust arguments--that applying the filed rate doctrine would displace provisions set out in the TFEAA, or that the filed rate doctrine as a whole does not apply to the TFEAA--are misplaced. "Courts have uniformly held . . . that [\*\*13] [HN7](#) the rationales underlying the filed rate doctrine apply equally strongly to regulation by state agencies." [Wegoland LTD., 27 F.3d at 20](#); see also [H.J. Inc. v. Northwestern Bell Tel. Co., 954 F.2d 485, 494 \(8th Cir. 1992\)](#) ("the filed rate doctrine applies whether the rate in question is approved by a federal or state agency"); [Taffet v. Southern Co., 967 F.2d 1483 \(11th Cir. 1992\)](#); [Korte v. Allstate Ins. Co., 48 F. Supp. 2d 647 \(E.D.Tex. 1999\)](#). Moreover, state antitrust claims do not need to be addressed separately because the TFEAA explicitly "mandates that its provisions be interpreted in harmony with federal **antitrust law**." [Johnson v. Hosp. Corp. of Am., 95 F.3d 383, 391 n.7 \(5th Cir. 1996\)](#). Thus, the filed rate doctrine applies with equal force to TCE's state antitrust claims.<sup>3</sup>

#### [\*\*14] B

TCE contends that the filed rate doctrine is inapplicable because PURA does not require rates in the BES market to be filed with PUCT, which does not set or approve these rates. We agree with the approach taken by other circuits who have addressed this issue in the context of rates filed with PUCT's federal counterpart, FERC. In *Town of Norwood, Massachusetts v. New England Power Co.*, the First Circuit concluded that [HN8](#) the filed rate doctrine applied to market-based energy rates because FERC was "responsible for ensuring 'just and reasonable' rates and, to that end, wholesale power rates continue to be filed and subject to agency review." [202 F.3d 408, 419 \(1st Cir. 2000\)](#). The Ninth Circuit echoed this view, noting that while FERC had waived many requirements that it had applied under a cost-based system, the filed rate doctrine continued to apply to market-based energy rates because the agency continued to "oversee wholesale electricity rates . . . by reviewing and approving a variety of documents filed by [market actors]." [\*\*15] [Public Util. Dist. No. 1 v. Dynegy Power Mktg., Inc., 384 F.3d 756, 760-61 \(9th Cir. 2004\)](#). Similarly, under Bill 7, PUCT is required to ensure "safe, reliable, and reasonably priced electricity" and "that ancillary services necessary to facilitate the transmission of electric energy are available at reasonable prices with terms and conditions that are not unreasonably preferential, prejudicial, discriminatory, predatory, or anticompetitive." [TEX. UTIL. CODE ANN. §§ 39.101\(a\)\(1\), 35.004\(e\)](#). PUCT also requires electricity generators to file detailed information to assess market power and even a market power mitigation plan for those generators that

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<sup>3</sup>TCE also contends that the district court erred by ruling that only the U.S. Congress has the authority to determine the applicability of the filed rate doctrine and that the doctrine may only be abrogated through an amendment to the [Sherman Act](#). The defendants, however, "do not dispute that the Texas legislature, had it chosen to do so, could have repealed the application of the filed rate doctrine to cases brought under the TFEAA." Since we conclude there is no evidence that the state legislature sought to eliminate this doctrine from state antitrust suits, this argument is moot.

control more than 20% of the electricity **[\*510]** market in a specific region. [TEX. UTIL. CODE ANN. §§ 39.155-156.](#) Accordingly, PUCT's oversight over the market is sufficient to conclude that the BES energy rates are "filed" within the meaning of the filed rate doctrine.

#### C

TCE argues that the filed rate doctrine should not be applied because antitrust exemptions should be narrowly construed. It morphs this general assertion into a more specific allegation that its claims are exempt from the filed rate doctrine under the "competitor exception." **[\*\*16]** "The competitor exception, which has never been recognized by this court or the Supreme Court, holds that "an anticompetitive practice embodied in a [filed] tariff may [still] violate the antitrust laws if it . . . impacts upon competitors as opposed to customers." [City of Groton v. Conn. Light and Power Co., 662 F.2d 921, 929 \(2d Cir. 1981\)](#); see also [Utilimax.com, Inc. v. PPL Energy, LLC, 378 F.3d 303, 307 \(3d Cir. 2004\)](#) (competitor exception exists "because competitors are not the intended beneficiaries of that rule of public utility regulation") (quoting [Essential Communications Sys. v. Am. Telephone & Telegraph Co., 610 F.2d 1114, 1121 \(3d Cir. 1979\)](#)). But cf. [Pinney Dock & Transp. Co. v. Penn Central Corp., 838 F.2d 1445-47 \(6th Cir. 1988\)](#) (rejecting competitor exception).

Assuming, without deciding, that such an exception exists, we find that the competitor exception is not applicable to this case. TXU has affiliated retail electric providers as part of its subsidiaries. However, TCE is not a competitor to TXU in the context of this case because all of its claims of market manipulation are focused solely on TXU's actions as an electric generation **[\*\*17]** company. Thus, the court did not err in refusing to apply the exception.

#### D

Finally, TCE argues that the filed rate doctrine is inapplicable because PURA did not create a "substitute mechanism for the recovery of damages." It also alleges that the "implication doctrine" warrants reversal and that the application of the filed rate doctrine violates the state constitution. TCE failed to raise these arguments before the district court. Accordingly, they are waived. [Horton v. Bank One, N.A., 387 F.3d 426, 435 \(5th Cir. 2004\)](#).

#### IV

For the above stated reasons, we AFFIRM the district court's judgment.

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End of Document

## Minn. Life Ins. Co. v. AXA Inv. Mgr

United States District Court for the District of Minnesota

June 22, 2005, Decided

Civil No. 03-4383 (DWF/SRN)

### **Reporter**

2005 U.S. Dist. LEXIS 12320 \*; 2005-2 Trade Cas. (CCH) P74,875

Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc., Plaintiffs, v. AXA Investment Mgr, Frederick Fritz Feuerherm, and Wayne Schmidt, Defendants, and AXA Investment Mgr, Counter-Claimant, v. Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc., Counter-Defendants, and Frederick Fritz Feuerherm and Wayne Schmidt, Counter-Claimant, v. Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc., Counter-Defendants.

**Subsequent History:** Motion denied by, in part, As moot, Motion denied by, in part, Motion denied by, As moot  
[Minn. Life Ins. Co. v. Axa Inv. Mgr, 2005 U.S. Dist. LEXIS 62011 \(D. Minn., July 11, 2005\)](#)

## **Core Terms**

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Plaintiffs', summary judgment, track record, trade secret, employees, tortious interference, damages, fixed income, Counter-Claimants, Defendants', literally, press release, contracts, Lanham Act, confidential information, unfair competition, fiduciary duty, misappropriation, conversion, booklet, pitch, duplicative, disclosure, consumers, buy, breach of fiduciary duty, injunctive relief, genuine, issue of material fact, business advantage

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

### **[HN1](#) [down arrow] Entitlement as Matter of Law, Appropriateness**

Summary judgment is proper if there are no disputed issues of material fact and the moving party is entitled to judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#). A court must view the evidence and the inferences that may be reasonably drawn from the evidence in the light most favorable to the nonmoving party. As the United States Supreme Court has stated, summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to secure the just, speedy, and inexpensive determination of every action. [Fed. R. Civ. P. 1](#).

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

## **HN2** [] **Summary Judgment, Opposing Materials**

The moving party on summary judgment bears the burden of showing that there is no genuine issue of material fact and that it is entitled to judgment as a matter of law. The nonmoving party must demonstrate the existence of specific facts in the record which create a genuine issue for trial. A party opposing a properly supported motion for summary judgment may not rest upon mere allegations or denials, but must set forth specific facts showing that there is a genuine issue for trial.

Trade Secrets Law > Civil Actions > Burdens of Proof

Torts > Business Torts > Unfair Business Practices > General Overview

Trade Secrets Law > Trade Secret Determination Factors > Competitive Advantage

Trade Secrets Law > Trade Secret Determination Factors > Ready Availability

Trade Secrets Law > Misappropriation Actions > Elements of Misappropriation > General Overview

Trade Secrets Law > Protection of Secrecy > Reasonable Measures > General Overview

## **HN3** [] **Civil Actions, Burdens of Proof**

In order to establish claims for misappropriation of confidential information and trade secrets, a plaintiff must show that: (1) the information is not generally known or ascertainable; (2) the information provides a demonstrable competitive advantage; and (3) the information was subject to reasonable efforts to maintain its secrecy.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Remedies

Civil Procedure > Remedies > Damages > Monetary Damages

Torts > Business Torts > General Overview

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > General Overview

## **HN4** [] **Lanham Act, Remedies**

To establish a Lanham Act or a Minnesota Deceptive Trade Practices Act claim, a plaintiff must demonstrate that: (1) the defendant made a false statement of fact in a commercial advertisement about its own or another's product; (2) the statement actually deceived or has the tendency to deceive a substantial segment of its audience; (3) the deception is material; (4) the defendant caused its false statement to enter into interstate commerce; and (5) plaintiff has been or is likely to be injured as a result of the false statement. In addition, to recover money damages under the Lanham Act, a plaintiff must prove both actual damages and a causal link between a defendant's actions and those damages.

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > General Overview

#### **HN5** **Federal Unfair Competition Law, Lanham Act**

The false statement necessary to establish a Lanham Act violation generally falls into one of two categories: (1) commercial claims that are literally false as a factual matter; and (2) claims that may be literally true or ambiguous but which implicitly convey a false impression, are misleading in context, or are likely to deceive consumers.

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

#### **HN6** **Federal Unfair Competition Law, False Advertising**

If a plaintiff is able to prove that a claim is literally false, a court may grant relief without considering whether the buying public was actually misled; the plaintiff need not prove actual consumer confusion. In determining whether a claim is literally false, a court must examine the message conveyed within its full context.

Evidence > Burdens of Proof > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

#### **HN7** **Evidence, Burdens of Proof**

In examining whether use of another's track record is false or misleading, a court will consider the portability requirements of the Securities & Exchange Commission (SEC) and the CFA Institute, formerly known as the Association for Investment Management and Research (AIMR). While a court considers these portability requirements, the burden is still on plaintiff to prove that the advertising is false and misleading.

Securities Law > Investment Companies > Activities

Securities Law > Investment Companies > Illegal Acts & Unlawful Representations

#### **HN8** **Investment Companies, Activities**

The Security and Exchange Commission's rules state that a registered investment company may not advertise the performance of accounts managed by its portfolio manager at a predecessor firm if other individuals played a significant role in achieving that record. [15 U.S.C.S. § 80b-6\(4\)](#). CFA Institute has also set forth portability standards. Generally, CFA Institute standards require that a firm's investment decision-making processes remain substantially unchanged in order for a new firm to claim a prior firm's performance record. AIMR-PPS Standard 5.A.4.

Antitrust & Trade Law > Consumer Protection > False Advertising > Lanham Act

Civil Procedure > Remedies > Damages > Monetary Damages

Trademark Law > ... > Remedies > Equitable Relief > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Remedies

#### **HN9** [blue icon] **False Advertising, Lanham Act**

A plaintiff's burden in a Lanham Act case is, in part, dependent on the relief the plaintiff seeks. A plaintiff that wishes to recover money damages for a violation of the Lanham Act and related state statutes must establish actual confusion among the consumers of the plaintiff's products, actual injury, and a causal connection between the confusion and the injury. When a plaintiff seeks only injunctive relief, however, it need only prove a likelihood of confusion among consumers that has resulted from defendants' actions. Where a defendant has engaged in literally false advertising, a court will presume that the plaintiff has suffered injury that warrants injunctive relief.

Business & Corporate Law > ... > Management Duties & Liabilities > Causes of Action > General Overview

Governments > Fiduciaries

Labor & Employment Law > Employment Relationships > Fiduciary Responsibilities

Business & Corporate Law > ... > Directors & Officers > Management Duties & Liabilities > General Overview

#### **HN10** [blue icon] **Management Duties & Liabilities, Causes of Action**

Corporate officers and directors owe fiduciary duties to their employers. The fiduciary duty requires officers and directors to act in good faith, with honesty in fact, with loyalty, in the best interests of the corporation. A claim for breach of fiduciary duty requires a showing of four elements: (1) the existence of a duty; (2) breach of that duty; (3) causation; and (4) damages.

Contracts Law > Contract Interpretation > Fiduciary Responsibilities

Governments > Fiduciaries

Labor & Employment Law > ... > Conditions & Terms > Trade Secrets & Unfair Competition > Trade Secrets

Labor & Employment Law > Employment Relationships > Employment Contracts > Breaches

Labor & Employment Law > ... > Conditions & Terms > Trade Secrets & Unfair Competition > General Overview

Labor & Employment Law > Employment Relationships > Fiduciary Responsibilities

Torts > Business Torts > Commercial Interference > General Overview

Torts > ... > Commercial Interference > Contracts > General Overview

Torts > ... > Contracts > Intentional Interference > Elements

Torts > Business Torts > Unfair Business Practices > General Overview

Torts > Business Torts > Unfair Business Practices > Elements

Torts > Intentional Torts > Breach of Fiduciary Duty > General Overview

Trade Secrets Law > Breach of Contract > General Overview

Business & Corporate Compliance > ... > Trade Secrets Law > Federal Versus State Law > Uniform Trade Secrets Act

Trade Secrets Law > Misappropriation Actions > General Overview

Trade Secrets Law > Misappropriation Actions > Unfair Competition

### **HN11** [💡] **Contract Interpretation, Fiduciary Responsibilities**

Unfair competition is not a tort with specific elements, but instead describes a general category of torts that courts recognize to protect commercial interests. Unfair competition can cover claims such as tortious interference with contract, misuse of trade secrets, and an employee's breach of their fiduciary duties. A claim that asserts nothing more than misappropriation or misuse of a trade secret is displaced by the Minnesota Trade Secrets Act.

Torts > ... > Prospective Advantage > Intentional Interference > Elements

Torts > Business Torts > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

### **HN12** [💡] **Intentional Interference, Elements**

In order to establish a tortious interference with prospective business relations claim, a plaintiff must show that a defendant intentionally and improperly interfered with plaintiffs' prospective business relations. The interference may come about by a defendant inducing a third-party not to enter into or to continue a prospective relation.

Torts > ... > Contracts > Intentional Interference > Elements

Torts > ... > Commercial Interference > Contracts > General Overview

### **HN13** [💡] **Intentional Interference, Elements**

In order to prevail on a tortious interference with contract claim, a plaintiff must demonstrate the existence of a contract, the alleged wrongdoer's knowledge of the contract, and an intentional procurement of its breach, without justification, that results in damage to the plaintiff.

Contracts Law > Contract Interpretation > Fiduciary Responsibilities

Governments > Fiduciaries

Torts > Intentional Torts > Breach of Fiduciary Duty > General Overview

Contracts Law > Breach > General Overview

Labor & Employment Law > Employment Relationships > Employment Contracts > Breaches

Labor & Employment Law > ... > Conditions & Terms > Trade Secrets & Unfair Competition > General Overview

Labor & Employment Law > ... > Conditions & Terms > Trade Secrets & Unfair Competition > Trade Secrets

Torts > Business Torts > Commercial Interference > General Overview

Torts > ... > Commercial Interference > Contracts > General Overview

Torts > Business Torts > Unfair Business Practices > General Overview

Trade Secrets Law > Breach of Contract > General Overview

Trade Secrets Law > Civil Actions > General Overview

Trade Secrets Law > Civil Actions > Questions of Fact

Trade Secrets Law > Misappropriation Actions > Elements of Misappropriation > Existence & Ownership

Trade Secrets Law > Protected Information > Customer Lists

#### **HN14** [ ] **Contract Interpretation, Fiduciary Responsibilities**

A viable tortious interference with contract claim can arise out of a breach of fiduciary duty claim.

Torts > Intentional Torts > Conversion > Elements

Torts > Intentional Torts > Conversion > General Overview

#### **HN15** [ ] **Conversion, Elements**

Under Minnesota law, conversion is defined as an act of willful interference with the personal property of another which is without justification or which is inconsistent with the rights of the person entitled to the use, possession or ownership of the property. Conversion may involve tangible property, or intangible property customarily merged in, or identified with some document.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Criminal Law & Procedure > ... > Bribery > Public Officials > General Overview

Torts > Public Entity Liability > Liability > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

Torts > Intentional Torts > Abuse of Process > Elements

Trade Secrets Law > Federal Versus State Law > **Antitrust Law**

### **HN16[] Noerr-Pennington Doctrine, Sham Exception**

The United States Supreme Court has established that the [First Amendment](#) right to petition includes a litigant's right to bring suit in state or federal court. Under the Noerr-Pennington doctrine, the act of filing a lawsuit is immune from antitrust or tort liability unless it is found to be a mere sham intended to disguise tortious or anti-competitive liability. In the United States Court of Appeals Eighth Circuit, this exception has been further defined as follows: It is only where a defendant's resort to the courts is accompanied or characterized by illegal and reprehensible practices such as perjury, fraud, conspiracy with or bribery of government decision makers, or misrepresentation, or is so clearly baseless as to amount to an abuse of process, that the Noerr-Pennington cloak of immunity provides no protection. The filing of suit will fit within the "sham exception," and will give rise to tort liability, only if "clearly baseless," or if accompanied by perjury, fraud, conspiracy, bribery, misrepresentation, or other "illegal and reprehensible practices." If a court finds a lawsuit to be objectively baseless or without probable cause, then the court may look to the subjective motivation of the party bringing suit to determine whether liability should attach.

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**Judges:** DONOVAN W. FRANK, Judge of United States District Court.

**Opinion by:** DONOVAN W. FRANK

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

#### **Introduction**

The above-entitled matter came before the undersigned United States District Judge on April 15, 2005, pursuant to the Motion for Preliminary Injunction and Motion for Summary Judgment on Defendants' Tortious Interference Counterclaims brought by Plaintiffs and Counter-Defendants Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc. (collectively "Plaintiffs") and the Motions for Summary

Judgment brought by Defendants and Counter-Claimants AXA Investment Mgr. ("AXA"), Frederick Fritz Feuerherm, and Wayne Schmidt (collectively "Defendants"). For the reasons set forth below, the Court grants in part and denies in part Plaintiffs' Motion for Preliminary Injunction and grants *in toto* Plaintiffs' Motion for Summary Judgment on Defendants' Tortious Interference Counterclaims. The Court also grants in part and denies in part Defendants' Motions for Summary Judgment.

## Background

Plaintiffs and Counter-Defendants [\*3] Minnesota Life Insurance Company ("MN Life"), Advantus Capital Management, Inc., ("Advantus"), and Securian Financial Group, Inc. ("Securian") are interrelated companies. MN Life is a wholly-owned subsidiary of Securian and is an affiliate of Advantus. Advantus is MN Life's investment manager and is also a wholly owned subsidiary of Securian.

Defendant and Counter-Claimant AXA is a foreign corporation that is part of the AXA Group based in Paris, France. AXA has an office in Hennepin County and does business in Minnesota.

Defendants and Counter-Claimants Feuerherm and Schmidt ("the Individual Defendants") once worked for Advantus, but now work for AXA. Feuerherm was a member of Advantus' Board of Directors and was an officer of MN Life and Securian. Schmidt was an officer of Advantus. At Advantus, Feuerherm served as vice-president of investment strategy and Schmidt served as portfolio manager. Both men worked in Advantus' Total Return Fixed Income Group ("the Total Return Group"). The Total Return Group managed bond portfolios for MN Life and other institutional clients.

In 2000, AXA made the decision to enter into the U.S. market. Using the name "Western Track," AXA planned to [\*4] buy a company that had an established track record in U.S. investments. AXA determined that it would be better to purchase an on-going concern rather than creating a new company to avoid the three- to five-year period it would take to grow the business and establish a track record. A track record is the official performance of a fund over a period of years. AXA referred to the period of time that it would lack a track record if it was not able to buy an on-going concern as the "credibility gap."

In order to implement Western Track, AXA hired a firm called Warren International to conduct a search for experienced fixed income investment professionals. Jacob Navon, a headhunter for Warren International, led the search. In spring 2003, Navon spoke with the Individual Defendants about the possibility of the two of them leaving Advantus to come to work for AXA. Both men told Navon that they were interested in the possibility of working for AXA.

Over the next few months, Feuerherm, Schmidt, and Navon discussed the possibilities of AXA and Advantus either partnering in a joint venture or of AXA buying Advantus' fixed income business. During the course of these conversations, the Individual [\*5] Defendants disclosed a great deal of information regarding Advantus and MN Life. Feuerherm disclosed to Navon that MN Life had agreed to sell its equity business to Waddell & Reed before this information had been made available to the public. The Individual Defendants also turned over information regarding the composition of the personnel that supported Advantus' total return team, the total return team's source of alpha,<sup>1</sup> client lists, revenue from clients, and performance data. Feuerherm and Schmidt assert that they believed the information they provided to AXA was not confidential. Advantus contends that the information was confidential and that many of the documents that were provided to AXA were stamped "for internal use only."

Feuerherm claims that he believed a potential transaction involving AXA and Advantus would benefit both companies and the members of the Total Return Group. Feuerherm asserts that he discussed a potential transaction [\*6] involving AXA with senior executives at Advantus as early as mid-June 2003. Advantus contends that the discussions between Feuerherm, Schmidt, and AXA were solely aimed at benefitting Feuerherm, Schmidt,

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<sup>1</sup> "Alpha" refers to the ability to add value over a benchmark.

and AXA at the expense of Advantus. Advantus also claims that it was not aware that discussions were taking place between Feuerherm, Schmidt, and AXA until AXA was prepared to make an offer to Advantus.

On April 26, 2003, Schmidt urged AXA to make offers of employment to Feuerherm, Kent Weber, and Steve Nelson, and himself (collectively "the former Advantus employees"). Weber and Nelson were also members of the Total Return Group. In May 2003, Feuerherm advised AXA that Advantus would likely sell its fixed income division to AXA if Feuerherm, Schmidt, Weber, and Nelson were hired by AXA.

On June 18, 2003, the Individual Defendants traveled to Paris to meet with AXA representatives to discuss AXA's proposal regarding the purchase of Advantus' fixed income division. Neither of the Individual Defendants informed Advantus of the purpose of this trip. While meeting with AXA representatives, the Individual Defendants signed confidentiality agreements.

On June 23, 2003, Feuerherm met with [\*7] Robert Senkler, the Chairman, Chief Executive Officer, and President of MN Life and Securian. Feuerherm told Senkler that AXA was prepared to make an offer to buy Advantus' fixed income division. Feuerherm also gave Senkler background information about AXA and its representatives. At this meeting, Senkler agreed to meet with AXA on July 1.

On July 1, 2003, Advantus and AXA representatives met to discuss AXA's proposal. AXA proposed a purchase of Advantus' fixed income division rather than a joint venture between the two parties. Senkler agreed to get back to AXA within two weeks.

On July 10, 2003, Senkler offered Schmidt, Weber, and Nelson significant increases in pay if they remained at Advantus. Senkler also offered to strengthen the business to meet Feuerherm's expectations.

On July 15, 2003, Senkler notified AXA and the total return group that Advantus was rejecting AXA's proposal. Later, Feuerherm, Schmidt, Weber, and Nelson resigned from Advantus. On July 31, 2003, this suit was filed against AXA, Feuerherm, and Schmidt alleging: (1) misappropriation of confidential information; (2) violation of the Minnesota Deceptive Trade Practices Act and the Lanham Act; (3) breach of [\*8] fiduciary duty; (4) breach of duty of loyalty; (5) unfair competition; (6) misappropriation of trade secrets; (7) tortious interference with business advantage; (8) tortious interference with contractual relations; and (9) conversion and civil liability for theft. Plaintiffs request both money damages and injunctive relief.

Plaintiffs contend that they have suffered millions of dollars in damages as a result of Defendants' alleged wrongdoing. Plaintiffs assert they have suffered three types of damages. First, Plaintiffs contend that they lost business for a roughly three-year period because analysts are wary of recommending a firm that has lost senior management or employees. In addition, Plaintiffs assert that they were not selected for any of the bids for which they were finalists.

Second, Plaintiffs contend that Defendants have been unjustly enriched by their use of Advantus' trade secrets and confidential information and their use of Advantus' track record. Plaintiffs contend that AXA's use of the Advantus track record has allowed AXA to land several large accounts.

Third, Plaintiffs assert that they have incurred certain costs as a result of Defendants' alleged misconduct. [\*9] These costs allegedly include the ability to invest in a product that was being created by Feuerherm, restaffing costs, and additional client costs.

Defendants contest each of Plaintiffs' claims. In addition, Defendants brought counterclaims against Plaintiffs for tortious interference alleging that Plaintiffs' claims are baseless and without merit.

## **Discussion**

### **I. Standard of Review**

**HN1** [↑] Summary judgment is proper if there are no disputed issues of material fact and the moving party is entitled to judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#). The court must view the evidence and the inferences that may be reasonably drawn from the evidence in the light most favorable to the nonmoving party. [Enter. Bank v. Magna Bank of Missouri](#), 92 F.3d 743, 747 (8th Cir. 1996). However, as the Supreme Court has stated, "summary judgment procedure is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed 'to secure the just, speedy, and inexpensive determination of every action.'" [Celotex Corp. v. Catrett](#), 477 U.S. 317, 327, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986) [\*10] (quoting [Fed. R. Civ. P. 1](#)).

**HN2** [↑] The moving party bears the burden of showing that there is no genuine issue of material fact and that it is entitled to judgment as a matter of law. [Enter. Bank](#), 92 F.3d at 747. The nonmoving party must demonstrate the existence of specific facts in the record which create a genuine issue for trial. [Krenik v. County of Le Sueur](#), 47 F.3d 953, 957 (8th Cir. 1995). A party opposing a properly supported motion for summary judgment may not rest upon mere allegations or denials, but must set forth specific facts showing that there is a genuine issue for trial. [Anderson v. Liberty Lobby, Inc.](#), 477 U.S. 242, 256, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986); [Krenik](#), 47 F.3d at 957.

## II. Defendants' Motions for Summary Judgment

### A. Misappropriation of Confidential Information (Count I) and Trade Secrets (Count VI)

**HN3** [↑] In order to establish claims for misappropriation of confidential information and trade secrets, a plaintiff must show that: (1) the information is not generally known or ascertainable; (2) the information provides a demonstrable competitive advantage; and (3) the information [\*11] was subject to reasonable efforts to maintain its secrecy. [Cherne Indus., Inc. v. Grounds & Assoc., Inc.](#), 278 N.W.2d 81, 92-93 (Minn. 1979) (stating the standard for common law misappropriation of confidential information claims); [Strategic Directions Group, Inc. v. Bristol-Myers Squibb Co.](#), 293 F.3d 1062, 1064-65 (8th Cir. 2002) (stating the standard for [Minnesota Uniform Trade Secrets Act](#) claims).

Plaintiffs have identified four categories of information that Defendants allegedly have misappropriated, including: (1) financial and client information; (2) marketing information; (3) operational information; and (4) information the Individual Defendants allegedly provided to AXA to assist it in negotiations with Plaintiffs. Plaintiffs claim that all of this information is subject to protection and that they took reasonable efforts to protect the information. Plaintiffs claim three types of damages with regard to this claim and the other claims found in their Amended Complaint: (1) lost profit; (2) unjust enrichment on the part of Defendants; and (3) additional administrative and business costs.

Defendants do not deny that certain information was given [\*12] to AXA by the Individual Defendants. Instead, Defendants contend that none of the information is entitled to protection as it is both readily ascertainable to the general public and Plaintiffs did not take reasonable measures to ensure its secrecy. AXA also claims that it did not know or have reason to know that the information was obtained by improper means or without the Plaintiffs' consent. Finally, Defendants claim that Plaintiffs have not been able to show that they were damaged in any way by AXA's use of the information or that AXA has been unjustly enriched by its access to this information.

The Court finds that Plaintiffs have demonstrated that AXA was provided information by the Individual Defendants. While the Court questions whether much of the information transferred to AXA is entitled to protection, the Court does find that genuine issues of material fact remain with regard to whether the information was readily ascertainable and subject to reasonable measures of protection. The Court also questions the damages, if any, that Plaintiffs suffered as a result of the transfer of this information. Plaintiffs assert that the transfer of information alone led to Advantus' lost [\*13] profits. The Court finds this position to be extremely tenuous. Nonetheless, the Court finds that Plaintiffs have presented sufficient evidence of damages such that fact issues remain with regard to this count of the Amended Complaint.

## B. Violation of the Minnesota Deceptive Trade Practices Act and the Lanham Act (Count II)

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Plaintiffs contend that a July 22, 2003, press release, a document prepared along with that press release ("the Q&A"), and "pitch books" prepared by AXA violate the Lanham Act and the Minnesota Deceptive Trade Practices Act ("MDTPA").<sup>3</sup> [HN4](#)<sup>4</sup> To establish a Lanham Act or MDTPA claim, a plaintiff must demonstrate that: (1) the defendant made a false statement of fact in a commercial advertisement about its own or another's product; (2) the statement actually deceived or has the tendency [\*14] to deceive a substantial segment of its audience; (3) the deception is material; (4) the defendant caused its false statement to enter into interstate commerce; and (5) plaintiff has been or is likely to be injured as a result of the false statement. [United Indus. Corp. v. Clorox Co., 140 F.3d 1175, 1180 \(8th Cir. 1998\)](#). In addition, to recover money damages under the Lanham Act, a plaintiff must prove both actual damages and a causal link between a defendant's actions and those damages. *Id.*

[HN5](#)<sup>5</sup> The false statement necessary to establish a Lanham Act violation generally falls into one of two categories: (1) commercial claims that are literally false as a factual matter; and (2) claims that may be literally true or ambiguous but which implicitly convey a false impression, are misleading in context, or are likely to deceive [\*15] consumers. *Id.* (citing [Southland Sod Farms v. Stover Seed Co., 108 F.3d 1134, 1139 \(9th Cir. 1997\)](#)). In this case, Plaintiffs contend that each of the documents previously mentioned unlawfully linked the former Advantus employees' work performance to the performance of Advantus' fixed income division.

AXA released a press release on June 22, 2003, discussing its hiring of the former Advantus employees and describing the former Advantus employees' success while at Advantus. The press release stated that the former Advantus employees had "produced a consistently strong track record of performance." (Affidavit of David M. Wilk ("Wilk Aff."), P 73, Ex. 75, at 1.)<sup>6</sup> The press release also provided that the former Advantus employees "have demonstrated a proven ability and track record . . ." (*Id.*) The Q&A booklet that was issued with the press release also contained statements attributing Advantus' track record to the former Advantus employees.

[\*16] AXA also produced a number of pitch books that it provided to prospective clients. The pitch books purported to provide a one-, three-, and five-year performance history for AXA's fixed income division. The pitch books showed Advantus' track record up until September 30, 2003, even though the former Advantus employees left the company one month earlier. The pitch book also contained an "Important Disclosure Regarding Past Performance Data." (Wilk Aff, P 79, Ex. 81, at 2.) The disclosure stated that the former Advantus employees were "assisted by a team of analysts and others" and that the Advantus team would be the group handling client accounts at AXA. (*Id.*)

### 1. Literally False Claims

[HN6](#)<sup>7</sup> If a plaintiff is able to prove that a claim is literally false, a court may grant relief without considering whether the buying public was actually misled; the plaintiff need not prove actual consumer confusion. [United Indus., 140 F.3d at 1180](#). In determining whether a claim is literally false, a court must examine the message conveyed within its full context. *Id.* (citing [Rhône-Poulenc Rorer Pharms. v. Marion Merrell Dow, 93 F.3d 511, 516 \(8th Cir. 1996\)](#)). [\*17]

<sup>2</sup> Plaintiffs' Motion for Preliminary Injunction is tied to these claims. Thus, the Court will consider both Plaintiffs' Motion for Preliminary Injunction and Defendants' Motion for Summary Judgment together.

<sup>3</sup> Pitch books are advertising materials containing information about a particular business entity sent to prospective customers by the business entity to solicit business.

<sup>4</sup> Plaintiffs incorrectly delineated their exhibit numbers on the Wilk Affidavit. Accordingly, the Court will cite to the actual exhibit numbers rather than the erroneous numbers contained in the affidavit.

**HN7** In examining whether AXA's use of Advantus' track record is false or misleading, the Court will consider the portability requirements of the Securities & Exchange Commission ("SEC") and the CFA Institute, formerly known as the Association for Investment Management and Research ("AIMR"). See *Surdyk's Liquor, Inc. v. MGM Liquor Stores, Inc.*, 83 F. Supp. 2d 1016, 1022 n.2 (D. Minn. 2000) (citing *Sandoz Pharm. Corp. v. Richardson-Vicks, Inc.*, 902 F.2d 222, 230 (3rd Cir. 1990)). While the Court considers these portability requirements, the burden is still on Plaintiffs to prove that the advertising is false and misleading. *Id.*

**HN8** The SEC's rules state that a registered investment company may not advertise the performance of accounts managed by its portfolio manager at a predecessor firm if other individuals played a significant role in achieving that record. [15 U.S.C. § 80b-6\(4\)](#). CFA Institute has also set forth portability standards. Generally, CFA Institute standards require that a firm's investment decision-making processes remain substantially unchanged in order for a new firm to claim a prior firm's performance record. AIMR-PPS [\*18] Standard 5.A.4.

After reviewing the record, the Court finds that AXA's statements regarding the former Advantus employees' track record are literally false as the statements are presented in the June 22, 2003, press release and the accompanying Q&A booklet. The SEC and CFA Institute place significant restrictions on the ability of firms to use performance records generated by their employees at their former places of business. As previously stated, the Court considers these standards in determining whether a statement or statements are false. In this case, the Court finds that AXA has not complied with the SEC and CFA Institute guidelines with regard to the above-referenced documents. Further, the Court finds that these statements are literally false insofar as they suggest to potential customers that the former Advantus employees were solely responsible for the performance of Advantus' fixed income division.

While the Court finds that the statements in the press release and Q&A booklet were literally false, the Court finds that those same claims are neither literally false nor misleading as presented in the pitch books. In contrast to the press release and the Q&A booklet, the pitch [\*19] books contain a disclosure that explicitly sets out that the former Advantus employees were assisted while at Advantus by a team of additional individuals.

Plaintiffs contend that the disclosure is not conspicuous and is ambiguous concerning the role played by other members of Advantus' fixed income division in the development of Advantus' track record. The Court finds that the disclosure is sufficient to clarify AXA's statements regarding the former Advantus employees' past performance. Thus, the Court finds that summary judgment is appropriate with regard to Plaintiffs' Lanham Act and MDTPA claims insofar as the claims arise out of the pitch books. However, the Court's ruling on this issue is limited in context to the claims before the Court. The SEC, CFA Institute, or other governmental and non-governmental entities may determine that additional action need to be taken with regard to AXA's pitchbooks.

## 2. Statement Actually Deceived or has the Tendency to Deceive

Plaintiffs must also establish that the statements contained in the press release and Q&A booklet were actually or likely deceptive. Plaintiffs can do so by showing that Defendants' statements were either: (1) literally [\*20] false; or (2) likely to mislead or confuse consumers. *Riggs Inv. Mgmt. Corp. v. Columbia Partners, L.L.C.*, 966 F. Supp. 1250, 1268 (D. D.C. 1997). Here, literal falsity has been shown.

**HN9** A plaintiff's burden in a Lanham Act case is, in part, dependent on the relief the plaintiff seeks. A plaintiff that wishes to recover money damages for a violation of the Lanham Act and related state statutes must establish actual confusion among the consumers of the plaintiff's products, actual injury, and a causal connection between the confusion and the injury. *Lenscrafters, Inc. v. Vision World, Inc.*, 943 F. Supp. 1481, 1489 (D. Minn. 1996). In light of the Court's finding that the statements made in the press release and the Q&A booklet were literally false, the Plaintiffs need not make a showing of consumer confusion. *Ott v. Target Corp.*, 153 F. Supp. 2d 1055, 1072 (D. Minn. 2001).

When a plaintiff seeks only injunctive relief, however, it need only prove a likelihood of confusion among consumers that has resulted from defendants' actions. *Id.* In addition, where a defendant has engaged in literally false

advertising, the Court will presume [\*21] that the plaintiff has suffered injury that warrants injunctive relief. *Id.* In this case, Plaintiffs seek both money damages and injunctive relief.

The Court has considered this issue and finds that Plaintiffs have not been able to establish actual confusion among consumers resulting from AXA's press release and Q&A booklet. Nonetheless, the Court finds that granting summary judgment solely on the damages issue would be inappropriate at this time. See [Slidell, Inc. v. Millennium Inorganic Chem., Inc.](#), 2004 U.S. Dist. LEXIS 11738, No. Civ. 02-213 (JRT/FLN), 2004 WL 1447921, at \*4 (D. Minn. June 28, 2004). Instead, the issue would be better considered in the form of a motion *in limine* at some later time.

Based on the Court's finding that AXA engaged in literally false advertising, the Court finds that it need not consider the remaining Lanham Act and MDTPA elements in order to grant Plaintiffs injunctive relief. Specifically, the Court finds that AXA may not link Advantus' track record to itself or the former Advantus employees without an appropriate and conspicuous disclosure. The Court acknowledges that this remedy might not be sufficient in light of SEC or CFA Institute standards, but [\*22] finds that the remedy is sufficient in relation to the Lanham Act and MDTPA claims before the Court.

### C. Breach of Fiduciary Duty (Count III) and Duty of Loyalty (Count IV)

**HN10** [↑] Corporate officers and directors owe fiduciary duties to their employers. [Westgor v. Grimm](#), 318 N.W.2d 56, 58 (Minn. 1982). The fiduciary duty requires officers and directors "to act in good faith, with honesty in fact, with loyalty, in the best interests of the corporation." [Writers, Inc. v. West Bend Mut. Ins. Co.](#), 465 N.W.2d. 419, 423 (Minn. Ct. App. 1991). A claim for breach of fiduciary duty requires a showing of four elements: (1) the existence of a duty; (2) breach of that duty; (3) causation; and (4) damages. [Storage Tech. Corp. v. Cisco Sys., Inc.](#), 2003 U.S. Dist. LEXIS 17347, No. Civ. 00-2253 (JNE/JGL), 2003 WL 22231544, at \*10 (D. Minn. Sept. 25, 2003).

Plaintiffs contend that the Individual Defendants violated their fiduciary duties to Advantus. Specifically, Plaintiffs assert that the Individual Defendants provided Advantus' confidential information to AXA. Plaintiffs also claim that the Individual Defendants assisted AXA in preparing its bid to buy Advantus' fixed income [\*23] division. Plaintiffs claim that each of these acts was against Plaintiffs' interests. Plaintiffs assert that they have suffered millions of dollars in losses as a result of the Individual Defendants' breaches of their fiduciary duties.

The Individual Defendants dispute that they had any fiduciary duties to Defendants or that either of them violated any alleged duties. Nonetheless, the Individual Defendants assert that the Court need not consider these issues as Plaintiffs have failed to submit any evidence of damages resulting from these alleged breaches. The Individual Defendants assert that any confidential information transferred to AXA was done in the best interests of Plaintiffs and did not result in any damages to Plaintiffs. Further, the Individual Defendants contend that the former Advantus employees were free to leave at any time and as such the business disruption that occurred would have happened even in the absence of any alleged breach.

The Court finds that summary judgment is not appropriate as to Plaintiffs' breach of fiduciary duty and loyalty claims. As previously discussed, the Court finds that some of Plaintiffs' business information was transferred to AXA by the [\*24] Individual Defendants. Plaintiffs have also made a showing that the Individual Defendants assisted AXA in preparing its bid to buy Advantus' fixed income division. Although the Court agrees with Defendants that some of Plaintiffs' damages claims are extremely tenuous, the Court finds that Plaintiffs have presented sufficient evidence of damages such that summary judgment is inappropriate.

### D. Unfair Competition (Count V)

**HN11** [↑] Unfair competition is not a tort with specific elements, but instead describes a general category of torts that courts recognize to protect commercial interests. [Rehab. Specialists, Inc. v. Koering](#), 404 N.W.2d 301, 305-06 (Minn. Ct. App. 1987). Unfair competition can cover claims such as tortious interference with contract, misuse of trade secrets, and an employee's breach of their fiduciary duties. See *id.* However, a claim that asserts nothing

more than misappropriation or misuse of a trade secret is displaced by the Minnesota Trade Secrets Act. [SL Montevideo Tech., Inc. v. Eaton Aerospace, LLC, 292 F. Supp. 2d 1173, 1179-80 \(D. Minn. 2003\)](#).

Plaintiffs contend that they have a viable unfair competition claim that is not [\*25] duplicative of their trade secrets claims. Plaintiffs assert that their unfair competition claims cover not only Defendants' actions regarding trade secrets, but also AXA's use of Advantus' track record and AXA's actions in "lifting out" the former Advantus employees. Plaintiffs describe their unfair competition claim as covering Defendants' overall approach to competition. Defendants contend that Plaintiffs' unfair competition is nothing but a trade secrets claim. Thus, Defendants assert that it must be disposed of as duplicative of the Minnesota Trade Secrets Act.

After reviewing Plaintiffs' Amended Complaint, the Court finds that Plaintiffs' unfair competition claim is duplicative of the Minnesota Trade Secrets Act. Plaintiffs attempt to broaden the scope of their claim but the claim remains essentially focused on the trade secrets issues. Thus, the Court finds that summary judgment is appropriate with regard to this claim.

#### **E. Tortious Interference with Business Advantage (Count VII)**

[HN12](#)[] In order to establish a tortious interference with prospective business relations claim, a plaintiff must show that a defendant intentionally and improperly interfered with Plaintiffs' prospective [\*26] business relations. [United Wild Rice, Inc. v. Nelson, 313 N.W.2d 628, 633 \(Minn. 1982\)](#). The interference may come about by a defendant inducing a third-party not to enter into or to continue a prospective relation. *Id.*

Plaintiffs assert that the Individual Defendants coerced AXA to open an office in Minneapolis by providing AXA with Advantus' confidential information. Plaintiffs contend that the former Advantus employees would not have left Advantus without this exchange of information because the former Advantus employees enjoyed living in the Twin Cities area. Plaintiffs claim that they lost one client directly to AXA, lost three clients as a result of the former Advantus employees leaving the company, and lost numerous prospective clients as a result of the mass resignation of its employees.

Defendants assert that this claim is duplicative of Plaintiffs' Minnesota Uniform Trade Secrets Act claim and, therefore, must be dismissed. Defendants point to the fact that the sole allegation in Plaintiffs' Complaint with regard to this claim is that Defendants "wrongfully obtained plaintiffs' trade secrets and confidential proprietary information." (Am. Compl. at P [\*27] 113.)

After reviewing Plaintiffs' Amended Complaint and the rest of the record, the Court finds that Plaintiffs' tortious interference with business advantage claim is duplicative of their Minnesota Uniform Trade Secrets Act claim. Plaintiffs attempt to broaden the scope of their tortious interference with business advantage claim, but it is clear from the Amended Complaint that the trade secrets issue is at the root of this claim. Accordingly, the Court finds that summary judgment in favor of Defendants is appropriate with regard to this claim.

#### **F. Tortious Interference with Contract (Count VIII)**

[HN13](#)[] In order to prevail on a tortious interference with contract claim, the plaintiff must demonstrate the existence of a contract, the alleged wrongdoer's knowledge of the contract, and an intentional procurement of its breach, without justification, that results in damage to the plaintiff. See [Maness v. Star-Kist Foods, Inc., 7 F.3d 704, 709 \(8th Cir. 1993\)](#) (citing [Furlev Sales and Assocs., Inc. v. North American Auto. Warehouse, Inc., 325 N.W.2d 20, 25 \(Minn. 1982\)](#)).

Plaintiffs assert that AXA tortiously interfered with the contracts of Plaintiffs' [\*28] employees and clients. Plaintiffs contend that AXA interfered with Plaintiffs' employee contracts by inducing its employees to breach their fiduciary duties to Plaintiffs. Specifically, Plaintiffs claim that AXA offered the former Advantus employees positions with AXA if they provided AXA with confidential information and assisted AXA in negotiations between AXA and Advantus.

Plaintiffs assert that AXA was, or should have been, aware that engaging the Individual Defendants in these actions would cause the Individual Defendants to breach their fiduciary duties to Plaintiffs. Plaintiffs also contend that AXA tortiously interfered with the contracts of Plaintiffs' clients.

AXA claims that it did not interfere with the at-will employment contracts of the former Advantus employees. AXA asserts that the former Advantus employees did nothing more than prepare to enter into competition with Plaintiffs while they were employed at Advantus. The Individual Defendants claim that they did not breach their fiduciary duties to Plaintiffs and AXA asserts that it is unaware of any such violations if they did occur.

Defendants also contend that they did not interfere with the contracts of Plaintiffs' [\*29] clients. Defendants claim that the only client Plaintiffs lost to AXA was an at-will client that chose to transfer its business to AXA after the former Advantus employees left the company. AXA contends that it secured the contract with this client without interfering in any way with the contract between Advantus and its former client. Defendants contend that any prospective clients that Plaintiffs assert were lost were not under contract with Plaintiffs at the time. Thus, Defendants contend that Plaintiffs' claim fails because there were no contracts to interfere with and Plaintiffs cannot show that, but for AXA, Plaintiffs would have been able to turn these prospects into clients.

The Court finds that Defendants are not entitled to summary judgment as to the portion of Plaintiffs' claim regarding employment contracts, but that summary judgment is appropriate as to the client contract allegations. As previously discussed, the Court finds that genuine issues of material fact exist regarding the trade secret and breach of fiduciary duty claims. [HN14](#) [↑] A viable tortious interference with contract claim can arise out of a breach of fiduciary duty claim. See [\*Storage Tech. Corp. v. Cisco Sys., Inc.\*, 395 F.3d 921, 925 \(8th Cir. 2005\)](#). [\*30] After reviewing the record, the Court finds that genuine issues of material fact exist with regard to this claim.

The Court comes to a different conclusion with regard to Plaintiffs' allegations regarding interference with client contracts. The Court finds that Plaintiffs have not been able to provide the Court with evidence that any of their existing clients breached their contracts with Advantus as a result of the mass-resignation. Further, Plaintiffs have not presented evidence that any of the prospective clients would have contracted with Plaintiffs "but for" AXA's actions. [\*North Central Co. v. Phelps Aero, Inc.\*, 272 Minn. 413, 139 N.W.2d 258, 263 \(Minn. 1965\)](#). Thus, summary judgment is appropriate as to the client contract portion of this claim.

#### G. Conversion and Civil Liability for Theft (Count IX)

[HN15](#) [↑] Under Minnesota law, conversion is defined as "an act of willful interference with the personal property of another which is without justification or which is inconsistent with the rights of the person entitled to the use, possession or ownership of the property." [\*Bloom v. Hennepin County\*, 783 F. Supp. 418, 440 \(D. Minn. 1992\)](#) (quoting [\*Dain Bosworth, Inc. v. Goetze\*, 374 N.W.2d 467, 471 \(Minn. Ct. App. 1985\)](#)). [\*31] Conversion may involve "tangible property, or intangible property customarily merged in, or identified with some document." *Id.*

Plaintiffs contend that Defendants have wrongfully made use of Advantus' trade secrets and track record. Plaintiffs assert that Defendants' use of Advantus' trade secrets and track record constitutes conversion. In contrast, Defendants claim that Advantus' track record is not personal property. Defendants also contend that they have not exercised dominion over Advantus' track record in such a way as to repudiate Plaintiffs' rights in the track record or deprived Plaintiffs of its possession of the track record.

The Court finds that Defendants are entitled to summary judgment on this claim. Insofar as Plaintiffs argue this claim is based on the alleged misuse of Plaintiffs' trade secrets, the claim would appear to be duplicative of the Minnesota Trade Secrets Act. Notwithstanding the Court's finding that the claim is likely duplicative, the Court finds that the trade secrets and the track record at issue are "not the types of intangible property traditionally subject to conversion . . ." See [\*Bloom\*, 783 F. Supp. at 441](#). Thus, the Court [\*32] grants summary judgment as to Plaintiffs' conversion and civil theft claims.

### III. Plaintiffs' Motion for Summary Judgment

Defendants have brought tortious interference counterclaims against Plaintiffs asserting that Plaintiffs' lawsuit is without merit and has been brought solely for the purpose of limiting Defendants' business prospects. Plaintiffs contend that their filing of this suit is protected under the *Noerr-Pennington* doctrine. In [\*Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.\*, 365 U.S. 127, 5 L. Ed. 2d 464, 81 S. Ct. 523 \(1961\)](#), and [\*United Mine Workers of America v. Pennington\*, 381 U.S. 657, 14 L. Ed. 2d 626, 85 S. Ct. 1585 \(1965\)](#), [HN16](#)[<sup>16</sup>] the Supreme Court established that the [\*First Amendment\*](#) right to petition includes a litigant's right to bring suit in state or federal court. Under the *Noerr-Pennington* doctrine, the act of filing a lawsuit is immune from antitrust or tort liability unless it is found to be a mere sham intended to disguise tortious or anti-competitive liability. [\*Noerr\*, 365 U.S. at 140](#). In the Eighth Circuit, this exception has been further defined as follows:

It is only where a defendant's resort to the courts is accompanied or [\*33] characterized by illegal and reprehensible practices such as perjury, fraud, conspiracy with or bribery of government decision makers, or misrepresentation, or is so clearly baseless as to amount to an abuse of process, that the *Noerr-Pennington* cloak of immunity provides no protection. . . . Thus the filing of suit will fit within the "sham exception," and will give rise to tort liability, only if "clearly baseless," or if accompanied by perjury, fraud, conspiracy, bribery, misrepresentation, or other "illegal and reprehensible practices."

[\*Surgidev Corp. v. Eye Tech., Inc.\*, 625 F. Supp. 800, 803 \(D. Minn. 1986\)](#) (following [\*Razorback Ready Mix Concrete Co., Inc. v. Weaver\*, 761 F.2d 484 \(8th Cir. 1985\)](#)) (citations omitted). See also [\*Lund Indus., Inc. v. Westin, Inc.\*, 764 F. Supp. 1342, 1345 \(D. Minn. 1990\)](#) (following same authority). If a court finds a lawsuit to be objectively baseless or without probable cause, then the court may look to the subjective motivation of the party bringing suit to determine whether liability should attach. [\*Prof'l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.\*, 508 U.S. 49, 59, 123 L. Ed. 2d 611, 113 S. Ct. 1920 \(1993\)](#). [\*34] While the *Noerr-Pennington* doctrine arose in the context of the [\*Sherman Act\*](#) and antitrust litigation, the doctrine has been appropriately adopted by courts to apply in other contexts as well.

The Court has reviewed the record and finds that Plaintiffs' suit is neither "objectively baseless," nor "subjectively motivated to harm" Defendants. [\*Prof'l Real Estate Investors\*, 508 U.S. at 59](#). As previously discussed, the Court has granted Plaintiffs injunctive relief with regard to their Motion for Preliminary Injunction and has denied summary judgment on several of Plaintiffs' claims. In light of the Court's findings with regard to these claims, the Court finds that summary judgment is appropriate on Defendants' counterclaims.

### Conclusion

Although the Court has denied summary judgment with regard to some of Plaintiffs' claims, the Court believes that Plaintiffs will have a difficult task in convincing a jury of at least some of their claimed damages. Thus, the Court believes it is in the best interests of the parties to negotiate a resolution of this dispute. As the parties are aware, Magistrate Judge Susan Richard Nelson remains available to assist in the negotiation [\*35] of a settlement should the parties find such services to be helpful. If the Court may be of assistance in this matter, the parties should contact Lowell Lindquist, Calendar Clerk for Judge Donovan W. Frank, at 651- 848-1296, or Beverly Riches, Calendar Clerk for Magistrate Judge Susan Richard Nelson, at 651-848-1200.

For the reasons stated, **IT IS HEREBY ORDERED:**

1. The Motion for Preliminary Injunction (Doc. No. 127) brought by Plaintiffs and Counter-Defendants Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc. is **GRANTED**, as follows:
  - a. Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are enjoined from making commercial statements linking Advantus' track record to themselves without an

appropriate and conspicuous disclosure concerning the role played by other members of Advantus' fixed income division in the development of Advantus' track record.

2. The Motions for Summary Judgment (Doc. Nos. 155 and 162) brought by Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are **GRANTED IN PART AND DENIED IN PART, [\*36]** as follows:

- a. The Motions for Summary Judgment brought by Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are **GRANTED** as to Counts V (Unfair Competition), VII (Tortious Interference with Business Advantage), and IX (Conversion and Civil Liability for Theft).
- b. The Motions for Summary Judgment brought by Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are **DENIED** as to Counts I (Misappropriation of Confidential Information), III (Breach of Fiduciary Duty), IV (Breach of Duty of Loyalty), and VI (Misappropriation of Trade Secrets).
- c. The Motions for Summary Judgment brought by Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are **GRANTED** as to the claims in Count II (Lanham Act and Minnesota Deceptive Trade Practices Act) regarding the pitchbooks, but are **DENIED** as to the claims regarding the press release and Q&A booklet.
- d. The Motions for Summary Judgment brought by Defendants and Counter-Claimants AXA Investment Mgr., Frederick Fritz Feuerherm, and Wayne Schmidt are **GRANTED** as to the claims [\*37] in Count VIII (Tortious Interference with Contract) regarding the customer contracts, but are **DENIED** as to the claims regarding employee contracts.

3. The Motion for Summary Judgment (Doc. No. 150) brought by Plaintiffs and Counter-Defendants Minnesota Life Insurance Company, Advantus Capital Management, Inc., and Securian Financial Group, Inc. is **GRANTED**.

Dated: June 22, 2005

s/Donovan W. Frank

DONOVAN W. FRANK

Judge of United States District Court

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## Am. Express Travel Related Servs. Co. v. Visa U.S.A.

United States District Court for the Southern District of New York

June 23, 2005, Decided

04 Civ. 8967 (BSJ)

### **Reporter**

2005 U.S. Dist. LEXIS 42852 \*; 2005 WL 1515399

AMERICAN EXPRESS TRAVEL RELATED SERVICES COMPANY Plaintiff, v. VISA U.S.A., et al., Defendants.

**Subsequent History:** Motion denied by [\*Discover Fin. Servs. v. Visa U.S.A., Inc., 2005 U.S. Dist. LEXIS 62687 \(S.D.N.Y., Nov. 9, 2005\)\*](#)

Motion denied by [\*Am. Express Travel Related Servs. Co. v. Visa U.S.A., 2005 U.S. Dist. LEXIS 63179 \(S.D.N.Y., Nov. 10, 2005\)\*](#)

Motion denied by [\*Discover Fin. Servs. v. Visa U.S.A., 2006 U.S. Dist. LEXIS 22097 \(S.D.N.Y., Apr. 17, 2006\)\*](#)

Objection overruled by, Decision reached on appeal by [\*Discover Fin. Servs. v. Visa U.S.A., Inc., 2006 U.S. Dist. LEXIS 116536 \(S.D.N.Y., Aug. 2, 2006\)\*](#)

## **Core Terms**

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conspiracy, antitrust, terminate, banks, motion to dismiss, horizontal, terminable at will, member bank, Defendants', allegations, merchant, cards, restraint of trade, forecloses, supplier, concerted action, anti trust law, district court, buyers, brand

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**Judges:** BARBARA S. JONES, UNITED STATES DISTRICT JUDGE.

**Opinion by:** BARBARA S. JONES

## **Opinion**

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**BARBARA S. JONES**

**UNITED STATES DISTRICT JUDGE**

American Express ("Plaintiff") brings a claim against both named and unnamed defendants for allegedly conspiring "to extend and perpetuate the effects of their [\*4] exclusionary rules, found unlawful by this Court, by agreeing to adopt and implement exclusive dealing arrangements with certain member banks." (Compl. at P160.) Plaintiff claims that these exclusive dealing arrangements violate [§ 1](#) of the Sherman Act, which prohibits, in relevant part, "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States." [15 U.S.C. § 1](#).

Both parties acknowledge that various members of Visa U.S.A., Inc. ("Visa") and MasterCard Incorporated ("MasterCard"), have entered into exclusive dealing arrangements ("EDAs") with Visa and MasterCard. Plaintiff describes the EDAs as

multi-year contracts, extending up to ten years in duration, which obligate member banks to dedicate themselves to issuing all new cards with the association with which they have contracted, and requiring among other things that within a short period of time, such banks issue 80% to 90% of their general purpose cards as the contracting association's card."

(Compl. at P160.)

The banks named as defendants (collectively, the "Bank Defendants") have moved to dismiss Plaintiff's [\*5] fifth claim pursuant to [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) insofar as it relies on the EDAs. The Bank Defendants present two grounds for dismissal:

(1) Plaintiff fails to make out a claim of a horizontal conspiracy, and therefore cannot aggregate each EDA's market foreclosure amount to arrive at a figure large enough to ground an exclusive dealing claim. Because it relies on a theory of horizontal conspiracy, Plaintiff has failed to plead that any individual Bank Defendant's EDA forecloses a sufficient share of the market to violate [§ 1](#).

(2) The EDAs do not last for the extended period of time required for an exclusive dealing claim.

After reviewing the standard on a motion to dismiss, the Court will consider these arguments in turn.

### **Standard on a Motion to Dismiss**

When considering a motion to dismiss under [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) for "failure to state a claim upon which relief can be granted," a district court must accept the allegations contained in the complaint as true and draw all reasonable inferences in favor of the non-moving party. [Burnette v. Carothers, 192 F.3d 52, 56 \(2d Cir. 1999\)](#). The Court "may [\*6] dismiss the complaint only if it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Id.*(citing [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#)).

In the context of antitrust cases, motions to dismiss "prior to giving the plaintiff ample opportunity for discovery should be granted very sparingly." [George Haug Co., Inc. v. Rolls Royce Motor Cars Inc., 148 F.3d 136, 139 \(2d Cir. 1998\)](#) (quoting [Hosp. Building Co. v. Trustees of Rex Hosp., 425 U.S. 738, 746, 96 S. Ct. 1848, 48 L. Ed. 2d 338 \(1976\)](#)). Thus while an antitrust plaintiff must "adequately define the relevant product market, . . . allege antitrust injury, [and] . . . allege conduct in violation of the antitrust laws," [Sage Realty Corp. v. ISS Cleaning Servs. Group, 936 F. Supp. 130, 135](#) (quoting [Re-Alco Indus. v. Nat'l Ctr. for Health Educ., 812 F. Supp. 387, 391 \(S.D.N.Y. 1993\)](#)), it faces "no greater [burden] than the [one] faced by a plaintiff alleging any cause of action not covered by the specific pleading requirements of [Rule 9 of the Federal \[\\*7\] Rules of Civil Procedure](#)." [Gross v. New Balance Athletic Shoe, Inc., 955 F. Supp. 242, 244 \(S.D.N.Y. 1997\)](#).

### **Discussion**

In the most general terms, [e]xclusive dealing arrangements require a buyer to purchase products or services for a period of time exclusively from one supplier." ABA SECTION ON [ANTITRUST LAW](#), 1 [ANTITRUST LAW DEVELOPMENTS](#) 214 (5th ed. 2002). Such agreements

may, in some circumstances, create or extend market power of a supplier or the purchaser party to the exclusive-dealing arrangement, and may thus restrain horizontal competition. Exclusive dealing can have adverse economic consequences by allowing one supplier of goods or services unreasonably to deprive other suppliers of a market for their goods, or by allowing one buyer of goods unreasonably to deprive other buyers of a needed source of supply.

[Jefferson Parish Hospital Dist. No. 2 v. Hyde, 466 U.S. 2, 45, 104 S. Ct. 1551, 80 L. Ed. 2d 2 \(1984\)](#). On the other hand, exclusive dealing arrangements can promote healthy markets; for buyers they "may assure supply, afford protection against rises in price, enable long-term planning on the basis of known costs, [\*8] and obviate the expense and risk of storage in the quantity necessary for a commodity having a fluctuating demand." [Standard Oil v. United States, 337 U.S. 293, 306-07, 69 S. Ct. 1051, 93 L. Ed. 1371 \(1949\)](#). By the same token, for sellers, exclusive dealing agreements "may make possible the substantial reduction of selling expenses, give protection against price fluctuations, and . . . offer the possibility of a predictable market . . . They may be useful, moreover, to a seller trying to establish a foothold against the counterattacks of entrenched competitors." *Id. at 307*.

In [Standard Oil](#), the Supreme Court applied what has been labeled the "quantitative substantiality test" to the government's exclusive dealing claims against Standard Oil, focusing almost exclusively on the amount of the market foreclosed by Standard Oil's exclusive dealing arrangements with various independent gas stations. *Id. at 314*. The Supreme Court later decided [Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 334, 81 S. Ct. 623, 5](#)

L. Ed. 2d 580 (1961),<sup>1</sup> where it reaffirmed the pro-competitive potential of exclusive dealing agreements and applied [\*9] a qualitative test to the plaintiff's exclusive dealing claim. The Supreme Court cited the following considerations:

structure of the market for the products or services in question . . . the probable effect of the contract on the relevant area of effective competition, taking into account the relative strength of the parties, the proportionate volume of commerce involved in relation to the total volume of commerce in the relevant market area, and the probable immediate and future effects which pre-emption of that share of the market might have on competition therein.

Tampa Elec., 365 U.S. at 329.

[\*10] Since Tampa Elec., exclusive dealing agreements are "judged under the Rule of Reason, and [are] condemned only if found to restrain trade unreasonably." Roland Machinery Co. v. Dresser Industries, Inc., 749 F.2d 380, 393 (7th Cir. 1984). Thus "in order not to condemn the positive aspects of exclusive dealing agreements, courts must take care to consider the competitive characteristics of the relevant market." Geneva Pharms. Tech. Corp. v. Barr Labs., Inc., 386 F.3d 485, 508 (2d Cir. 2004). See also Am. Motor Inns, Inc. v. Holiday Inns, Inc., 521 F.2d 1230, 1251 (3d Cir. 1975) (Courts must therefore conduct a "broad inquiry," in order to "take into account the economic justification for the arrangement").

An additional factor to those cited by the Supreme Court in Tampa Elec. is "the duration and terminability of the arrangement: the shorter an agreement's term and the easier it is to terminate, the more likely that it will be upheld . . . In fact, courts increasingly view at-will exclusive arrangements as presumptively valid." 3M v. Appleton Papers Inc., 35 F. Supp. 2d 1138, at 1143. Other relevant considerations include [\*11] "ease of entry" into the market, "the extent to which competitors also employ exclusive dealing arrangements, the relationship between the parties to the exclusive dealing arrangement, and the extent to which competition is actually injured." ABA SECTION ON ANTITRUST LAW, 1 ANTITRUST LAW DEVELOPMENTS 224-25. (5th ed. 2002).

Nonetheless, even after Tampa Elec., the degree to which an agreement forecloses the market remains arguably the most important factor in determining whether the agreement violates § 1. In Jefferson Parish, the most recent exclusive dealing case to reach the Supreme Court, the Court held that "[e]xclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal." Jefferson Parish, 466 U.S. at 45. Generally speaking, cases construing Jefferson Parish have held that an agreement must foreclose at least 30 percent to 40 percent of the market to support a § 1 violation, and one treatise

<sup>1</sup> In Tampa Elec., the Supreme Court addressed the plaintiff's claims brought under § 3 of the Clayton Act. That section provides:

It shall be unlawful for any person . . . to . . . make a sale or contract for sale of goods . . . on the condition, agreement, or understanding that the . . . purchaser thereof shall not use or deal in the goods . . . of a competitor or competitors of the . . . seller, where the effect of such . . . sale, or contract for sale or such condition, agreement, or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.

15 U.S.C. § 14. Plaintiff here has not asserted a claim under § 3 based on the EDAs, presumably because § 3 reaches only arrangements dealing with "goods, wares, merchandise, machinery, supplies or other commodities," which are not at issue here. Id. The Court notes that in Tampa Elec., the Supreme Court stated that if an exclusive dealing arrangement "does not fall within the broader proscription of § 3 of the Clayton Act it follows that it is not forbidden by those of the [Sherman Act]." Tampa Elec., 365 U.S. at 335 (citing Times-Picayune Pub. Co. v. United States, 345 U.S. 594, 608-609, 73 S. Ct. 872, 97 L. Ed. 1277 (1953)).

Professor Hovenkamp explains that "a few courts have followed the rule suggested in Times-Picayune of applying a more aggressive test under the Clayton Act than under the Sherman Act, but most apply the same test under both statutes . . . Nevertheless, the cases are divided, with a likely majority stating that the Clayton Act requires a smaller showing of anticompetitive effects." Herbert Hovenkamp, Antitrust Law 2d P1800c4 (2005). See also Twin City Sportservice, Inc. v. Charles O. Finley & Co., 676 F.2d 1291, 1304 (9th Cir. 1982) ("a greater showing of anticompetitive effect is required to establish a Sherman Act violation than a section 3 Clayton Act violation in exclusive-dealing cases").

advises that there thus exists a "virtual safe harbor . . . for market foreclosure of 20 percent or less." ABA SECTION ON ANTITRUST LAW, 1 ANTITRUST LAW DEVELOPMENTS [\*12] 222 (5th ed. 2002). See, e.g., T.A.M., Inc. v. Gulf Oil Corp., 553 F. Supp. 499, 505 (E.D.Pa. 1982); Minnesota Mining and Manuf. Co. v. Appleton Papers Inc., 35 F. Supp. 2d 1138, 1143 (D.Minn. 1999); United States v. Microsoft Corp., No. 98-1232, 1998 U.S. Dist. LEXIS 14231, at \*61 (D. D.C. 1998).

### ***The Bank Defendants' Motion to Dismiss***

With these general standards in mind, the Court turns to the issues raised by the Bank Defendants' motion to dismiss. The Bank Defendants' primary attack is that Plaintiff fails to state a claim for a horizontal conspiracy among the defendants, and therefore "may not aggregate the effects of all of the Visa or MasterCard dedication agreements in asserting an exclusive dealing claim against an individual bank." (D. Mem. at 5.) The Bank Defendants also argue for dismissal of the exclusive dealing claim because, pursuant to the Court's opinion in United States v. Visa U.S.A., Inc., 183 F. Supp. 2d 613 (S.D.N.Y. 2001), the EDAs are terminable at will, and therefore will not last the extended period of time required for an exclusive dealing claim.

### ***Horizontal Conspiracy***

[\*13] Plaintiff faces no additional pleading requirements by virtue of the fact that this is an antitrust case. Indeed, "a short plain statement of a claim for relief which gives notice to the opposing party is all that is necessary in antitrust cases, as in other cases under the Federal Rules." George C. Frey Ready-Mixed Concrete, Inc. v. Pine Hill Concrete Mix Corp., 554 F.2d 551, 554 (2d Cir. 1977). To make out a § 1 conspiracy claim, a plaintiff must allege three things: "(1) concerted action, (2) by two or more persons that (3) unreasonably restrains trade." In re Nine West Shoes Antitrust Litigation, 80 F. Supp. 2d 181, 190 (S.D.N.Y. 2000).

The Bank Defendants argue that Plaintiff has failed to satisfy its obligation to "do more than merely allege that a conspiracy exists," but rather "provide some factual basis for that allegation." Granite Partners, L.P. v. Bear, Stearns & Co., 58 F. Supp. 2d 228, at 238. The Bank Defendants argue that as a result, for the Court to find that Plaintiff states a claim for horizontal conspiracy, it must adopt a "walking conspiracy" view of the Association Defendants.

Under a walking conspiracy theory, every action undertaken [\*14] by either Visa or MasterCard would be the equivalent of concerted action by each individual member. But the Second Circuit has rejected the concept of "membership-ratification theory as a basis for antitrust conspirator liability," holding that "every action by a trade association is not concerted action by the association's members." AD/SAT v. Associated Press, 181 F.3d 216, 234 (2d Cir. 1999) (citing Willk v. Am. Medical Ass'n, 671 F. Supp. 1465, 1492 (N.D. Ill. 1987), aff'd, 895 F.2d 352 (7th Cir. 1990)). The Second Circuit reasoned that "a finding of concerted action based on the defendants' status as members of the [association] would seriously undermine the standards articulated by the Supreme Court in Matsushita and Monsanto." Id. (citing Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986) and Monsanto Co. v. Spray-Rite Service Corp., 465 U.S. 752, 104 S. Ct. 1464, 79 L. Ed. 2d 775 (1984)). Under Matsushita and Monsanto, "an antitrust plaintiff must present evidence tending to show that association members, in their individual [\*15] capacities, consciously committed themselves to a common scheme designed to achieve an unlawful objective." Id. The Second Circuit therefore rejected the use of "a 'walking conspiracy' theory in place of such a showing." Id.

The Bank Defendants also rely on Kendall v. Visa, U.S.A., Inc., 2005 U.S. Dist. LEXIS 21449, No. 04 Civ. 4276 (JSW) (N.D. Cal. 2005), where Judge White recently dismissed the plaintiffs' § 1 claims against two member banks of Visa and MasterCard,<sup>2</sup> because their complaint made "no allegations that, as part of the Bank Defendants' participating in the management of, or their proprietary interest in, VISA or MASTERCARD, the Bank Defendants

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<sup>2</sup> The plaintiffs in Kendall alleged that the associations' setting of merchant discount fees constitutes a horizontal price fixing arrangement in violation of § 1.

'knowingly, intentionally and actively participated in an individual capacity in the alleged scheme' to fix the interchange fee or merchant discount fee." *Kendall v. Visa, U.S.A., Inc., 2005 U.S. Dist. LEXIS 21449, No. 04 Civ. 4276 (JSW), at 3-4 (N.D. Cal. 2005)*. Having reviewed the complaint from *Kendall*, the Court finds that it is indeed devoid of any mention of the individual defendants' intentional involvement in the horizontal price-fixing scheme allegedly orchestrated by them, Visa and MasterCard. The only allegations the *Kendall* plaintiffs directed towards [\*16] the member banks were that the banks "obtain supracompetitive profits by assessment of merchant discount fees on the deposits of Plaintiffs," and that "member banks of both VISA and MASTERCARD find it economically to their advantage not to opt out of systems which establish a non-competitive merchant discount." (Kendall Compl. at PP10, 11.)

By contrast, Plaintiff here alleges that the Bank Defendants engaged in concerted action to exclude Plaintiff from the relevant market. The complaint alleges that the Bank Defendants, "in collaboration with" the Association Defendants and other unnamed member banks, have supported the EDAs, and that they do so "because they receive the benefit of continuing the elimination of competition among each other based upon the actual or potential issuance of American Express general purpose cards by competing banks. [\*17]" (Compl. at PP161, 160.) At oral argument, counsel for Plaintiff clarified that when it alleges that banks have "supported" other member banks' EDAs, it means that those banks "have voted for the procedure of the dedication agreements, and have voted to subsidize those agreements." (4/14/05 Tr. at 60.) Thus even banks without EDAs participate in the conspiracy to restrain trade "by agreeing to subsidize those banks that do, because it has the effect of continuing the horizontal constraint." *Id.* at 61. The unreasonable restraint of trade, according to the complaint, consists of "the harm to competition caused by the continuing boycott of American Express," a harm that outweighs any benefits accruing from "competition between Visa and MasterCard to sign member banks" to EDAs. (Compl. at P162.) Finally, the complaint alleges that the EDAs "foreclose a substantial volume of commerce from free and open competition." (Compl. at P163.)

Based on these allegations, the Court cannot conclude that Plaintiff can prove no set of facts in support of its claim that the Bank Defendants each "consciously committed themselves to a common scheme designed to achieve an unlawful objective," here, [\*18] the boycott of American Express through a restraint of trade. *AD/SAT v. Associated Press, 181 F.3d at 234*. Plaintiff has satisfied the pleading requirements for a horizontal conspiracy under § 1, and does so without relying on the "walking conspiracy" theory rejected by the Second Circuit.<sup>3</sup> Plaintiff therefore need not allege that any individual EDA forecloses enough of the relevant market to violate that section. Accordingly, the Bank Defendant's motion to dismiss the exclusive dealing claim based on market foreclosure is denied.

### ***The Terminability of the Exclusive Dealing Arrangements***

The Bank [\*19] Defendants also argue for dismissal of Plaintiff's exclusive dealing claims based on the fact that according to the Court's order in *United States v. Visa U.S.A., Inc., 183 F.Supp.2d 613 (S.D.N.Y. 2001)*, the EDAs are terminable at will by the member banks. That order provides the following injunctive relief:

In the event that any issuing member enters into an agreement to issue American Express or Discover brand payment cards on those respective networks . . . Defendants Visa U.S.A. and MasterCard shall permit that issuer to terminate, without penalty, any agreement it entered into with that Defendant prior to the effective date of this Final Judgment, pursuant to which the issuer committed to maintain a certain percentage of its general purpose card volume, new card issuance or total number of cards in force in the United States on that Defendant's network.

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<sup>3</sup>Because the Court finds that Plaintiff has stated a claim for a horizontal conspiracy, it does not reach the issue of whether, without such a conspiracy, Plaintiff can aggregate the portion of the market foreclosed by each individual EDA in order to show that a "significant fraction of buyers and sellers are frozen out of a market." *Jefferson Parish, 466 U.S. at 45*.

*United States v. Visa, U.S.A., Inc., 183 F. Supp. 2d at 618.* The Bank Defendants point to case law upholding exclusive dealing arrangements with "reasonable termination provisions," arguing that because the Court's injunction allows banks to terminate their EDAs at will, Plaintiff's [\*20] exclusive dealing claim fails as a matter of law. (Def. Br. at 6.)

The Bank Defendants rely primarily on *Balaklaw v. Lovell, 14 F.3d 793 (2d Cir. 1994)*, where the Second Circuit rejected the plaintiff's exclusive dealing claim. In *Balaklaw*, the plaintiff, an anesthesiologist, claimed that a hospital "violated the Sherman Act by entering into an exclusive contract with a group of anesthesiologists of which Dr. Balaklaw was not a member." *Balaklaw, 14 F.3d at 795*. The Second Circuit dismissed this claim because it found no "foreclosure of competition" and therefore no antitrust injury. *Id.* Under the agreement at issue, the hospital "was free at the end of six months to enter into a new arrangement with either [the current group] or with any other anesthesiologist." *Id.* The court explained that "[s]uch a situation may actually encourage, rather than discourage, competition, because the incumbent and other, competing anesthesiology groups have a strong incentive continually to improve the care and prices they offer in order to secure the exclusive positions." *Id.*

As in *Balaklaw*, agreements "providing short notice for termination" [\*21] are often upheld. ABA SECTION ON **ANTITRUST LAW**, 1 **ANTITRUST LAW** DEVELOPMENTS 225 (5th ed. 2002). See, e.g., *Western Parcel Express v. UPS of Am., 190 F.3d 974, 976 (9th Cir. 1999)* (rejecting the plaintiff's exclusive dealing claim in part because "the challenged contracts had termination provisions that allowed a customer to terminate the contract for any reason with very little notice"); *CDC Techs., Inc. v. IDEXX Lab., Inc., 186 F.3d 74, 81 (2d Cir. 1999)* (finding it "highly significant" that the exclusive dealing agreements at issue "were easily terminable on short notice" in rejecting plaintiff's exclusive dealing claim).

An agreement's duration, however, is not dispositive of whether it violates § 1. Indeed, courts have held that even if an exclusive dealing contract is terminable at will, it can still operate as an unreasonable restraint on trade. For example, in *Minnesota Mining & Manuf. Co. v. Appleton Papers, Inc., 35 F. Supp. 2d 1138 (D.Minn. 1999)* ("3M"), the district court denied the defendant's motion for summary judgment on an exclusive dealing claim, despite the fact that the agreements at issue, "sole-source" [\*22] relationships between the defendant and various paper merchants, were terminable at will. The complaint alleged that by "saturating local markets with these agreements," the defendant "increased its market share by blocking its rivals' avenues of distribution." *3M, 35 F. Supp. 2d at 1140*. In its motion for summary judgment, the defendant argued that because the agreements were terminable at will, its competitors remained "free to attempt to convert exclusive distributors," and therefore the agreements did not violate § 1. *Id. at 1144.*

Citing *Tampa Elec., supra*, the district court focused on "the 'practical effect' of the agreement, not merely its form," and found a genuine issue of fact as to whether or not the agreements were indeed terminable at will. The plaintiff pointed to evidence indicating that the "agreements often include incentives that have the practical effect of tying up the paper sheet inventory of a merchant over a period of several years." *Id.* Moreover, there existed "unique distribution factors, like the high costs a paper merchant must incur to switch completely from one brand to another, that make it very [\*23] difficult for a supplier to dislodge a competitive brand from an exclusively dealing merchant." *Id.* There was also evidence that the defendant's "high market share and the deeply rooted customer preference for [its] brand of paper prevent merchants from surrendering [the defendant] as a supplier, which they must do under these agreements if they desire to distribute non-Appleton brands." *Id.* Finally, "major distributors have agreed among themselves that they will remain loyal to Appleton carbonless sheets regardless of competitors' pricing or product innovations." *Id.* Based on these four showings, the district court denied the defendant's motion for summary judgment on the plaintiff's exclusive dealing claims. See also *United States v. Dentsply Int'l, Inc., 2001-1 Trade Cas. (CCH) P73,247 (D. Del. 2001)* (denying summary judgment motion on exclusive dealing claims despite the fact that the agreements at issue were terminable at will).

Plaintiff argues that similarly, the "practical effect" of the EDAs is to bind individual member banks to a particular Visa or MasterCard for longer than permitted by the Court's order in *United States v. Visa*. Plaintiff [\*24] explains that "[d]islodging banks from dedication agreements is likely to be particularly difficult where, as here, the parties

who have conspired so effectively and for so long to boycott American Express will necessarily have a continuing incentive to accomplish the same end by other means." (P. Opp. at 11.)

The Court agrees that dismissal would be inappropriate based on the terminability of the EDAs because it remains to be seen whether the EDAs are, in fact, terminable at will. The practical ramifications considered by the court in 3M are important ones, even more so given that the motion before the Court is one to dismiss on the pleadings, rather than one for summary judgment. Moreover, under the rule of reason analysis applicable to Plaintiff's exclusive dealing claim, "the factfinder weighs all of the circumstances of a case in deciding whether a restrictive practice should be prohibited." K.M.B. Warehouse Distrib. v. Walker Mfg. Co., 61 F.3d 123, 127 (2d Cir. 1995) (quoting Continental T. V. v. GTE Sylvania, 433 U.S. 36, 49, 97 S. Ct. 2549, 53 L. Ed. 2d 568 (1977)). Therefore a single factor - the terminability of the agreements [\*25] - cannot outweigh all the other factors the Court must consider, particularly not at this early pleading stage. See Am. Motor Inns, Inc. v. Holiday Inns, Inc., 521 F.2d 1230 at 1252 (reversing where the district court failed to engage in the "broad inquiry" required under Tampa Elec.). Accordingly, the Bank Defendants' motion to dismiss Plaintiff's exclusive dealing claim based on the terminability of the EDAs is denied.

## Conclusion

For the reasons stated above, the Bank Defendants' motion to dismiss Plaintiff's fifth claim for restraint of trade, grounded on the EDAs, is denied.

## SO ORDERED:

BARBARA S. JONES

UNITED STATES DISTRICT JUDGE

Dated: New York, New York

June 23, 2005

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## Tippecanoe Assocs. II, LLC v. Kimco Lafayette 671, Inc.

Supreme Court of Indiana

June 23, 2005, Decided

No. 79S05-0506-CV-289

### **Reporter**

829 N.E.2d 512 \*; 2005 Ind. LEXIS 564 \*\*

TIPPECANOE ASSOCIATES II, LLC, Appellant (Defendant below), v. KIMCO LAFAYETTE 671, INC., Appellee (Plaintiff below).

**Prior History:** [\*\*1] Appeal from the Tippecanoe Superior Court, No. 79D02-0112-CP-249. The Honorable Thomas H. Busch, Judge. On Petition To Transfer from the Indiana Court of Appeals, No. 79A05-0302-CV-85.

[Tippecanoe Assocs. II, LLC v. Kimco Lafayette 671, Inc., 811 N.E.2d 438, 2004 Ind. App. LEXIS 1272 \(Ind. Ct. App., 2004\).](#)

**Disposition:** Trial court's declaratory judgment affirmed.

## **Core Terms**

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covenant, restrictive covenant, shopping center, tenant, lease, grocery store, competitors, antitrust, unenforceable, promisee, space, site, trial court

## **LexisNexis® Headnotes**

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Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Covenants

Real Property Law > Encumbrances > Restrictive Covenants > General Overview

Real Property Law > ... > Lease Agreements > Commercial Leases > General Overview

Real Property Law > ... > Lease Agreements > Commercial Leases > Shopping Center Leases

### **HN1[ Types of Contracts, Covenants**

A covenant given by a shopping center to a tenant prohibiting the center from leasing to competitors of the tenant is generally enforceable. However, once the tenant or its successor voluntarily relinquishes the original use of the site, the anticompetitive covenant is severed from the occupancy and no longer enforceable to give the tenant or an assignee the right to restrict competition for a location outside the center.

829 N.E.2d 512, \*512L2005 Ind. LEXIS 564, \*\*1

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Covenants

Contracts Law > Types of Contracts > Lease Agreements > General Overview

Real Property Law > Landlord & Tenant > Lease Agreements > Lease Provisions

Real Property Law > ... > Lease Agreements > Commercial Leases > General Overview

Real Property Law > ... > Lease Agreements > Commercial Leases > Shopping Center Leases

Real Property Law > Encumbrances > Restrictive Covenants > General Overview

## **HN2** [down] **Types of Contracts, Covenants**

Indiana law permits restrictive covenants but finds them disfavored and justified only to the extent they are unambiguous and enforcement is not adverse to public policy. Doubts should be resolved in favor of the free use of property and against restrictions. Courts have been quite willing to enforce restrictive covenants written in shopping center lease contracts even though they prevent competition within the center. Rather than restricting competition, such covenants serve to facilitate trade and induce tenants to rent in a particular shopping center. Restrictive covenants in shopping center leases have, for the most part, been found not to restrain competition unreasonably and have been generally found to be consistent with the public interest.

Governments > Legislation > Overbreadth

Real Property Law > Encumbrances > Restrictive Covenants > General Overview

## **HN3** [down] **Legislation, Overbreadth**

A restraint may be unreasonable in either of two situations. The first occurs when the restraint is greater than necessary to protect the legitimate interests of the promisee. The second occurs when, even though the restraint is not greater than necessary to protect those interests, the promisee's need for protection is out-weighed by the hardship to the promisor and the likely injury to the public. Usually if a restriction is unenforceable it is because it prohibits an overbroad type of activity by the promisor.

Antitrust & Trade Law > Sherman Act > General Overview

Real Property Law > ... > Lease Agreements > Commercial Leases > Shopping Center Leases

## **HN4** [down] **Antitrust & Trade Law, Sherman Act**

Under the Sherman Act, the issue is whether there is an adverse effect on competition. In a Sherman Act action, the proper inquiry is whether there has been an actual adverse effect on competition as a whole in the relevant market.

**Counsel:** FOR APPELLANT: Charles R. Vaughan, Linda H. Havel, Lafayette, Indiana.

FOR APPELLEE: Stephen R. Pennell, William P. Kealey, Lafayette, Indiana.

**Judges:** Boehm, Justice. Dickson and Rucker, JJ., concur. Sullivan, J., dissents with separate opinion in which Shepard, C.J., joins.

**Opinion by:** Boehm

## Opinion

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### [\*512] Boehm, Justice.

We hold that **HN1** a covenant given by a shopping center to a tenant prohibiting the center from leasing to competitors of the tenant is generally enforceable. However, [\*513] once the tenant or its successor voluntarily relinquishes the original use of the site, the anticompetitive covenant is severed from the occupancy and no longer enforceable to give the tenant or an assignee the right to restrict competition for a location outside the center.

### Facts & Procedural History

In 1973, SES Development Company leased one of the stores in its Sagamore shopping center to Kroger Company for an initial term of twenty years, with four options to renew [\*2] the lease, each for a term of five years.<sup>1</sup> The lease contained a restrictive covenant preventing SES from leasing space in the shopping center to another grocery store. Kroger operated a supermarket at the leased premises until 1982. In 1983, Kroger closed all three of its Tippecanoe County stores and assigned their leases to Pay Less Super Markets, Inc., which at the time operated two other grocery stores within two miles of the Sagamore Center.<sup>2</sup> After the assignment, Pay Less opened stores in two of the former Kroger sites, but Pay Less cheerfully concedes that it never intended to operate a grocery store in the Sagamore Center and acquired the Sagamore lease for the purpose of excluding competitors of its nearby stores. In 1984, Pay Less subleased its Sagamore space to H.H. Gregg, an appliance dealer, who remains in that location today.<sup>3</sup> The defendant, Tippecanoe Associates II, LLC, is a limited liability company owned by the family controlling Pay Less and the current holder of the Sagamore leasehold interest Pay Less acquired from Kroger. Tippecanoe acquired the lease in a series of maneuvers and seeks to enforce this thirty-year-old covenant against the current owner of [\*3] the center, Kimko Lafayette 671, Inc.,<sup>4</sup> even though there has been no grocery store in the center since 1982.

In 2000, another large tenant, Target, left Sagamore Center, leaving nearly one-half of the center's space unoccupied. Kimco contends that the only prospective tenant to fill the void caused by Target's departure is Schuncks, a Missouri-based operator of grocery stores. Kimco filed a complaint asking the trial court to declare [\*4] the restrictive covenant unenforceable. After a hearing the trial court granted Kimco's request, reasoning that "the use of the property and the surrounding area have changed so radically . . . that the original purpose of the covenant can no longer be achieved."

The Court of Appeals reversed, concluding that Tippecanoe's lease of the space to an appliance store and the empty space resulting from the Target move are not sufficient changes in the covenant to support invalidating the restrictive covenant. *Tippecanoe Assoc. II, LLC v. Kimco Lafayette 671, Inc.*, 811 N.E.2d 438, 448-49 (Ind. Ct. App. 2004). The result is that Tippecanoe, which operates grocery stores within a few miles of the center, is allowed to enforce a restrictive covenant that neither benefits the shopping center nor Tippecanoe's interest in the shopping center [\*514] (its sublease to H.H. Gregg). We now grant transfer.

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<sup>1</sup> In 1974, the lease was amended by a lease modification agreement to provide that the initial lease began on June 1, 1974 and ended on May 31, 1994.

<sup>2</sup> The record is not clear as to how many other grocery stores, if any, Pay Less operated in the county.

<sup>3</sup> If H.H. Gregg chooses to exercise its options, it has the right to continue to occupy the former Kroger space at Sagamore Center until the expiration of the lease on June 1, 2014.

<sup>4</sup> In 1997, Kimko Lafayette 671, Inc., purchased the center from SES, subject to the Pay Less lease and the H.H. Gregg sublease.

## Restrictive Covenants in Shopping Centers

**HN2** [↑] Indiana law permits restrictive covenants but finds them disfavored and justified only to the extent they are unambiguous and enforcement is not adverse to public policy. [One Dupont Ctr., LLC v. Dupont Auburn, LLC, 819 N.E.2d 507, 516 \(Ind. Ct. App. 2004\)](#). [\*\*5] Doubts should be resolved in favor of the free use of property and against restrictions. *Id.* However, courts have been quite willing to enforce restrictive covenants written in shopping center lease contracts even though they prevent competition within the center. See, e.g., [Almacs, Inc. v. Drogin, 771 F. Supp. 506, 513 \(D. R.I. 1991\)](#); [Whitinsville Plaza, Inc. v. Kotseas, 378 Mass. 85, 390 N.E.2d 243, 252-53 \(Mass. 1979\)](#); [Kingpin, Inc. v. Hillcrest Dev., 267 Minn. 256, 126 N.W.2d 435, 439 \(Minn. 1964\)](#); [Keith Hardware v. White, 956 S.W.2d 500, 501 \(Tenn. Ct. App. 1997\)](#) ("Rather than restricting competition, such covenants serve to facilitate trade and induce tenants to rent in a particular shopping center. . . . It is reasonable for the plaintiff to want to avoid competition within this center."); [49 Am.Jur.2d Landlord and Tenant § 70](#) (1995).

Restrictive covenants in shopping center leases have, for the most part, been found not to restrain competition unreasonably and have been generally found to be consistent with the public interest. The rationales for this result focus on the need to encourage [\*\*6] the investment in new development by both the shopping center developer and its tenants. See, e.g., [Vt. Nat'l Bank v. Chittenden Trust Co., 143 Vt. 257, 465 A.2d 284, 287 \(Vt. 1983\)](#). Courts have recognized that landlords and tenants of shopping centers invest considerable sums of money to make the center attractive to customers. [Parker v. Lewis Grocer Co., 246 Miss. 873, 153 So. 2d 261, 272 \(Miss. 1963\)](#) ("Tremendous outlays of venture capital and risk are required and entailed from the supermarket tenant as well as the developer-landlord. Restrictive covenants in the nature of ancillary and reasonable restraints are absolutely required to induce investors to place a new venture in such untried area."); [Wal-Mart Stores, Inc. v. Ingles Mkts., Inc., 158 N.C. App. 414, 581 S.E.2d 111, 116 \(N.C. Ct. App. 2003\)](#) ("The development of new shopping centers requires tremendous outlays of venture capital and risk by prospective tenants as well as by landlords; restrictive covenants against unwanted competition are consistent with the public interest in such development."). Thus, restrictive covenants have allowed shopping centers to offer "noncompetitive and diversified, but interrelated, [\*\*7] businesses designed not to serve just one need but as many needs of the consumer as is feasible within the economic framework of the shopping center." Annotation, 97 A.L.R.2d 4, 11 (1964). Accord [Valley Prop., Inc. v. King's Dep't Stores, Inc., 505 F. Supp. 92, 95 \(D. Mass. 1981\)](#) (restrictive covenants are "necessary inducements to shopping center tenants which facilitate the orderly and harmonious development for commercial use of real property"). All of these cited reasons support limiting the covenant to protection of current tenants of the center. Both the trial court and the Court of Appeals agreed that the initial covenant to Kroger was enforceable. In evaluating Kimco's claim that the covenant created in 1982 was no longer enforceable, the trial court and Court of Appeals focused on whether there have been significant changes in the circumstances. We think there is only one factor that is central and dispositive here. Because the Kroger site in the Sagamore Center is no longer being used as a grocery store location, there is no interest within the center for the restrictive [\*\*515] covenant to protect. Pay Less is attempting to use the covenant to restrict [\*\*8] competition for its grocery stores located at other locations. Kroger was within its rights to assign the lease to Pay Less, and if Pay Less had chosen to continue grocery operations at the center, its interest in the lease would support enforcement of the covenant. However, Pay Less voluntarily abandoned grocery operations in the center and thereby severed the restrictive covenant from the occupancy.

The shopping center obviously receives no benefit from permitting a transfer of the covenant. And it seems unlikely that a prospective new tenant would be significantly motivated by the prospect of recouping its investment by selling a restrictive covenant to a nearby competitor if the tenant's business fails. In any event, the effect of permitting a covenant to be sold separately from the operation it is designed to protect is perhaps to add some minimal value to the original lessee, but at considerable cost to the lessor and the public. None of these rationales suggests a powerful reason to permit a secondary market in restrictive covenants divorced from the real estate they are designated to protect. It is one thing to conclude that restrictive covenants in leases of shopping center [\*\*9] tenants should be enforceable to protect the interests of the center and those tenants who have a current protectible interest within the center. It is quite another to permit enforcement of an anticompetitive covenant by someone foreign to the center who simply acquires the right to exclude competition without making any investment

in the center. And the interest of the original lessee, Kroger in this case, may well be fully served by permitting enforcement of the covenant as long as it or a successor operates a grocery store in the center.

Finally, the issue is not whether the covenant violates federal or state **antitrust law**. We assume Judge Posner was correct in his passing observation deeming "implausible" a claim that federal **antitrust law** prevented a drug store from invoking a shopping center covenant to exclude a competitor.<sup>5</sup> But the issue here is not whether the antitrust laws prevent enforcement of such a covenant. It is whether state law permits its enforcement not by a tenant of the center, but in the hands of one who has never occupied the center and merely attempts to purchase the right to exclude competition from a remote site. As the comment to the Restatement **[\*\*10]** (Second) of Contracts explains:

**HN3**<sup>↑</sup> The restraint may be unreasonable in either of two situations. The first occurs when the restraint is greater than necessary to protect the legitimate interests of the promisee. The second occurs when, even though the restraint is not greater than necessary to protect those interests, the promisee's need for protection is out-weighed by the hardship to the promisor and the likely injury to the public.

Restatement (Second) of Contracts § 188 cmt. a (1981). This restraint is an example of a restriction that "proscribes types of activity more extensive than necessary to protect those engaged in by the promisee." *Id.* § 188 cmt. d. Usually if a restriction is unenforceable it is because it prohibits an overbroad "type of activity" by the promisor. In this case it is the protected activity of the promisee that needs to be narrowed to bring the justification and the existence of the restriction into harmony. It is true that this concern usually comes **[\*516]** up in the context of an agreement not to compete, but the rationale is equally applicable where the agreement prevents the owner of a shopping **[\*\*11]** center from leasing to a specified type of store that is no longer present in the center.

The restriction also runs afoul of the second concern: it is excessively burdensome to the public and the promisor compared to a remote promisee's need for protection. There is little doubt that a competitor in the same center may be harmful to a given store, even if overall competition is unharmed. The fact that tenants demand and seek to enforce these covenants demonstrates that. Indeed, the justification for the restriction is incentive for the tenant to invest--assuming the tenant expects to be benefited from the restriction. Similarly, Tippecanoe's effort to enforce the covenant demonstrates its belief that sales will flow **[\*\*12]** to a new store if one is placed in the center. It follows that the convenience of the public and certainly the interest of the landlord are served by having a grocery store in the center.

The issue **HN4**<sup>↑</sup> under the **Sherman Act** is whether there is an adverse effect on competition, i.e. whether overall competition suffers if a second drugstore is precluded from operating in a single shopping center. United States v. Visa USA, Inc., 344 F.3d 229, 242 (2d Cir. 2003) (in a **Sherman Act** action, "the proper inquiry is whether there has been an '*actual* adverse effect on competition as a whole in the relevant market." (emphasis in original)). A typical shopping center covenant has no such effect because customers in the center are served by the one seeking to enforce the covenant, and other locations for competitors are plentiful. See, e.g., Keith Hardware, 956 S.W.2d at 501. The issue here, however, is whether it is reasonable to deny the public access to any grocery store in the center and to deny the center the benefit of a grocery store and perhaps of any tenant at all for one of its largest spaces. Enforcement of the covenant in the hands of a non-tenant **[\*\*13]** runs afoul of the policy against restrictive covenants unless justified by legitimate concerns of the promisee balanced against the interests of the public and the detriment to the promisor. As explained above, the policy usually justifying covenants in shopping centers--protection and encouragement of investment--is inapplicable here. The only policy the dissent identifies is naked enforcement of contracts. That is not a sufficient policy reason. If it were, all restrictive covenants would be enforceable. But the law recognizes that public interest may under some circumstances limit the ability of private parties to arrange their affairs. This is such a case.

<sup>5</sup> The issue was expressly not addressed in Walgreen Co. v. Sara Creek Prop. Co., 966 F.2d 273, 274 (7th Cir. 1992) ("Such an exclusivity clause, common in shopping-center leases, is occasionally challenged on antitrust grounds, . . . but that is an issue for another day . . .").

In sum, because Pay Less voluntarily relinquished the Kroger site as a grocery store location, it cannot enforce the restrictive covenant to prevent the shopping center from leasing to a grocery tenant. We hold that the restrictive covenant is not enforceable and cannot be used to stop competition and protect the holder's interests at some other site.

## **Conclusion**

We affirm the trial court's declaratory judgment that the restrictive covenant has been severed from the occupancy and is unenforceable.<sup>6</sup>

[\*\*14] Dickson and Rucker, JJ., concur.

Sullivan, J., dissents with separate opinion in which Shepard, C.J., joins.

**Dissent by:** Sullivan

## **Dissent**

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[\*517] **Sullivan, Justice, dissenting.**

The Court here declares unenforceable a covenant in a contract bargained for at arm's length by two sophisticated parties. I respectfully dissent.

It is on grounds of public policy violation that the Court sets aside this contract: the covenant, the Court says, is "anticompetitive." But the trial court made no findings as to the degree of competition among grocery stores in the Lafayette market and the Court cites no evidence of any.

It is true that the reported cases challenging the enforceability of shopping center lease covenants like this one--cases the Court must distinguish because they all uphold the covenants--involve situations where the beneficiary of the restrictive covenant continues to be in the business that is the subject of the covenant. The Court says it makes a difference that the beneficiary of the covenant here is in a different business. That does not justify setting aside a freely-bargained-for contractual provision unless competition is materially and adversely affected by the [\*\*15] covenant--that the citizens of Lafayette must pay more for their groceries or travel unreasonable distances to buy them or the like. There is, to repeat, no evidence of any of that here. In setting aside the covenant on this record, the Court favors one business (the landlord) by depriving the other (the lessee) of the benefit of its bargain without any evidence of any compensating benefit to the public.

Judge Posner has called challenges to the enforceability of shopping center restrictive covenants on antitrust grounds "implausible . . . given the competition among malls." [Walgreen Co. v. Sara Creek Property Co., 966 F.2d 273, 274 \(7th Cir. 1992\)](#) (Posner, J.). And two scholars have observed that:

A noncompetition clause in a lease of property ordinarily poses no threat to the competitive process, since the arrangement restrains one person in a relevant market that normally is replete with competitors engaged in vigorous competition with one another. Absent the effect of creating or tendency to create a monopoly in the relevant geographic market, such ancillary restraint should be upheld.

Milton Handler and Daniel E. Lazaroff, Restraint of Trade [\*\*16] and the Restatement (Second) of Contracts, 57 N.Y.U.L. Rev. 669, 679 (1982).

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<sup>6</sup> We summarily affirm the Court of Appeals on all issues not addressed in this opinion. [Ind. Appellate Rule 58\(A\)\(2\)](#).

The Court says that Judge Posner's comment and the Handler and Lazaroff analysis are irrelevant because they address the applicability of antitrust statutes, not common law, to such covenants. But it was not the provisions of any statute that caused Judge Posner to call antitrust challenges to the enforceability of these covenants "implausible"; it was simply because these covenants don't adversely affect competition "given the competition among malls." [Walgreen Co., 966 F.2d at 274](#). The Court's discussion of antitrust statutes reminds us that the legislative branch has undertaken to regulate competition where it has found it to be appropriate. That the legislative branch has not chosen to do so in these circumstances is another reason why I believe the court should not undo this contract.

I also dissent from the Court's willingness to go beyond declaring this particular covenant unenforceable and mandate that all such covenants are and will be unenforceable whenever they are "severed from the occupancy." This rewrites existing commercial leases and [\\*\\*17](#) restrains the ability of parties in the future to enter them on terms they view to be mutually beneficial, regardless of whether there is any demonstrable adverse effect on competition.

**[\*518]** I would affirm the decision of the Court of Appeals.

Shepard, C.J., joins.

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## **ASAP Paging Inc. v. Centurytel of San Marcos Inc.**

United States Court of Appeals for the Fifth Circuit

June 24, 2005, Filed

No. 04-50838

### **Reporter**

137 Fed. Appx. 694 \*; 2005 U.S. App. LEXIS 12642 \*\*; 2005-1 Trade Cas. (CCH) P74,849; 36 Comm. Reg. (P & F) 289

ASAP PAGING INC, Plaintiff-Appellant, versus CENTURYTEL OF SAN MARCOS INC; CENTURYTEL SERVICE GROUP LLC; CENTURYTEL SECURITY SYSTEMS OF TEXAS LP; CENTURYTEL INC, Defendants-Appellees.

**Notice:** [\*\*1] RULES OF THE FIFTH CIRCUIT COURT OF APPEALS MAY LIMIT CITATION TO UNPUBLISHED OPINIONS. PLEASE REFER TO THE RULES OF THE UNITED STATES COURT OF APPEALS FOR THIS CIRCUIT.

**Prior History:** Appeal from the United States District Court for the Western District of Texas. 1:04-CV-181-SS.

## **Core Terms**

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tariff, antitrust claim, numbers, district court, filed rate doctrine, charges, Skiing, switch, toll, doctrine of primary jurisdiction, Telecommunications, antitrust, proceedings, Preemption, customers, rated

## **LexisNexis® Headnotes**

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Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN1[] Standards of Review, De Novo Review**

The United States Court of Appeals for the Fifth Circuit reviews a dismissal for failure to state a claim de novo.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN2[] Motions to Dismiss, Failure to State Claim**

A claim should be dismissed only if it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.

137 Fed. Appx. 694, \*694L 2005 U.S. App. LEXIS 12642, \*\*1

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Common Carriers

Communications Law > Federal Acts > Federal Communications Act > General Overview

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Administrative Law > Judicial Review > Reviewability > Jurisdiction & Venue

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

### **HN3** Filed Rate Doctrine, Common Carriers

Under the "filed rate doctrine" (also sometimes called the "filed tariff doctrine"), when a carrier is required to file a tariff of its charges with a regulatory body, the charges filed are the only charges that the carrier may lawfully assess. The carrier cannot deviate from the tariff, and the terms of the tariff can be initially challenged only before the agency that approved the tariff, not in a court.

Administrative Law > Separation of Powers > Jurisdiction

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Administrative Law > Judicial Review > Reviewability > Jurisdiction & Venue

Administrative Law > Separation of Powers > Primary Jurisdiction

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Communications Law > ... > Regulated Entities > Cable Systems > US Federal Communications Commission Jurisdiction

Communications Law > Federal Acts > Federal Communications Act > Jurisdiction

Communications Law > Federal Acts > Telecommunications Act > Jurisdiction

Communications Law > Regulators > US Federal Communications Commission > Jurisdiction

### **HN4** Separation of Powers, Jurisdiction

The doctrine of primary jurisdiction applies either when a government agency has exclusive original jurisdiction over an issue within a case or when a court having jurisdiction wishes to defer to an agency's superior expertise.

Communications Law > Federal Acts > General Overview

Energy & Utilities Law > Administrative Proceedings > General Overview

Governments > Legislation > Statutory Remedies & Rights

Administrative Law > Judicial Review > Reviewability > Jurisdiction & Venue

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

137 Fed. Appx. 694, \*694L 2005 U.S. App. LEXIS 12642, \*\*1

Communications Law > ... > Regulated Entities > Cable Systems > US Federal Communications Commission Jurisdiction

Communications Law > Federal Acts > Federal Communications Act > General Overview

Communications Law > Federal Acts > Federal Communications Act > Jurisdiction

Communications Law > Federal Acts > Telecommunications Act > Jurisdiction

## **HN5** Communications Law, Federal Acts

Under [47 U.S.C.S. § 207](#), a plaintiff may complain of being damaged either to the Federal Communications Commission or in federal district court.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Governments > Legislation > Statutory Remedies & Rights

Transportation Law > Carrier Duties & Liabilities > Damages

Administrative Law > Judicial Review > Reviewability > Jurisdiction & Venue

Communications Law > Federal Acts > Federal Communications Act > General Overview

## **HN6** Subject Matter Jurisdiction, Jurisdiction Over Actions

See [47 U.S.C.S. § 207](#).

Administrative Law > Judicial Review > Reviewability > Jurisdiction & Venue

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Administrative Law > Separation of Powers > Primary Jurisdiction

## **HN7** Reviewability, Jurisdiction & Venue

Even where the doctrine of primary jurisdiction could be applied to a plaintiff's claims, a court must weigh the benefits of obtaining an agency's aid against the need to resolve the litigation expeditiously and may defer only if the benefits of agency review exceed the costs imposed on the parties.

Administrative Law > Separation of Powers > Primary Jurisdiction

Civil Procedure > ... > Entry of Judgments > Stays of Judgments > General Overview

Communications Law > ... > Regulated Entities > Cable Systems > US Federal Communications Commission Jurisdiction

Civil Procedure > Dismissal > Involuntary Dismissals > General Overview

## **HN8** Separation of Powers, Primary Jurisdiction

When dismissal may cause a plaintiff to lose rights, claims should be stayed pending deferral to an agency rather than dismissed.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > Regulated Industries > Communications > General Overview](#)

[Antitrust & Trade Law > Regulated Industries > Communications > Sherman Act](#)

[Antitrust & Trade Law > Regulated Industries > Communications > State Regulation](#)

[Antitrust & Trade Law > Regulated Industries > Communications > Telecommunications Act](#)

[Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview](#)

[Antitrust & Trade Law > ... > Private Actions > Standing > Sherman Act](#)

[Communications Law > Federal Acts > Telecommunications Act > General Overview](#)

[Communications Law > Federal Acts > Telecommunications Act > Federal Preemption](#)

## **[HN9](#)[] Antitrust & Trade Law, Sherman Act**

The Telecommunications Act specifically provides that it will not impair or supersede antitrust law. The Telecommunications Act does not expand the coverage of the antitrust laws, so behavior needs to constitute an antitrust violation in its own right for an antitrust action to lie. The Sherman Act generally does not restrict a private entity's refusal to deal, except in certain egregious circumstances. A refusal to deal does not fit within the limited exception where factors indicating a willingness to forgo short-term profit for anticompetitive purposes are absent.

[Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

## **[HN10](#)[] Monopolies & Monopolization, Attempts to Monopolize**

Where a defendant ends a previous voluntary practice that is presumably profitable, and will not accept retail price from a plaintiff for its product, this indicates a willingness to forsake short-term profits to achieve an anticompetitive end.

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

[Governments > Legislation > Interpretation](#)

## **[HN11](#)[] Public Enforcement, State Civil Actions**

Texas law instructs that Texas antitrust provisions shall be construed in harmony with federal judicial interpretations of comparable federal antitrust statutes. [Tex. Bus. & Com. Code Ann. § 15.04](#).

**Counsel:** For ASAP PAGING INC, Plaintiff - Appellant: W Scott McCollough, Austin, TX.

For CENTURYTEL OF SAN MARCOS INC, CENTURYTEL SERVICE GROUP LLC, CENTURYTEL SECURITY SYSTEMS OF TEXAS LP, CENTURYTEL INC, Defendants - Appellees: Richard D Milvenan, McGinnis, Lochridge & Kilgore, Capitol Center, Austin, TX.

**Judges:** Before GARWOOD, GARZA and BENAVIDES, Circuit Judges.

## **Opinion**

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[\*694] PER CURIAM: \*

ASAP Paging, Inc. (ASAP) appeals the dismissal without prejudice of its antitrust, [\*695] *Communications Act*, and tortious interference claims against CenturyTel of San Marcos, Inc., [\*\*\*2] CenturyTel Service Group, L.L.C., CenturyTel Security Systems of Texas, L.P., and CenturyTel, Inc. (collectively, CenturyTel). We affirm the district court's dismissal of the antitrust claims. We vacate the dismissal of the remaining claims and remand to the district court with instructions to stay these claims pending the outcome of related proceedings in state court and with the Federal Communications Commission (FCC).

### **Facts and Proceedings Below**

ASAP provides paging services and access to Internet service providers (ISPs) for customers in San Marcos, Texas and the surrounding communities of Fentress, Kyle, and Lockhart. CenturyTel is the incumbent local telephone company for San Marcos. There is an extended local calling service (ELCS) arrangement between the San Marcos exchange and several surrounding exchanges, including those of Kyle, Fentress and Lockhart, such that calls between these exchanges are charged at a local call rate. ASAP obtained telephone numbers from the FCC pursuant to its license as a commercial mobile radio service (CMRS) provider, and chose numbers that are normally associated with the Fentress, Lockhart, and Kyle exchanges. Calls to these phone [\*\*\*3] numbers are routed by the relevant local telephone carriers to ASAP's switch, which was located in Austin, outside of the San Marcos ELCS area, during 2001 and 2002.

From October 2001 through March 2002, CenturyTel customers in San Marcos could dial ASAP's numbers assigned to Lockhart, Fentress or Kyle as local calls. Starting on April 1, 2002, however, CenturyTel began charging these calls as long-distance calls. This resulted in a greatly reduced call volume to ASAP's customers having these phone numbers. According to CenturyTel, it started charging calls to the ASAP numbers as toll calls once it determined that the calls were going to ASAP's switch in Austin.

ASAP immediately filed a complaint with the Texas Public Utility Commission (PUC), asking the commission to order CenturyTel to stop assessing toll charges on the calls. In an order issued October 9, 2003, the PUC ruled against ASAP, finding that the geographic location being called, rather than the exchange associated with the number being called, should determine whether a call is rated local or long distance. The commission also found that CenturyTel was following the tariff it filed with the PUC in assessing the toll [\*\*\*4] charges. ASAP's appeal of the PUC order is currently working its way through the Texas court system.

In October or November of 2003, ASAP installed a switch in Kyle, which is in the San Marcos ELCS area. CenturyTel refused to rate calls from San Marcos to this Kyle switch as local, however. CenturyTel indicated to ASAP that ASAP would have to establish a direct interconnection with CenturyTel through an interconnection

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\* Pursuant to 5TH CIR. R. 47.5 the Court has determined that this opinion should not be published and is not precedent except under the limited circumstances set forth in 5TH CIR. R. 47.5.4.

agreement, rather than the existing indirect connection through another telephone company, in order for the calls to be rated as other than toll calls, regardless of the location of the switch.<sup>1</sup>

In December of 2003, ASAP filed a Petition for Preemption with the FCC, requesting that the FCC [\*\*5] preempt the PUC order in accordance with the FCC's authority to preempt state regulation that has the effect of prohibiting the provision [\*696] of telecommunications service. See [47 U.S.C. §§ 253\(d\), 332\(c\)\(3\)](#). The FCC has not acted on this petition, which remains pending before it.

ASAP subsequently filed a complaint in the Western District of Texas including federal and state antitrust claims, state tortious interference claims, and claims for damages under [sections 206](#) and [207](#) of the Communications Act ([47 U.S.C. §§ 206, 207](#)), alleging violations of [47 U.S.C. §§ 201, 202, 251\(a\)](#) and [251\(b\)\(3\)](#). *Id.* at 38-42. ASAP points out in the complaint that some of its claims may be nearing the end of statute-of-limitations periods, and suggests that abatement of the action pending disposition of the petition for preemption to the FCC could be helpful to the court.

CenturyTel filed a motion to dismiss under [Rule 12\(b\)\(6\) of the Federal Rules of Civil Procedure](#), arguing that (1) all of the claims are barred by the filed rate doctrine, (2) the antitrust claims are defective and barred [\*\*6] as a matter of law by the Supreme Court's decision in [Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 124 S. Ct. 872, 157 L. Ed. 2d 823 \(2004\)](#), and (3) that the claims under the Communications Act should be dismissed because of the "primary jurisdiction" of the FCC. After a response to the motion, reply to the response, and a hearing, the district court issued an order dismissing ASAP's claims without prejudice. The court found that all of ASAP's claims are barred by the filed rate doctrine, and that, alternatively, the antitrust claims are barred by the *Trinko* decision and the Communications Act claims are barred by the doctrine of primary jurisdiction. ASAP appeals.

## Discussion

### I. Standard of Review

[HN1](#) This court reviews a dismissal for failure to state a claim *de novo*. [United States ex rel. Riley v. St. Luke's Episcopal Hosp., 355 F.3d 370, 375 \(5th Cir. 2004\)](#). The [HN2](#) claim should be dismissed "only if 'it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.'" *Id.* (quoting [Conley v. Gibson, 355 U.S. 41, 78 S. Ct. 99, 102, 2 L. Ed. 2d 80 \(1957\)](#)).

### [\*\*7] II. Filed Rate Doctrine and Doctrine of Primary Jurisdiction

[HN3](#) Under the "filed rate doctrine" (also sometimes called the "filed tariff doctrine"), when a carrier is required to file a tariff of its charges with a regulatory body, the charges filed are the only charges that the carrier may lawfully assess. [Am. Tel. & Tel. Co. v. Cent. Office Tel., Inc., 524 U.S. 214, 118 S. Ct. 1956, 1962-63, 141 L. Ed. 2d 222 \(1998\)](#). The carrier cannot deviate from the tariff, and the terms of the tariff can be initially challenged only before the agency that approved the tariff, not in a court. [Arsberry v. Illinois, 244 F.3d 558, 562 \(7th Cir. 2001\)](#); [Southwestern Elec. Power Co. v. Grant, 73 S.W.3d 211, 216-17, 45 Tex. Sup. Ct. J. 502 \(Tex. 2002\)](#). ASAP argues that the filed rate doctrine does not apply to its dispute with CenturyTel because ASAP is not challenging the terms of the tariff, but rather CenturyTel's (and the PUC's) interpretation of the tariff: specifically, whether calls to ASAP's numbers should be classified as local or toll for application of the tariff.

There is no indication in the record that CenturyTel's filed tariff directly addresses [\*\*8] which rate should be applied to calls to numbers such as ASAP's. Whether CenturyTel is following its tariff such that the filed rate

<sup>1</sup>The Telecommunications Act of 1996 provides for interconnection agreements between telecommunications carriers establishing compensation between the carriers for various services. See [47 U.S.C. §§ 251\(c\)\(1\), 252](#). There is no interconnection agreement between ASAP and CenturyTel.

doctrine would apply therefore depends on whether the PUC's interpretation of CenturyTel's tariff survives review by the state appellate courts and the FCC. In the event that either a Texas court or the FCC overturns the [\*697] PUC's interpretation of the tariff, ASAP may have rights against CenturyTel that will be lost through the running of statutes of limitations. Staying the action in the district court to avoid this potential prejudice to ASAP is therefore the appropriate course, particularly since the district court seems to have intended that ASAP be able to present its claims again depending on the outcome of the other proceedings.<sup>2</sup> [\*\*9] In addition, this approach would allow time for ASAP to obtain a ruling from the PUC on whether CenturyTel was following its tariff in refusing to rate calls to ASAP's Kyle switch as local calls.<sup>3</sup>

The district court also dismissed ASAP's Communications Act claims based on the doctrine of primary jurisdiction. [HN4](#)[] The doctrine of primary jurisdiction applies either when a government agency has exclusive original jurisdiction over an issue within a case or when a court having jurisdiction wishes to defer to an agency's superior expertise. [Arsberry](#), 244 F.3d at 563. These circumstances do not appear to apply to ASAP's Communications Act claims. Although the district court indicated that ASAP had requested that "the FCC exercise jurisdiction over each of its [Telecommunications Act] claims," ASAP's Petition for Preemption does not appear to be an assertion of Communications Act or Telecommunications Act claims against CenturyTel. [\*\*10] [HN5](#)[] Under [47 U.S.C. § 207](#), ASAP may complain of being damaged by CenturyTel either to the FCC or in federal district court, and ASAP has chosen to do so in district court.<sup>4</sup> ASAP's petition for preemption is not a submission of its claims against CenturyTel to the FCC, but instead it is essentially a claim against the PUC, specifically an assertion that the PUC's interpretation is preempted by federal law.

[HN7](#)[] Even to the extent that the doctrine of primary jurisdiction could [\*\*11] be applied to any of ASAP's claims, a court "must weigh the benefits of obtaining the agency's aid against the need to resolve the litigation expeditiously and may defer only if the benefits of agency review exceed the costs imposed on the parties." [Wagner & Brown v. ANR Pipeline Co.](#), 837 F.2d 199, 201 (5th Cir. 1988). [HN8](#)[] When dismissal may cause a plaintiff to lose rights, claims should be stayed pending deferral to an agency rather than dismissed. [Id. at 206](#). Staying of the case pending the outcome of the state court and FCC proceedings is therefore appropriate for any dismissals based on the primary jurisdiction doctrine as well as for those based on the filed rate doctrine.

### III. Antitrust Claims

The district court dismissed ASAP's antitrust claims as barred by the Supreme Court's *Trinko* decision, in addition to dismissing them under the filed rate doctrine. Although we do not agree with the district [\*698] court's apparent rationale, that the antitrust claims should be dismissed by virtue of being premised on the Telecommunications Act, dismissal of the antitrust claims was nonetheless proper.

The Supreme Court noted in *Trinko* that [\*\*12] [HN9](#)[] the Telecommunications Act specifically provided that it would not impair or supersede [antitrust law](#). [Trinko](#), 124 S. Ct. at 878. The Court held that the Telecommunications

<sup>2</sup> In addition to dismissing the claims without prejudice, the court asked CenturyTel about its willingness to waive statute-of-limitations defenses.

<sup>3</sup> The PUC appears to have exclusive primary jurisdiction on this question, which it has not yet considered with respect to the Kyle switch. [TEX. UTIL. CODE § 52.002\(a\)](#) (stating that the PUC "has exclusive original jurisdiction over the business and property of a telecommunications utility," subject to certain limitations).

<sup>4</sup> [HN6](#)[] [Section 207](#) provides:

"Any person claiming to be damaged by any common carrier subject to the provisions of this chapter may either make complaint to the Commission as hereinafter provided for, or may bring suit for the recovery of the damages for which such common carrier may be liable under the provisions of this chapter, in any district court of the United States of competent jurisdiction; but such person shall not have the right to pursue both such remedies."

Act did not expand the coverage of the antitrust laws, however, so that the complained-of behavior would need to constitute an antitrust violation in its own right for an antitrust action to lie. *Id.* The Court characterized the claim in *Trinko* as a refusal-to-deal claim and noted that the *Sherman Act* generally does not restrict a private entity's refusal to deal, except in certain egregious circumstances such as those in *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.*, 472 U.S. 585, 105 S. Ct. 2847, 86 L. Ed. 2d 467 (1985). *Trinko*, 124 S. Ct. at 879. The Court proceeded to compare the complained-of actions to those in *Aspen Skiing*, stating that *Aspen Skiing* was "at or near the outer boundary of § 2 liability." <sup>5</sup> *Id. at 879-80*. The Court determined that the refusal to deal alleged in *Trinko* did not fit within the limited exception recognized in *Aspen Skiing*, since factors indicating a willingness to forgo short-term profit for [\*\*13] anticompetitive purposes were absent.<sup>6</sup> *Id.*

[\*\*14] ASAP's complaint alleges that CenturyTel's decision to rate its customers' calls to ASAP's numbers as long distance was part of a scheme to harm ASAP as a competitor in the one-way inbound call capability market. This is essentially a milder form of the refusal-to-deal claim in *Trinko*. In *Trinko*, the defendant allegedly refused to connect competitors, while in this case, CenturyTel allegedly refused to connect ASAP on favorable enough terms. CenturyTel's conduct should therefore be compared to that of the defendant in *Aspen Skiing* to see whether an antitrust action can be recognized.

Although ASAP claims that CenturyTel "voluntarily" rated calls to their numbers as local from October 2001 through March 2002, the complaint does not allege that CenturyTel understood where ASAP's switch was located at that time. So there is no indication that the prior arrangement was agreed to, and therefore presumably profitable, in the manner of the ski ticket arrangement in *Aspen Skiing*. And there is otherwise nothing that would suggest that CenturyTel is giving up short-term profits in hopes of running ASAP out of business. CenturyTel gets more short-term profit, not less, [\*699] by charging [\*\*15] the calls to ASAP's numbers as toll calls. Even if no one calls ASAP anymore when the calls are rated as toll, CenturyTel is not giving up profits as compared to rating calls to ASAP as local, because CenturyTel's customers pay a flat fee for local service. ASAP's allegations do not fit into the *Aspen Skiing* exception for refusal-to-deal claims, and therefore do not state a cognizable antitrust claim. The antitrust claims were therefore properly dismissed.<sup>7</sup>

## Conclusion

Because ASAP's antitrust claims are barred by the Supreme Court's *Trinko* decision, we AFFIRM the district court's dismissal of the antitrust claims. We VACATE the dismissal of the Communications Act and tortious interference claims [\*\*16] and REMAND to the district court with instructions to stay these claims pending the outcome of the state court appeals of the PUC order and the Petition for Preemption with the FCC.

<sup>5</sup> In *Aspen Skiing*, the defendant, who operated three ski resorts in the area, decided to stop participating with the plaintiff, who operated the fourth resort, in a joint all-resort ski ticket. *Trinko*, 124 S. Ct. at 879; *Aspen Skiing*, 105 S. Ct. at 2851-52. The defendant refused all efforts by the plaintiff to reinstate the ticket, even an offer to essentially buy the defendant's tickets at retail price. *Trinko*, 124 S. Ct. at 879; *Aspen Skiing*, 105 S. Ct. at 2853. In upholding a verdict for the plaintiff, the Court in *Aspen Skiing* found significant that the *HN10* [defendant] ended a previous voluntary practice that was presumably profitable, and would not accept retail price. This indicated a "willingness to forsake short-term profits to achieve an anticompetitive end." *Trinko*, 124 S. Ct. at 880; *Aspen Skiing*, 105 S. Ct. at 2861.

<sup>6</sup> In *Trinko*, a customer of a competing local exchange carrier sued Verizon, the incumbent local exchange carrier, when Verizon fell behind on filling orders by competing carriers for access to its network. *Trinko*, 124 S. Ct. at 876-77. The plaintiff did not claim that Verizon had previously engaged in a voluntary course of dealing with its competitors, and Verizon did not refuse an offer at retail price, but rather refused (according to the plaintiff) to provide services at a statutory wholesale rate. *Id.*

<sup>7</sup> *HN11* [Texas law instructs that Texas antitrust provisions "be construed in harmony with federal judicial interpretations of comparable federal antitrust statutes." *TEX. BUS. COMM. CODE § 15.04*. Dismissal of both the state and federal antitrust claims was therefore proper.

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## Med. Sav. Ins. Co. v. HCA, Inc.

United States District Court for the Middle District of Florida, Fort Myers Division

June 24, 2005, Decided ; June 24, 2005, Filed

Case No. 2:04-cv-156-FtM-29DNF

### **Reporter**

2005 U.S. Dist. LEXIS 20206 \*; 2005 WL 1528666

MEDICAL SAVINGS INSURANCE COMPANY, Plaintiff, vs. HCA, INC., HCA HEALTH SERVICES OF FLORIDA, INC., LEE MEMORIAL HEALTH SYSTEM, CAPE MEMORIAL HOSPITAL, MARTIN MEMORIAL HEALTH SYSTEMS, INC., MARTIN MEMORIAL MEDICAL CENTER, INC., FLORIDA HOSPITAL ASSOCIATION, INC., and FLORIDA HOSPITAL ASSOCIATION MANAGEMENT CORPORATION, Defendants.

**Subsequent History:** Affirmed by *Medical Sav. Ins. Co. v. HCA, Inc.*, 186 Fed. Appx. 919, 2006 U.S. App. LEXIS 16430 (11th Cir. Fla., June 27, 2006)

**Prior History:** [\*Medical Sav. Ins. Co. v. HCA, Inc.\*, 2005 U.S. Dist. LEXIS 51601 \(M.D. Fla., Jan. 31, 2005\)](#)

## **Core Terms**

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insureds, antitrust, alleges, amended complaint, business relationship, defendants', injuries, tortious interference, acute care hospital, inflated, prices, acute care, defamation, motion to dismiss, overcharges, patients, charges, hospitalization, customers, conspiracy, asserts, boycott, Counts, hospitalization insurance, fail to state a claim, prospective insured, health insurance, Sherman Act, contractual, customary

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

### **[HN1](#) [down arrow] Motions to Dismiss, Failure to State Claim**

In deciding a motion to dismiss, a court must accept all factual allegations in a complaint as true and take them in the light most favorable to the plaintiff. A complaint should not be dismissed unless it appears beyond doubt that plaintiff can prove no set of facts that would entitle it to relief. Dismissal is warranted under [\*Fed. R. Civ. P. 12\(b\)\(6\)\*](#) if, assuming the truth of the factual allegations of plaintiff's complaint, there is a dispositive legal issue which precludes relief. A court need not accept unsupported conclusions of law or of mixed law and fact in a complaint.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Evidence > Burdens of Proof > General Overview

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrs & Objections > Motions to Dismiss

## **HN2** Justiciability, Standing

The [Fed. R. Civ. P. 12\(b\)\(6\)](#) standard applies when a court reviews issues of standing pursuant to a motion to dismiss. The principal purpose of standing is to ensure that the parties before a court have a concrete interest in the outcome of the proceedings such that they can be expected to properly frame the issues. Every complaint must contain sufficient allegations of standing, but a complaint may be dismissed for lack of standing only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations. Standing always remains an open issue, and can be revisited under a different standard at the summary judgment stage or at trial. It is plaintiff's responsibility to allege facts sufficient to establish its standing, and a court cannot speculate concerning the existence of standing, nor should it imagine or piece together an injury sufficient to give plaintiff standing when it has demonstrated none.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

## **HN3** Justiciability, Standing

In order to establish standing, a plaintiff must adequately allege, and ultimately prove, three elements: (1) that it has suffered an "injury-in-fact;" (2) a causal connection between the asserted injury-in-fact and the challenged conduct of the defendant; and (3) that the injury likely will be redressed by a favorable decision. These requirements are the "irreducible minimum" required by the Constitution for a plaintiff to proceed in federal court.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Civil Procedure > ... > Injunctions > Grounds for Injunctions > General Overview

## **HN4** Justiciability, Standing

A plaintiff seeking injunctive relief lacks standing unless it alleges facts giving rise to an inference that it will suffer future injury by defendant. A party has standing to seek injunctive relief only if the party alleges, and ultimately proves, a real and immediate--as opposed to a merely conjectural or hypothetical--threat of future injury.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN5** Antitrust & Trade Law, Sherman Act

The Florida Antitrust Act, [Fla. Stat. Ann. § 542.15 et seq.](#), was patterned after the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), and was intended to complement and follow the federal court interpretations of the Sherman Act. [Fla. Stat. Ann. § 542.32.](#)

Civil Procedure > ... > Justiciability > Standing > Injury in Fact

Constitutional Law > ... > Case or Controversy > Standing > Elements

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Preliminary Considerations > Justiciability > General Overview

Civil Procedure > ... > Justiciability > Case & Controversy Requirements > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > The Judiciary > Case or Controversy > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

## **HN6** [down] Standing, Injury in Fact

The question of standing to sue under the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), is one of law. In order to determine whether a plaintiff has standing to bring an antitrust action, a court must review the allegations contained in the complaint. More than constitutional standing must exist; a court must find a close relationship between a plaintiff's injury and an alleged antitrust violation. Antitrust standing requires more than the injury in fact and the case or controversy required by Article III of the Constitution.

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **HN7** [down] Regulated Industries, Higher Education & Professional Associations

The United States Court of Appeals for the Eleventh Circuit uses a two-prong approach in deciding whether a plaintiff has antitrust standing. First, a plaintiff must establish that it has suffered "antitrust injury. As the United States Supreme Court has made clear, to have standing antitrust plaintiffs must prove more than injury causally linked to an illegal presence in the market, that is, but for causation. Plaintiffs must prove antitrust injury, which is to say injury of the type that the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful. Antitrust injuries include only those injuries that result from interference with the freedom to compete. Second, a plaintiff must establish that it is an efficient enforcer of the antitrust laws. This determination is predicated on the "target area test," which requires that an antitrust plaintiff both prove that he is within that sector of the economy endangered by a breakdown of competitive conditions in a particular industry and that he is the target against which anticompetitive activity is directed. A plaintiff must show that it is a customer or competitor in the relevant antitrust market.

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

Torts > Business Torts > General Overview

## **HN8** [down] **Commercial Interference, Prospective Advantage**

Under Florida law, the elements of tortious interference with a business relationship are: (1) the existence of a business relationship that affords plaintiff existing or prospective legal rights; (2) defendant's knowledge of the business relationship; (3) defendant's intentional and unjustified interference with the relationship; and (4) damage to plaintiff.

Torts > ... > Business Relationships > Intentional Interference > Elements

Torts > Business Torts > General Overview

Torts > ... > Commercial Interference > Business Relationships > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

## **HN9** [down] **Intentional Interference, Elements**

An action for tortious interference with a business relationship generally requires a business relationship evidenced by an actual and identifiable understanding or agreement which in all probability would have been completed if defendant had not interfered. A claim of tortious interference with a business relationship requires proof that plaintiff had a business relationship with "identifiable customers." The cause of action cannot be established by proof that defendant interfered with a relationship between plaintiff and the public at large.

Torts > ... > Defamation > Defenses > Fair Comment & Opinion

Torts > Intentional Torts > Defamation > General Overview

Torts > ... > Defamation > Elements > General Overview

## **HN10** [down] **Defenses, Fair Comment & Opinion**

Under Florida law, to state a cause of action for defamation, a plaintiff must allege that (1) defendant published a false statement (2) about plaintiff (3) to a third party and (4) that the falsity of the statement caused injury to plaintiff. Florida courts also recognize a distinction between a pure expression of opinion, which is not actionable, and a mixed expression of opinion. Pure opinion occurs when a defendant makes a comment or opinion based on facts which are set forth in the article or which are otherwise known or available to the reader or listener as a member of the public. Mixed expression of opinion occurs when an opinion or comment is made which is based upon facts regarding the plaintiff or his conduct that have not been stated in the article or assumed to exist by the parties to a communication.

Civil Procedure > Trials > Jury Trials > Province of Court & Jury

Torts > ... > Defamation > Defenses > Fair Comment & Opinion

Torts > Intentional Torts > Defamation > General Overview

Torts > Intentional Torts > Defamation > Procedural Matters

## **HN11** [blue icon] Jury Trials, Province of Court & Jury

In a defamation action, whether a statement is one of pure or mixed opinion is an issue of law. In determining whether a statement is one of pure or mixed opinion, a court must examine the statement in its totality and the context in which it was uttered or published. A court must consider all of the words used, not merely a particular phrase or sentence. A court must give weight to cautionary terms used by the person publishing the statement and consider all of the circumstances surrounding the statement, including the medium by which the statement is disseminated and the audience to which it is published.

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For Lee Memorial Health Systems, Inc., Defendant: Geoffrey P. Forgione, Julia C. Ambrose, Kevin D. McDonald, Toby G. Singer, Jones Day, Washington, DC; H. Jack Klingensmith, Walters Levine Brown Klingensmith & Thomison, PA, Sarasota, FL; Robert Clark McCurdy, Lee Memorial Health System, Ft. Myers, FL.

For Martin Memorial Health System, Martin Memorial Medical Center, Inc., Defendants: Jerome W. Hoffman, Holland & Knight LLP, Tallahassee, FL; Steven L. Brannock, David C. Borucke, Holland & Knight, LLP, Tampa, FL.

For Florida Hospital Association, Inc., Florida Hospital Association Management Corporation, Defendants: James R. Atwood, Jay T. Smith, Covington & Burling, Washington, DC; Robert L. Ciotti, Carlton [\*2] Fields, P.A., Tampa, FL.

**Judges:** JOHN E. STEELE, United States District Judge.

**Opinion by:** JOHN E. STEELE

## **Opinion**

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### **OPINION AND ORDER**

This matter comes before the Court on the following dispositive motions: (1) HCA defendants' Motion to Dismiss the Second Amended Complaint for Lack of Standing and for Failure to State a Claim (Doc. #108); (2) Martin Memorial's Motion to Dismiss Second Amended Complaint (Doc. #109); (3) Florida Hospital Association, Inc. and Florida Hospital Association Management Corporation's Motion to Dismiss Second Amended Complaint (Doc. #110); and (4) Defendants Lee Memorial Health System and Cape Memorial Hospital's Motion to Dismiss the Second Amended Complaint (Doc. #111). Plaintiff Medical Savings Insurance Company filed Plaintiff's Consolidated Memorandum in Opposition to Defendants' Motions to Dismiss Third Amended Complaint (Doc. #122).<sup>1</sup> Plaintiff filed a Notice of Supplemental Authority (Doc. #125) on February 24, 2005.

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<sup>1</sup> On January 4, 2005, plaintiff filed a motion for leave to file a third amended complaint omitting the claim under the Florida Deceptive and Unfair Trade Practices Act against all defendants. Plaintiff's other claims remain unaltered. The Court, on January 31, 2005, granted leave to amend the Second Amended Complaint and applied the pending Motions to Dismiss (Doc. ##108-111) to the Third Amended Complaint, with the exception of the arguments directed to FDUTPA, which became moot. (Doc. #117.) Thus, the remaining arguments in the subject motions are applicable to the Third Amended Complaint (Doc. #119).

[\*3] In an Order (Doc. #87) dated October 25, 2004, the Court dismissed certain counts with prejudice and other counts without prejudice. At plaintiff's request (Doc. #92), the Court allowed plaintiff to file another amended complaint to attempt to cure the deficiencies identified by the Court. (Doc. #104). Thus, for the reasons set forth in footnote one, the Third Amended Complaint (Doc. #119) is now the operative pleading. The Court freely plagiarizes from its October 25, 2004, Order where appropriate.

## I.

**HN1** [↑] In deciding a motion to dismiss, the Court must accept all factual allegations in a complaint as true and take them in the light most favorable to the plaintiff. *Christopher v. Harbury*, 536 U.S. 403, 406, 153 L. Ed. 2d 413, 122 S. Ct. 2179 (2002); *Hill v. White*, 321 F.3d 1334, 1335 (11th Cir. 2003). A complaint should not be dismissed unless it appears beyond doubt that plaintiff can prove no set of facts that would entitle it to relief. *Conley v. Gibson*, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957) (footnote omitted); *Marsh v. Butler County, Ala.*, 268 F.3d 1014, 1022 (11th Cir. 2001) (en banc). Even this liberal standard has its limits, however. *Dura Pharm., Inc. v. Broudo*, 544 U.S. 336, 161 L. Ed. 2d 577, 125 S. Ct. 1627, 1634 (2005). [\*4] Additionally, dismissal is warranted under *Fed. R. Civ. P. 12(b)(6)* if, assuming the truth of the factual allegations of plaintiff's complaint, there is a dispositive legal issue which precludes relief. *Neitzke v. Williams*, 490 U.S. 319, 326, 104 L. Ed. 2d 338, 109 S. Ct. 1827 (1989); *Brown v. Crawford County, Ga.*, 960 F.2d 1002, 1009-10 (11th Cir. 1992). The Court need not accept unsupported conclusions of law or of mixed law and fact in a complaint. *Marsh*, 268 F.3d at 1036 n.16.

**HN2** [↑] This standard applies when the Court reviews issues of standing pursuant to a motion to dismiss. The principal purpose of standing is to ensure that the parties before the Court have a concrete interest in the outcome of the proceedings such that they can be expected to properly frame the issues. *Harris v. Evans*, 20 F.3d 1118, 1121 (11th Cir. 1994) (en banc), cert. denied, 513 U.S. 1045, 115 S. Ct. 641, 130 L. Ed. 2d 546 (1994). Every complaint must contain sufficient allegations of standing. *Church v. City of Huntsville*, 30 F.3d 1332, 1336 (11th Cir. 1994), but the complaint may be dismissed for lack of standing only "if it is clear [\*5] that no relief could be granted under any set of facts that could be proved consistent with the allegations." *Jackson v. Okaloosa County, Fla.*, 21 F.3d 1531, 1534 (11th Cir. 1994) (citation omitted). Standing always remains an open issue, and can be revisited under a different standard at the summary judgment stage or at trial. *Church*, 30 F.3d at 1336; *Harris*, 20 F.3d at 1121 n.4. This having been said, it is still plaintiff's responsibility to allege facts sufficient to establish its standing, and the Court cannot "speculate concerning the existence of standing, nor should we imagine or piece together an injury sufficient to give plaintiff standing when it has demonstrated none." *Miccosukee Tribe of Indians of Fla. v. Florida State Athletic Comm'n*, 226 F.3d 1226, 1229-30 (11th Cir. 2000); see also *Shotz v. Cates*, 256 F.3d 1077, 1081 (11th Cir. 2001).

**HN3** [↑] In order to establish standing, a plaintiff must adequately allege, and ultimately prove, three elements: (1) that it has suffered an "injury-in-fact;" (2) a causal connection between the asserted injury-in-fact and the challenged conduct of the [\*6] defendant; and (3) that the injury likely will be redressed by a favorable decision. *Shotz*, 256 F.3d at 1081, citing *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 560, 119 L. Ed. 2d 351, 112 S. Ct. 2130 (1992). These requirements are the "irreducible minimum" required by the Constitution for a plaintiff to proceed in federal court. *Vermont Agency of Natural Res. v. United States*, 529 U.S. 765, 771, 146 L. Ed. 2d 836, 120 S. Ct. 1858 (2000); *Northeastern Fla. Chapter, Associated Gen. Contractors of Am. v. City of Jacksonville*, 508 U.S. 656, 664, 124 L. Ed. 2d 586, 113 S. Ct. 2297 (1993).

In addition, **HN4** [↑] a plaintiff seeking injunctive relief lacks standing unless it alleges facts giving rise to an inference that it will suffer future injury by the defendant. *Shotz*, 256 F.3d at 1081. "[A] party has standing to seek injunctive relief only if the party alleges, and ultimately proves, a real and immediate - as opposed to a merely conjectural or hypothetical - threat of future injury." *Church*, 30 F.3d at 1337; see also *Bowen v. First Family Fin. Servs., Inc.*, 233 F.3d 1331, 1340 (11th Cir. 2000).

## II.

The forty-six page Third Amended Complaint (Doc. #119) sets forth the following [\*7] material facts, which at this stage of the proceedings are assumed to be true. Plaintiff Medical Savings Insurance Company (plaintiff or Medical Savings) is an insurance company authorized to do business as an acute care hospitalization insurer in, among other places, the State of Florida. Plaintiff's hospitalization insurance product requires a fairly significant level of self-insurance by the patients/insureds through Health Savings Accounts. Plaintiff's insurance policies provide coverage for "reasonable and customary" hospital charges, not the commonly referenced "usual and customary" charges. Pursuant to this policy provision, plaintiff will not pay what it considers to be unreasonable overcharges by health care providers. Medical Savings is also a provider in the health care financial services market, which it views as making it a competitor with defendants in the "related and inextricably intertwined" health insurance market. (Doc. #119, P21).

Medical Savings qualified for the acute care hospitalization insurance market in Florida in 1997, and began actively marketing its insurance product in early 2000. Medical Savings has approximately 15,000 insureds in Florida. Florida [\*8] sales of its insurance policies rose generally at a substantial overall rate from April 2000 through December 2002. By December 2003, however, the sales growth of its insurance product in Florida had significantly declined, and this decline continued through the filing of the Third Amended Complaint. Plaintiff contends that this decline in sales growth and volume is attributable to certain unlawful actions (concerted refusal to deal or conspiracy to boycott, inflated prices, group boycott, deceptive practices, defamation, and wrongful business interference) by the defendants. Plaintiff describes the eight defendants as the principal Florida hospital "malfeasors," their principal acute care hospital "co-conspirators," and their trade association.

Defendant HCA, Inc. (HCA) is a for-profit hospital system with 41 acute care hospitals in Florida, and is a publicly traded company on the New York Stock Exchange. Defendant HCA Health Services of Florida, Inc. (HCA Florida) is a for-profit hospital system with 3 or more acute care hospitals in Florida.<sup>2</sup> HCA and HCA Florida are dominant or controlling members of defendant Florida Hospital Association, Inc. HCA controls over 10,000 acute [\*9] care hospital beds in Florida, and are dominant providers of acute care hospital beds in Florida.

Defendant Lee Memorial Health System (LMHS) operates three acute care hospitals: Cape Memorial Hospital, Lee Memorial Hospital, and Lee Memorial Health System Health Park. Lee Memorial Hospital and Lee Memorial System Health Park are registered fictitious names for LMHS. Cape Memorial Hospital is owned by defendant Cape Memorial Hospital, Inc.<sup>3</sup> Defendant LMHS is a member of defendant Florida Hospital Association, Inc., and controls over 900 acute care hospital beds in Florida. In the past two years, the Lee Memorial defendants have initiated litigation against plaintiff and its insureds.

[\*10] Defendants Martin Memorial Health Systems, Inc. and Martin Memorial Medical Center, Inc. are non-profit corporations that operate two acute care hospitals in Florida.<sup>4</sup> The Martin defendants have a total of 336 acute care hospital beds in Florida. Defendant Martin Memorial Medical Center, Inc. has initiated litigation against some of plaintiffs' insureds.

Defendant Florida Hospital Association, Inc. (FHA) is a tax-exempt, non-profit entity composed, in part, of 47 hospital systems that operate 322 acute care hospitals in Florida. Defendant Florida Hospital Association Management Corporation is a wholly owned subsidiary of defendant FHA.<sup>5</sup> Defendant FHA, through its FHA Insurance Services, competes with plaintiff in the Florida market for acute care hospitalization insurance by writing, selling, or otherwise providing such insurance. Defendant [\*11] FHA has coordinated or attempted to coordinate

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<sup>2</sup> Where appropriate, the Court will refer to defendants HCA, Inc. and HCA Health Services of Florida, Inc. collectively as HCA.

<sup>3</sup> Where appropriate, the Court will refer to defendants Lee Memorial Health System and Cape Memorial Hospital collectively as the Lee Memorial defendants.

<sup>4</sup> Where appropriate, the Court will refer to defendants Martin Memorial Health Systems, Inc. and Martin Memorial Medical Center, Inc. collectively as the Martin defendants.

<sup>5</sup> Where appropriate, the Court will refer to defendants Florida Hospital Association and Florida Hospital Association Management Corporation collectively as FHA.

legal action against plaintiff and has urged its members to avoid a dispute resolution program established by the Florida legislature.<sup>6</sup>

The eight-count Third Amended Complaint (Doc. #119) alleges the following causes of action: (1) violation of Section 1 of the Sherman Act (group boycott and/or concerted refusal to deal) as to six defendants; (2) violation of Section 1 of the Sherman Act (price-fixing conspiracy) as to all defendants; (3) violation of section 2 of the Sherman Act (monopolization) as to two defendants; (4) violation of Florida's Antitrust Act (price-fixing and group boycott and/or concerted refusal to deal) as to all defendants; (5) [\*12] violation of Florida's Antitrust Act (monopolization) as to one defendant; (6) tortious interference with business relations under Florida law, apparently as to all defendants; (7) defamation under Florida law as to two defendants; and (8) injunctive relief pursuant to Section 16 of the Clayton Act as to all defendants.

Count I alleges that six defendants (all except Lee Memorial Health System and Cape Memorial Hospital) entered into a contract, combination, or conspiracy to refuse to deal with and to boycott Medical Savings in order to maintain, enhance or further solidify their concerted efforts to stabilize inflated prices for acute care hospitalization services, in violation of Section 1 of the Sherman Act, 15 U.S.C. § 1. Plaintiff asserts this was either a *per se* violation of § 1, or a violation of the "rule of reason" standard. The unlawful behaviors by defendants are alleged to include: (1) rejecting payments tendered by Medical Savings for hospital goods and services; (2) refusing medical treatment to Medical Savings' insureds; (3) refusing to recognize Medical Savings' insurance when admitting patients; (4) requiring Medical Savings' insureds to [\*13] pay in advance before treatment is rendered; (5) coordinating sham litigation against Medical Savings and/or its insureds solely to deter challenges to defendants' inflated prices; (6) coercing insureds/patients into suing Medical Savings; and (7) making false statements to current and prospective insureds that Medical Savings refuses to pay and/or has not paid reasonable hospital charges. Plaintiff further alleges that the purpose of the boycott and refusal to deal with Medical Savings is to (1) punish Medical Savings for challenging inflated hospital prices, and (2) force Medical Savings out of the Florida health insurance market. Plaintiff alleges that defendants' behavior has resulted in antitrust injuries to competition in the acute care hospitalization services market and the healthcare insurance market, with the following specific antitrust injuries to Medical Savings: (1) lost customers; (2) lost sales; (3) lost revenue; (4) lost profits; (5) lost goodwill; (6) lost business opportunities in the healthcare insurance market; and (7) litigation expenses resulting from a pattern of "sham" proceedings initiated solely to further defendants' anti-competitive scheme. Plaintiff alleges [\*14] that these injuries are distinct from injuries suffered by its insureds.

Count II alleges that all defendants entered into one or more agreement(s) to set prices in the acute care hospitalization services market at artificially elevated levels which bore no relation to the true prices that would prevail in a competitive marketplace, in violation of §1 of the Sherman Act. Plaintiff asserts this was either a *per se* violation of §1, or a violation of the "rule of reason." The unlawful behaviors by defendants are alleged to include: (1) knowingly sending inflated invoices to Medical Services and demanding full payment; (2) rejecting payments for the reasonable value for goods and services rendered; and (3) initiating efforts to collect on the inflated amounts. The efforts to collect on the artificially inflated invoices are alleged to have caused the same seven antitrust injuries to Medical Savings as described in Count I.

Count III alleges that HCA and LMHS conspired and attempted to monopolize the acute care health services market in Lee County, Florida. Defendants are alleged to have charged "supra-competitive prices" to Medical Savings and to patients, and to have engaged in [\*15] anticompetitive conduct, including the deliberate misrepresentation and/or concealment of material facts and information concerning the true economic cost of acute care from patients and their insurers. Plaintiff asserts that while HCA does not compete in the health insurance services market, its monopolistic behavior in the acute care hospitalization services market has direct and substantial impact on insurers like Medical Savings by raising prices which insurers are obligated to pay. Plaintiff asserts that HCA's attempts to collect the excessive overcharges have caused and continue to cause injury to Medical Savings, even though it is not responsible to pay for the artificially inflated prices. This injury is the

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<sup>6</sup> In addition to the named defendants, the Third Amended Complaint identifies some 23 "possible co-conspirators" to this action. (Doc. #119, p. 25).

hindrance of Medical Savings' ability to renew and sell Hospital Savings Accounts to current and prospective insureds. The use of the monopoly power to inflate invoices and enforce payment is alleged to have caused the same seven antitrust injuries to Medical Savings as described in Count I and Count II.

Count V alleges violation of [Florida's Antitrust Act](#) by all defendants through a contract, combination or conspiracy in constraint of Medical Savings' trade and in constraint [\*16] of competitive commerce in the acute health care hospitalization market place. Plaintiff adopts the prior allegations set forth in Counts I through Count III.

Count VI alleges violation of [Florida's Antitrust Act](#) by defendant HCA based on its monopolistic conduct targeting trade or commerce in the acute health care hospitalization marketplace in Florida. Plaintiff adopts the prior allegations set fourth in Counts III and Count V.

Count VII alleges tortious interference with business relations, apparently by all defendants. Plaintiff asserts that it had valid contractual relationships with its insureds, that defendants intentionally interfered with its insureds and induced breach or termination of the existing and prospective business relationships, and that Medical Savings lost current and prospective business relationships and incurred significant litigation expenses. The interference consisted of: (1) refusing to provide medical treatment to Medical Savings' insureds; (2) refusing to recognize Medical Savings' insurance when admitting its insureds; (3) requiring Medical Savings' insureds to provide down payments as condition precedent to treatment; (4) instituting sham litigation [\*17] against Medical Savings' insureds for purposes of coercing them to aid and abet defendants' illicit practices; (5) misleading Medical Savings' insureds by telling them that Medical Savings does not pay reasonable charges for hospital goods and services; and (6) defaming Medical Savings to its insureds by telling patients and the public that Medical Savings does not honor its contractual obligation to pay reasonable amounts for hospital goods and services.

Count VIII alleges that LMHS and MMMC used defamatory language concerning Medical Savings to current and prospective insureds which was false and which adversely affected Medical Savings' reputation in the health insurance market. More specifically, plaintiff alleges that LMHS sent a letter to an insured stating "You need to be aware that Medical Savings Health Plan is engaged in a practice, state-wide, of discounting hospital bills and claiming that the charges are not 'reasonable.' Unfortunately, Medical Savings Health Plan does not appear to have any factual basis for its assertions in this regard. This policy of Medical Savings seems to be based on the desire to maximize its profits by under-paying hospitals, rather than on any [\*18] real survey of the marketplace." Plaintiff alleges that MMMC sent a letter to an insured stating "I would like to explain why we do not accept your insurance plan. The Florida Department of Insurance has recommended that hospitals not accept the plan.... Your insurance company ... arbitrarily pays whatever it deems appropriate." Plaintiff alleges that these false statements were made with malice to further the conspiracy to protect defendants' inflated pricing scheme, and resulted in actual lost sales, lost profits, lost customers, lost business opportunities, and lost goodwill.

In Count IX, plaintiff re-alleges all its prior statements and claims entitlement to injunctive relief under [Section 16](#) of the Clayton Act and Florida law.

### III.

Defendants assert that dismissal of claims in the Third Amended Complaint is warranted on the following grounds: (1) plaintiff lacks antitrust standing and antitrust injury, (2) plaintiff fails to make any specific allegations of a conspiracy, and (3) plaintiff fails to plead essential elements under Florida law for its state common law claims.

#### A. Antitrust Standing

Defendants contend that plaintiff's antitrust claims (Counts I, II, [\*19] III, V, VI, and IX) must be dismissed because there is an absence of facts supporting plaintiff's antitrust standing.<sup>7</sup> Because plaintiff cannot show antitrust standing, the Court will dismiss the antitrust counts.

**HN6**[] The question of standing to sue under the *Sherman Act* is one of law. *Todorov v. DCH Healthcare Auth.*, 921 F.2d 1438, 1448 (11th Cir. 1991); *Austin v. Blue Cross and Blue Shield of Ala.*, 903 F.2d 1385, 1387 (11th Cir. 1990)). In order [\*20] to determine whether a plaintiff has standing to bring an antitrust action, a court must review the allegations contained in the complaint. *Austin*, 903 F.2d at 1387. More than constitutional standing must exist; "the court must find a close relationship between the plaintiff's injury and the alleged antitrust violation." *Id.*, quoting *Amey, Inc. v. Gulf Abstract & Title, Inc.*, 758 F.2d 1486, 1493 (11th Cir. 1985) (internal quotes omitted); *see also Florida Seed Co., Inc. v. Monsanto Co.*, 105 F.3d 1372, 1374 (11th Cir. 1997) ("Antitrust standing requires more than the injury in fact and the case or controversy required by Article III of the Constitution.") (internal quotes and citation omitted).

**HN7**[] The Eleventh Circuit uses a two-prong approach in deciding whether a plaintiff has antitrust standing. *Florida Seed Co., Inc.*, 105 F.3d at 1374, citing *Municipal Utils. Bd. of Alberville v. Alabama Power Co.*, 934 F.2d 1493, 1499 (11th Cir. 1991). First, the plaintiff must establish that it has suffered "antitrust injury." *Municipal Utils. Bd. of Alberville*, 934 F.2d at 1499. "As the Supreme [\*21] Court has made clear, to have standing antitrust plaintiffs 'must prove more than injury causally linked to an illegal presence in the market, [i.e., but for causation]. Plaintiffs must prove antitrust injury, which is to say injury of the type that the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful.'" *Florida Seed*, 105 F.3d at 1374, quoting *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977). "Antitrust injuries include only those injuries that result from interference with the freedom to compete." *Johnson v. University Health Servs., Inc.*, 161 F.3d 1334, 1338 (11th Cir. 1998).

"Second, the plaintiff must establish that it is an efficient enforcer of the antitrust laws." *Florida Seed*, 105 F.3d at 1374, citing *Municipal Utils. Bd. of Alberville*, 934 F.2d at 1499. This determination is predicated on the "target area test," which "requires that an antitrust plaintiff both 'prove that he is within that sector of the economy endangered by a breakdown of competitive conditions in a particular industry' and that he is 'the target against which [\*22] anticompetitive activity is directed.'" *Florida Seed*, 105 F.3d at 1374, quoting *National Indep. Theatre Exhibitors, Inc. v. Buena Vista Distribution Co.*, 748 F.2d 602, 608 (11th Cir. 1984). "Basically, a plaintiff must show that it is a customer or competitor in the relevant antitrust market." *Florida Seed*, 105 F.3d at 1374, citing *Associated Gen. Contractors of Cal., Inc. v. California State Council of Carpenters*, 459 U.S. 519, 539, 74 L. Ed. 2d 723, 103 S. Ct. 897 (1983).

Despite its new allegations, the Third Amended Complaint fails to allege antitrust standing. The core allegations are that Medical Savings has a hospitalization insurance policy that it offers to consumers; this hospitalization insurance policy is a contractual agreement between Medical Savings and its insureds; pursuant to this contract. Medical Savings agrees to pay those hospital charges which Medical Savings finds to be "reasonable and customary," and only those charges; Medical Savings does not pay those portions of hospital charges it determines are not "reasonable and customary;" Medical Savings has no contractual relationships with the defendants, and defendants have not [\*23] agreed to accept the payments which Medical Savings finds to be "reasonable and customary" as full satisfaction for its services; and Medical Savings' insureds are responsible to the defendant hospitals for payment of those portions of the hospital bills not paid by Medical Services.

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<sup>7</sup> **HN5**[] The Florida Antitrust Act, *FLA. STAT. § 542.15 et seq.*, was patterned after the Sherman Act, and was intended to complement and follow the federal court interpretations of the *Sherman Act*. *FLA. STAT. § 542.32*; *Auton v. Dade City, Fla.*, 783 F.2d 1009, 1010 n.1 (11th Cir. 1986). Accordingly, the Court's rulings on Counts I, II, and III, based on the *Sherman Act*, will apply as well to Counts V and VI, which assert parallel charges under the *Florida Antitrust Act*.

With respect to the first prong, plaintiff has not alleged an antitrust injury to itself. There is no allegation which would indicate an interference with the freedom to compete in the health care insurance business.<sup>8</sup> Quite the contrary, plaintiff markets a health insurance product that consumers are free to purchase if, as with any insurance product, they deem the coverage worth the premium. While lost sales and profits have been recognized as antitrust injuries in the Third Circuit, that court found those losses to be cognizable injuries when they were linked with actual payments of alleged overcharges. See *Pennsylvania Dental Ass'n v. Medical Serv. Ass'n of Pa.*, 815 F.2d 270 (3d Cir. 1987). That is not the case here. Plaintiff made no payments of overcharges, but only partial payments which plaintiff, at its discretion, determined to be reasonable. Plaintiff has cited no binding [\*24] case authority in which the alleged injuries were sufficient for antitrust standing without the actual payment of the alleged overcharges.

Additionally, plaintiff clearly falls short of the second prong. Plaintiff contends that it has antitrust standing under a direct purchaser theory, that is, that plaintiff also "purchases" the medical services through its insureds. The Court concludes that plaintiff is neither a customer nor a competitor of these defendants. Unlike *Pennsylvania Dental Ass'n*, plaintiff does not utilize a pre-paid insurance plan whereby the medical services have already been purchased. Plaintiff cannot base its injuries on an occurrence - payment of the alleged overcharge - that has not happened and which under its contractual obligations will never happen. [\*25] Moreover, plaintiff does not fall within the target area of the alleged misconduct. As discussed in a prior Order, the targets are the patients, not an insurer such as plaintiff.

Moreover, the patients, as direct purchasers, would be the efficient enforcer.<sup>9</sup> *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 735, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977) ("antitrust laws will be more effectively enforced by concentrating the full recovery for the overcharge in the direct purchasers rather than by allowing every plaintiff potentially affected by the overcharge to sue only for the amount it could show was absorbed by it.")

[\*26] Plaintiff's complaints, in essence, stem from a lack of market demand for its particular insurance product in the absence of an agreement by defendants to accept plaintiff as the arbiter of reasonable service fees. Nothing in the **antitrust law** compels defendants to acquiesce to such a role by an insurer. The Third Amended Complaint does not allege that plaintiff has suffered an antitrust injury<sup>10</sup>, and therefore the antitrust related claims will be dismissed.

## B. State Common Law Claims

### (1) Tortious Interference of Business Relations

Plaintiff alleges that, as a result of defendants' conduct, plaintiff's "ability to sell insurance to prospective insureds and renew policies for current insureds has been hindered...." (Doc. #119, pp. 26-27.) Defendants [\*27] contend that plaintiff fails to state a claim under Count VII (tortious interference with business relations) because (1) there are no allegations that plaintiff's current insureds breached any contract with plaintiff, and (2) plaintiff's allegation of defendants' interference with its prospective insureds is insufficient because plaintiff fails to allege identifiable customers and renewals are not protected.

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<sup>8</sup>While plaintiff asserts it is a provider in the health care financial services market, there are no allegations at all about its activities in this market or support for its assertion that this makes it a competitor of defendants.

<sup>9</sup>Plaintiff urges the Court to find that plaintiff has standing to pursue injunctive relief because the law does not require an efficient enforcer under **section 16**. (Doc. #122, pp. 29-30.) The Court disagrees. Standing for injunctive relief under the antitrust laws requires that the plaintiff allege "threatened injury that would constitute antitrust injury if inflicted upon the plaintiff and the defendant's causal responsibility for such threatened injury." *Todorov*, 921 F.2d at 1452. Having found that plaintiff does not suffer from antitrust injury, the Court concludes that plaintiff does not have standing to seek injunctive relief.

<sup>10</sup>Because of the Court's conclusion that plaintiff lacks antitrust standing to pursue its antitrust claims, the Court will not consider defendants' remaining arguments regarding the alleged pleading deficiencies of plaintiff's antitrust claims.

**HN8** [↑] Under Florida law, the elements of tortious interference with a business relationship are: (1) the existence of a business relationship that affords the plaintiff existing or prospective legal rights; (2) the defendant's knowledge of the business relationship; (3) the defendant's intentional and unjustified interference with the relationship; and (4) damage to the plaintiff. *International Sales & Serv., Inc. v. Austral Insulated Prods., Inc.*, 262 F.3d 1152, 1154 (11th Cir. 2001), citing *Ethan Allen, Inc. v. Georgetown Manor*, 647 So. 2d 812, 814 (Fla. 1994); see also *Salit v. Ruden, McClosky, Smith, Schuster & Russell, P.A.*, 742 So. 2d 381, 385-86 (Fla. 4th DCA 1999), citing *Tamiami Trail Tours, Inc. v. Cotton*, 463 So. 2d 1126, 1127 (Fla. 1985). [\*28]

As the Florida Supreme Court said in *Ethan Alien Inc.*, **HN9** [↑] an action for tortious interference with a business relationship generally requires "a business relationship evidenced by an actual and identifiable understanding or agreement which in all probability would have been completed if the defendant had not interfered." *647 So. 2d 812, 815*. The Court added in *Ferguson Transp. Inc. v. North Am. Van Lines*, that a claim of tortious interference with a business relationship requires proof that the plaintiff had a business relationship with "identifiable customers." *687 So. 2d 821, 821 (Fla. 1996)*. The cause of action cannot be established by proof that the defendant interfered with a relationship between the plaintiff and the public at large. *Sarkis v. Pafford Oil Co., Inc.*, 697 So. 2d 524, 526-27 (Fla. 1st DCA 1997).

The Court agrees with defendants' positions. The Third Amended Complaint does not allege that existing insureds were induced to breach their contracts with plaintiff or that any breach occurred. A non-renewal of an insurance policy does not constitute an induced breach, since plaintiff does not allege any agreement with its [\*29] existing insureds that they would renew their policies at the end of the current term. The mere hope that some of its past insureds may choose to renew their policy cannot be the basis for a tortious interference claim under Florida law. Therefore, plaintiff fails to state a claim, with respect to its current insureds, for tortious interference with business relations.

With respect to prospective customers, the Third Amended Complaint does not identify "a business relationship evidenced by an actual and identifiable understanding or agreement which in all probability would have been completed if the defendant had not interfered." *Ethan Allen, Inc.*, *647 So. 2d at 815*. No cause of action exists for tortious interference with a business's relationship to the community at large. *Id.* Thus, plaintiff fails to state a claim under Count VII.

## (2) Defamation

Defendants Lee Memorial Health System and Martin Memorial Medical Center contend that the subject statements are pure opinion, and thus plaintiff's defamation count fails to state a claim. Plaintiff challenges the veracity of the subject statements, and thus insists then that a jury should resolve the issue [\*30] of whether the statements are false.

**HN10** [↑] Under Florida law, to state a cause of action for defamation, a plaintiff must allege that (1) the defendant published a false statement (2) about the plaintiff (3) to a third party and (4) that the falsity of the statement caused injury to the plaintiff. *Valencia v. Citibank Int'l*, 728 So. 2d 330, 330 (Fla. 3d DCA 1999). Florida courts also recognize a distinction between a pure expression of opinion, which is not actionable, and a mixed expression of opinion. *Sullivan v. Barrett*, 510 So. 2d 982, 983-84 (Fla. 4th DCA 1987); see also *From v. Tallahassee Democrat, Inc.*, 400 So. 2d 52, 56 (Fla. 1st DCA 1981). Pure opinion occurs when a defendant makes a comment or opinion based on facts which are set forth in the article or which are otherwise known or available to the reader or listener as a member of the public. *Hoch v. Rissman, Weisberg, Barrett*, 742 So. 2d 451, 459 (Fla. 5th DCA 1999), citing *Miami Child's World, Inc. v. Sunbeam Television Corp.*, 669 So. 2d 336 (Fla. 3d DCA 1996). Mixed expression of opinion occurs when an opinion or comment is made which is based [\*31] upon facts regarding the plaintiff or his conduct that have not been stated in the article or assumed to exist by the parties to the communication. *Hoch*, *742 So. 2d at 459-60*.

**HN11** [↑] Whether a statement is one of pure or mixed opinion is an issue of law. *Id. at 460*. In determining whether the statement is one of pure or mixed opinion, the court must examine the statement in its totality and the context in

which it was uttered or published. Id. The court must consider all of the words used, not merely a particular phrase or sentence. Id. In addition, the court must give weight to cautionary terms used by the person publishing the statement and consider all of the circumstances surrounding the statement, including the medium by which the statement is disseminated and the audience to which it is published. Id.

The Court agrees with defendants. While defendants published these statements to third parties - plaintiff's insureds - the Court finds the statements constitute opinions and are therefore not actionable. Defendants' statements are based on plaintiff's refusal to render full payment of the amount due. Plaintiff concedes that it makes only partial [\*32] payments, and admits that the payment amount is based upon what plaintiff deems as reasonable for . the particular service. Viewing the statements in the context in which they were published, the Court concludes that the subject remarks are opinions. Because opinions cannot be the basis for a defamation claim, plaintiff fails to state a claim for defamation against defendants. Thus, the defamation claim is due to be dismissed.

Plaintiff's request for leave to file yet another amended complaint is denied. Plaintiff has been afforded several opportunities to allege viable claims, and failed to do so. Moreover, plaintiff has not provided any basis for the Court to grant leave to amend the Third Amended Complaint.

Accordingly, it is hereby

**ORDERED:**

1. HCA defendants' Motion to Dismiss the [Third] Amended Complaint for Lack of Standing and for Failure to State a Claim (Doc. #108) is **GRANTED**;
2. Martin Memorial's Motion to Dismiss [Third] Amended Complaint (Doc. #109) is **GRANTED**;
3. Florida Hospital Association, Inc. and Florida Hospital Association Management Corporation's Motion to Dismiss [Third] Amended Complaint (Doc. #110) is **GRANTED**;
4. Defendants [\*33] Lee Memorial Health System and Cape Memorial Hospital's Motion to Dismiss the [Third] Amended Complaint (Doc. #111) is **GRANTED**;
5. Plaintiff's request for leave to amend the Third Amended Complaint is **DENIED**; and
6. The Clerk shall enter judgment in favor of defendants and against plaintiff. The Clerk shall terminate any pending motions or deadlines, and close the file.

**DONE AND ORDERED** at Fort Myers, Florida, this 24th day of June, 2005.

**JOHN E. STEELE**

**United States District Judge**



## **Asociacion de Detallistas de Gasolina de P.R., Inc. v. Shell Chem. Yabucoa Inc.**

United States District Court for the District of Puerto Rico

July 5, 2005, Decided

CIVIL NO. 04-1848 (JAG)

### **Reporter**

380 F. Supp. 2d 40 \*; 2005 U.S. Dist. LEXIS 15930 \*\*; 2005-2 Trade Cas. (CCH) P74,917

Asociacion de Detallistas de Gasolina de Puerto Rico, Inc., represented by its President, Efrain Reyes Hernandez Plaintiff(s) v. Shell Chemical Yabucoa Inc., et al. Defendant(s)

### **Core Terms**

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removal, Writs, cause of action, federal court, questions

### **LexisNexis® Headnotes**

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Civil Procedure > ... > Removal > Elements for Removal > Federal Venue

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > Preliminary Considerations > Removal > General Overview

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Civil Procedure > ... > Removal > Elements for Removal > General Overview

#### **HN1[] Elements for Removal, Federal Venue**

See [28 U.S.C.S. § 1441\(a\)](#).

Civil Procedure > ... > Removal > Procedural Matters > General Overview

#### **HN2[] Removal, Procedural Matters**

A removal notice shall be filed within thirty days after receipt by the defendant, through service or otherwise, of a copy of the complaint. [28 U.S.C.S. 1446\(b\)](#).

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

380 F. Supp. 2d 40, \*40L2005 U.S. Dist. LEXIS 15930, \*\*15930

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

Civil Procedure > ... > Removal > Procedural Matters > General Overview

### **HN3** Removal, Specific Cases Removed

The United States Supreme Court of the United States has held that, in deciding (for removal purposes) whether a case presents a federal claim or right, a court is to ask whether the plaintiff's claim to relief rests upon a federal right, and the court is to look only to the plaintiff's complaint to find the answer.

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

### **HN4** Removal, Specific Cases Removed

The existence of a federal defense is not sufficient for removal jurisdiction.

Civil Procedure > ... > Jurisdiction > Jurisdictional Sources > General Overview

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > Limited Jurisdiction

### **HN5** Jurisdiction, Jurisdictional Sources

Federal courts are courts of limited jurisdiction.

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

Governments > Legislation > Statutory Remedies & Rights

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

### **HN6** Subject Matter Jurisdiction, Federal Questions

While a defendant does have a right, given by statute, to remove in certain situations, a plaintiff is still the master of his own claim. As master of his own claim, a plaintiff may avoid federal jurisdiction by exclusive reliance on state law.

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Evidence > Burdens of Proof > General Overview

380 F. Supp. 2d 40, \*40LAW2005 U.S. Dist. LEXIS 15930, \*\*15930

Civil Procedure > ... > Removal > Procedural Matters > General Overview

#### **HN7[] Removal, Specific Cases Removed**

When a party questions the propriety of a removal petition, the removing party bears the burden of showing that removal is proper.

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Governments > Legislation > Interpretation

#### **HN8[] Removal, Specific Cases Removed**

Removal statutes are strictly construed against removal.

Civil Procedure > ... > Removal > Postremoval Remands > Jurisdictional Defects

Civil Procedure > ... > Removal > Postremoval Remands > General Overview

#### **HN9[] Postremoval Remands, Jurisdictional Defects**

When a plaintiff and a defendant clash about jurisdiction, uncertainties are construed in favor of remand.

Civil Procedure > ... > Removal > Procedural Matters > General Overview

Constitutional Law > Supremacy Clause > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

#### **HN10[] Removal, Procedural Matters**

The United States Supreme Court has clearly ruled that a plaintiff can prevent removal by choosing not to pursue federal claims that are potentially available, without incurring in the artful pleading exception recognized in *Franchise Tax Board v. Construction Laborers Vacation Trust*. In fact, the Supreme Court has noted that the artful pleading doctrine only allows removal where federal law completely preempts a plaintiff's state law claim.

Banking Law > Consumer Protection > State Law > General Overview

Constitutional Law > Supremacy Clause > General Overview

Energy & Utilities Law > Natural Gas Industry > General Overview

Antitrust & Trade Law > Consumer Protection > General Overview

380 F. Supp. 2d 40, \*40L2005 U.S. Dist. LEXIS 15930, \*\*15930

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Energy & Utilities Law > Oil & Petroleum Products > Gasoline Fuels > Gasoline Dealers & Distributors

## [\*\*HN11\*\*](#) [ ] Consumer Protection, State Law

Neither the Puerto Rico Gasoline Law, 23 P.R. Laws Ann. § 1101 et seq., nor the Puerto Rico **Antitrust Law**, 10 P.R. Laws Ann. § 257 et seq., is preempted by federal law.

Civil Procedure > Remedies > Writs > All Writs Act

Civil Procedure > ... > Jurisdiction > Jurisdictional Sources > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > Remedies > Writs > General Overview

## [\*\*HN12\*\*](#) [ ] Writs, All Writs Act

While the All Writs Act (Act), [28 U.S.C.S. § 1651](#), does empower a federal court to issue all the writs necessary to protect its jurisdiction, the United States Supreme Court has held that the Act is not an independent source of federal subject-matter jurisdiction.

Civil Procedure > Remedies > Writs > All Writs Act

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Civil Procedure > Remedies > Writs > General Overview

## [\*\*HN13\*\*](#) [ ] Writs, All Writs Act

The All Writs Act, [28 U.S.C. § 1651](#), does not give federal courts authority to remove a state court case in order to prevent frustration of orders a federal court has previously issued. Rather, removal is only be proper if the federal court independently has original subject-matter jurisdiction over the suit.

Civil Procedure > Preliminary Considerations > Removal > General Overview

Evidence > Burdens of Proof > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Removal > Specific Cases Removed > General Overview

Civil Procedure > ... > Removal > Elements for Removal > General Overview

Civil Procedure > ... > Removal > Elements for Removal > Removability

Civil Procedure > Remedies > Writs > General Overview

## HN14 [ ] Preliminary Considerations, Removal

Defendants must demonstrate that a state cause of action is removable under [28 U.S.C. § 1441](#) in order for the All Writs Act, [28 U.S.C. § 1651](#), to control the removal. Where the plaintiff's state action is not removable under [28 U.S.C. § 1441](#), the All Writs Act does not empower a federal court to entertain the case on removal.

**Counsel:** [\*\*1] For Plaintiffs: Carlos E. Montanez, Carlos E. Montanez Law Office, San Juan, PR.

For Defendants: Frank La Fontaine-Maestre, Samuel T. Cespedes, McConnell Valdes, San Juan, PR; Ana M. Nin-Torregrosa, Nin Torregrosa & Rodriguez Ruiz Law Office, San Juan, PR; Alberto G. Estrella, William Estrella Law Offices, San Juan, PR; Carlos A. Valldejuly-Sastre, Hermann D. Bauer-Alvarez, O'Neill & Borges, San Juan, PR.

**Judges:** Jay A. Garcia-Gregory, United States District Judge.

**Opinion by:** Jay A. Garcia-Gregory

## Opinion

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### [\*41] OPINION AND ORDER

Pending before this Court is Plaintiffs' Motion to Remand (Docket No. 14). After carefully reviewing the record, the Court **GRANTS** the Motion and **REMANDS** the case to the Puerto Rico Court of First Instance.

### PROCEDURAL BACKGROUND

Asociacion de Detallistas de Gasolina Puerto Rico ("ADG") filed a civil action in the Puerto Rico Court of First Instance seeking a declaratory judgment under Rule 59 of the Puerto Rico Rules of Civil Procedure.<sup>1</sup> In that action, ADG questions the legality under state law of certain incentive programs implemented by the defendants.

[\*\*2] On August 17th, 2004, Shell Chemical Yabucoa Inc., and the Shell Company (Puerto Rico) Ltd., filed a "Notice of Removal" of the state action filed by ADG. (Docket No. 1). Shortly thereafter, the Esso Standard Oil Company of Puerto Rico and Texaco Puerto Rico Inc., filed motions joining Shell (collectively, "defendants") in its "Notice of Removal." (Dockets No. 10 and 11).

Defendants contend that this Court has original jurisdiction over the matter pursuant to [28 U.S.C. § 1331](#). Alternatively, defendants contend that under the All Writs Act, [28 U.S.C. § 1651](#), this Court is empowered to remove the state proceeding in order to protect the integrity of an [\*42] order issued in case No. 04-1141 (JAF), in which a settlement agreement between Shell and other defendants was approved by this Court.<sup>2</sup>

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<sup>1</sup> Asociacion de Detallistas de Gasolina de Puerto Rico, Inc. v. Shell Chemical Yabucoa Inc., The Shell Company (Puerto Rico) Ltd.; Texaco de Puerto Rico Inc.; Esso Standard Oil Company of Puerto Rico Inc., KAC-2004-5026 (Docket 1, Exhibit 1).

<sup>2</sup> Section 2 of the "Settlement Agreement" provides that

Notification of any order, action, filing, intervention or proceeding, which intends to restrict, or by operation restricts, Shell's use or conduct of its Price Incentive Program shall be personally notified to Shell at least ten (10) business days prior to seeking enforcement of the same. The parties expressly understand and agree that, should any such event occur, the Plaintiffs may move to reopen Civil No. 04-1441-JAF. All arguments and objections, as well as the defenses raised by the Defendants in that case, and those that may result from or arise in any other action, intervention or proceeding, are hereby expressly preserved and reserved.

[\*\*3] ADG then filed a "Motion for Remand" stating that no federal cause of action is actually alleged in state court and hence the case is not removable regardless of whether a federal claim could have been alleged. (Docket No. 14). ADG further states that it was never a party in case 04-1441 (JAF) and thus the settlement agreement reached in that case is not binding upon it. Moreover, ADG alleges that even if it had been a party, remand is still appropriate because the All Writs Act cannot be used to confer federal jurisdiction where another statute specifically addresses the particular issue at hand (referring to the removal statute, [28 U.S.C. § 1441\(a\)](#)).

On September 24th, 2004, defendant Shell filed a "Consolidated Motion for More Definite Statement and Opposition to Motion for Remand." (Docket No. 20). On October 1st, 2004, both Esso and Texaco joined Shell's request for a more definite statement under [Rule of Civil Procedure 12\(e\)](#). (Dockets No. 21 and 22).

## DISCUSSION

### A. Standard

Pursuant to [HN1](#) [28 U.S.C. § 1441\(a\)](#), "any civil action brought in a State court of which the district courts of the United States have original jurisdiction, [\*\*4] may be removed by the defendant or the defendants, to the district court of the United States for the district and division embracing the place where such action is pending." [City of Chicago v. International Coll. of Surgeons](#), 522 U.S. 156, 163-64, 139 L. Ed. 2d 525, 118 S. Ct. 523 (1997). [HN2](#) The removal notice "shall be filed within thirty days after receipt by the defendant, through service or otherwise, of a copy of the [Complaint]." [28 U.S.C. 1446\(b\)](#).

[HN3](#) The Supreme Court of the United States has held that, in deciding (for removal purposes) whether a case presents a federal claim or right, a court is to ask whether the plaintiff's claim to relief rests upon a federal right, and the court is to look only to plaintiff's complaint to find the answer. [Rossello-Gonzalez v. Calderon-Serra](#), 398 F.3d 1, 10 (1st Cir. 2004); [Hernandez-Agosto v. Romero-Barcelo](#), 748 F.2d 1, 2 (1st Cir. 1984). [HN4](#) The existence of a federal defense is not sufficient for removal jurisdiction. [Franchise Tax Bd. v. Construction Laborers Vacation Trust](#), 463 U.S. 1, 10-11, 77 L. Ed. 2d 420, 103 S. Ct. 2841 (1983).

[HN5](#) Federal courts are courts of limited jurisdiction. [HN6](#) While a defendant does have a right, [\*\*5] given by statute, to remove in certain situations, plaintiff is still the master of his own claim. [Caterpillar, Inc. v. Williams](#), 482 U.S. 386, 391, 96 L. Ed. 2d 318, 107 S. Ct. 2425 (1987). As master of his own claim, plaintiff "**may avoid federal jurisdiction by exclusive reliance on state law.**" [Id., at 392](#); (emphasis added).

[HN7](#) [\*43] When a party questions the propriety of a removal petition, the removing party bears the burden of showing that removal is proper. See [Danca v. Private Health Care Systems](#), 185 F.3d 1, 4 (1st Cir. 1999) (citing [BIW Deceived v. Local S6, Industrial Union of Marine and Shipbuilding Workers of America, IAMAW District Lodge 4](#), 132 F.3d 824, 831 (1st Cir. 1997)). [HN8](#) Removal statutes are strictly construed against removal. See [Rossello-Gonzalez](#), 398 F.3d at 11 (citing [Shamrock Oil & Gas Corp. v. Sheets](#), 313 U.S. 100, 108-09, 85 L. Ed. 1214, 61 S. Ct. 868 (1941)). [HN9](#) When plaintiff and defendant clash about jurisdiction, uncertainties are construed in favor of remand. [Burns v. Windsor Ins. Co.](#), 31 F.3d 1092, 1097 (11th Cir. 1994).

### B. The Propriety of Removal in this Case

Defendants argue that this [\*\*6] Court has original federal question jurisdiction--and hence removal is appropriate--because "but for [ADG's] artful pleading, the removed action would clearly raise substantial questions of federal jurisdiction." Relying on the [Franchise Tax Board](#) analysis,<sup>3</sup> defendants argue that plaintiff may not defeat removal by omitting necessary federal questions in its state court complaint.

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<sup>3</sup> [Franchise Tax Board](#), 463 U.S. at 22 (1983).

However, defendants fail to establish which unavoidable particular questions of federal law the state claim does not address. Furthermore, defendants' allegations seem to suggest that they are entitled to have ADG plead the causes of action they (the defendants) prefer. These allegations do not persuade this Court.

ADG, as master of its claim, chose to rely exclusively on the Puerto Rico Gasoline Law, 23 L.P.R.A. § 1101 et seq., and the Puerto Rico **Antitrust Law**, 10 L.P.R.A. § 257 et seq. This Court is [\*\*7] convinced that no federal cause of action is necessary for the resolution of the state claims raised by ADG. Moreover, HN10[<sup>↑</sup>] the Supreme Court has clearly ruled that a plaintiff can prevent removal by choosing not to pursue federal claims that are potentially available, without incurring in the artful pleading exception recognized in Franchise Tax Board. See Caterpillar, Inc. v. Williams, 482 U.S. at 392. In fact, the Supreme Court has noted that the artful pleading doctrine only allows removal "where federal law completely preempts a plaintiff's state law claim." Rivet v. Regions Bank, 522 U.S. 470, 475-76, 139 L. Ed. 2d 912, 118 S. Ct. 921 (1998); see also Rossello-Gonzalez, 398 F.3d at 12 ("we are skeptical of the applicability of the artful pleading doctrine outside of complete federal preemption of a state cause of action").

HN11[<sup>↑</sup>] Neither the Puerto Rico Gasoline Law nor the **Antitrust Law** is preempted by federal law. See e.g. Puerto Rico Department of Consumer Affairs v. Isla Petroleum Corp., 485 U.S. 495, 501, 99 L. Ed. 2d 582, 108 S. Ct. 1350 (1988); Caribe BMW v. Bayerische Motoren Werke Aktiengesellschaft, 19 F.3d 745, 754 (1st Cir. 1994). Thus, to require ADG to invariably claim federal [\*\*8] causes of action when they are available would amount to this Court preempting an area of the law when Congress has chosen not to do so. Such a proposition offends basic principles of federalism and separation of powers.

Since the state cause of action is not one of which the district courts of the United States have original jurisdiction, removal is therefore improper under section 1441.

#### C. All Writs Act

Defendants alternatively ask this Court to remove ADG's complaint under the purview of the All Writs Act, 28 U.S.C. § 1651. [\*44] They allege that removal is warranted under that statute in order for this Court to protect the integrity of its Order in Civil No. 04-1441 (JAF). That is, defendants argue that this Court is empowered by the All Writs Act to issue any order necessary to protect its jurisdiction from any action that threatens to undermine the consent order in case 04-1441 (JAF). This argument also fails to convince this Court.

HN12[<sup>↑</sup>] While the All Writs Act does empower a federal court to issue all the writs necessary to protect its jurisdiction, the Supreme Court has held that the Act is not an independent source of federal subject-matter jurisdiction. [\*\*9] Syngenta Crop Prot., Inc. v. Henson, 537 U.S. 28, 31, 154 L. Ed. 2d 368, 123 S. Ct. 366 (2002). In Syngenta, the Court dealt with a case in which, like the one at hand, defendants based their All Writs Act claim on a prior federal court settlement which the state court action would arguably frustrate. Finding against removal, the Court held that by itself, HN13[<sup>↑</sup>] the All Writs Act does not give federal courts authority to remove a state court case in order to prevent frustration of orders the federal court had previously issued. Rather, removal would only be proper if the federal court independently has original subject-matter jurisdiction over the suit. Syngenta, 537 U.S. at 33-34.

Accordingly, HN14[<sup>↑</sup>] defendants must demonstrate that the state cause of action is removable under 28 U.S.C. § 1441 in order for the All Writs Act to control the removal. Inasmuch as plaintiff's state action is not removable under section 1441, the All Writs Act does not empower this Court to entertain this case on removal.

#### CONCLUSION

In light of the foregoing, the Court hereby **REMANDS** (Docket No. 14) the case to the Puerto Rico Court of First Instance. All pending motions are [\*\*10] **MOOT**.

IT IS SO ORDERED.

In San Juan, Puerto Rico, this 5th day of July, 2005.

380 F. Supp. 2d 40, \*44L2005 U.S. Dist. LEXIS 15930, \*\*10

**s/Jay A. Garcia-Gregory**

JAY A. GARCIA-GREGORY

United States District Judge

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## Am. Copper & Brass, Inc. v. Donald Boliden AB

United States District Court for the Western District of Tennessee, Western Division

July 6, 2005, Decided ; July 6, 2005, Filed

No. 04-2771-DV

### **Reporter**

2005 U.S. Dist. LEXIS 43642 \*; 2005 WL 1631034

AMERICAN COPPER & BRASS, INC. and THE BANKRUPT ESTATE OF SMITH AND WOFFORD PLUMBING AND INDUSTRIAL SUPPLY, INC., on behalf of themselves and all others similarly situated, Plaintiffs v. DONALD BOLIDEN AB, et al., Defendants

**Subsequent History:** Motion denied by [Am. Copper & Brass, Inc. v. Donald Boliden Ab, 2006 U.S. Dist. LEXIS 102874 \(W.D. Tenn., Mar. 27, 2006\)](#)

Modified by, Motion denied by, On reconsideration by [Am. Copper & Brass v. Boliden, 2006 U.S. Dist. LEXIS 102878 \(W.D. Tenn., Mar. 27, 2006\)](#)

Dismissed by, Sub nomine at [Am. Copper & Brass, Inc. v. Mueller Eur., Ltd., 452 F. Supp. 2d 821, 2006 U.S. Dist. LEXIS 68828 \(W.D. Tenn., Sept. 13, 2006\)](#)

Dismissed by, Motion granted by [Am. Copper & Brass, Inc. v. Boliden AB, 2006 U.S. Dist. LEXIS 102876 \(W.D. Tenn., Oct. 10, 2006\)](#)

## **Core Terms**

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copper, tubing, Sherman Act, conspiracy, purposes, interstate commerce, Plaintiffs', motion to dismiss, antitrust, diligence, principal place of business, concealment, averred, fraudulent concealment, statute of limitations, unreasonable restraint, alleged conspiracy, antitrust claim, business entity, press release, fix prices, anticompetitive, discovery

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For Yorkshire Copper Tube LTD, Europa Metalli Spa, Defendant: Colin J. Carnahan, BOULT CUMMINGS CONNERS & BERRY, Nashville, TN; Paul A. Alexis, BOULT CUMMINGS CONNERS & BERRY, Nashville, TN; Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN.

For Trefimetaux SA, Defendant: Colin J. Carnahan, BOULT CUMMINGS CONNERS & BERRY, Nashville, TN; Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN.

For Mueller Industries, Inc., Defendant: Alexandra H. Russello, WILLKIE FARR & GALLAGHER LLP, New York, NY; Kelly M. Hnatt, WILLKIE FARR & GALLAGHER LLP, New York, NY; Robert L. Crawford, WYATT TARRANT & COMBS, Memphis, TN; Sameer Nitanand Advani, WILLKIE FARR & GALLAGHER LLP, New York, NY; Scott S. Rose, WILLKIE FARR & GALLAGHER LLP, New York, NY; William [\*3] H. Rooney, WILLKIE FARR & GALLAGHER LLP, New York, NY; Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN.

For Mueller Europe LTD, WTC Holding Company, Inc., Defendant: Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN; Robert L. Crawford, WYATT TARRANT & COMBS, Memphis, TN.

For Outokumpu Oyj, Outokumpu Copper Products Oy, Defendant: Robert J Fluskey, HODGSON RUSS LLP, Buffalo, NY, US; Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN.

For Austria Buntmetall AG, Defendant: Susanne M Kandel, PAUL WEISS RIFKIND WHARTON & GARRISON LLP, New York, NY, US; James R. Newsom, III, HARRIS SHELTON HANOVER WALSH, PLLC., Memphis, TN; Jerome A. Broadhurst, Apperson, Crump & Maxwell, PLC, Memphis, TN.

For Buntmetall Amstetten G.M.B.H., Defendant: Aidan Synnott, PAUL WEISS RIFKIND WHARTON & GARRISON, New York, NY; Danielle M. Aguirre, PAUL WEISS RIFKIND WHARTON AND GARRISON, LLP, New York, NY; Moses Silverman, PAUL WEISS RIFKIND WHARTON & GARRISON, New York, NY; Susanne M Kandel, PAUL WEISS RIFKIND WHARTON & GARRISON LLP, New York, NY, US; James R. Newsom, III, HARRIS SHELTON HANOVER WALSH, PLLC., Memphis, TN; Jerome A. Broadhurst, [\*4] Apperson, Crump & Maxwell, PLC, Memphis, TN.

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**Judges:** BERNICE BOUIE DONALD, UNITED STATES DISTRICT JUDGE.

**Opinion by:** BERNICE BOUIE DONALD

**Opinion**

**ORDER GRANTING MOTION TO DISMISS OF WTC HOLDING COMPANY, INC., AND DENO HOLDING COMPANY, INC., AND DENYING MOTION TO DISMISS OF DEFENDANTS' MUELLER INDUSTRIES, INC., KME AMERICA INC., OUTOKUMPU COPPER (U.S.A.), INC., AND WIELAND METALS, INC. (DKT. # 71)**

This matter is before the Court upon the motion of Defendants, Mueller Industries, Inc. ("Mueller"); WTC Holding Company, Inc. ("WTC"); DENO Holding Company, Inc. ("DENO"); KME America Inc. ("KME"); Outokumpu Copper (U.S.A.), Inc. ("Outokumpu"); and Wieland Metals, Inc. ("Wieland"), (collectively "moving Defendants" or "Defendants") to dismiss in its entirety the class action complaint of American Copper & Brass, Inc. ("American Copper") and The Bankrupt Estate of Smith and Wofford Plumbing and Industrial Supply, Inc. ("Smith Estate"), (collectively "Plaintiffs"). The moving Defendants' motion was brought pursuant to [Fed.R.Civ. P. 12\(b\)\(6\)](#) [\*6] as to Plaintiffs' [section 1](#) Sherman Act claim, and pursuant to [Rules 12\(b\)\(6\)](#) and [9\(b\)](#) as to Plaintiffs' fraudulent concealment claim. For the following reasons, the Court **DENIES** the motion to dismiss as to moving Defendants Mueller, KME, Outokumpu, and Wieland, and **GRANTS** the motion to dismiss as to moving Defendants WTC and DENO.

**I. BACKGROUND****A. Procedural Background<sup>1</sup>**

On September 24, 2004, American Copper invoked this Court's jurisdiction pursuant to the provisions of sections 4 and 16 of the Clayton Act, [15 U.S.C. §§ 15](#) and [26](#), to recover treble damages for, and obtain injunctive relief from, Defendants' alleged violations of section 1 of the Sherman Act, [15 U.S.C. § 1](#), and the cost of this suit, including [\*7] reasonable attorneys fees. On March 9, 2005, Plaintiffs<sup>2</sup> filed a Consolidated Amended Class Action Complaint<sup>3</sup> (hereinafter, "complaint") with this Court. On May 6, 2005, the moving Defendants sought dismissal of Plaintiffs' complaint in its entirety.

**B. Factual Background**

American Copper is a Michigan corporation. Compl. P 8. The Smith Estate is an entity in the State of Tennessee. Id. at P 9. The moving Defendants hail from various jurisdictions across the United States ("U.S."). Mueller, the leading producer of copper tubing in the world, is a corporation with its principal place of business in Memphis, Tennessee. WTC is a corporation with its principal place of business in Michigan. DENO is a corporation with its principal place of business in Michigan. KME is a Delaware corporation [\*8] with its principal place of business in Illinois. Outokumpu is a corporation with its principal place of business in Illinois. Wieland is a corporation with its principal place of business in Illinois.

There are twenty-three (23) defendants in this case. Of the six moving Defendants, Mueller, KME, Outokumpu and Wieland have affiliations, either as a subsidiary or a parent entity, to at least one of the non-moving EU-based Defendants: Mueller (Mueller Europe Ltd., United Kingdom), KME (KM Europa Metal AG, Germany), Outokumpu (Outokumpu OYJ and Outokumpu Copper Products of OY, Finland), and Wieland (Wieland Werke AG, Germany).

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<sup>1</sup> The Court received a letter from Plaintiffs' counsel dated June 30, 2005. The Court did not consider this letter in deciding this motion because the communication did not constitute a proper pleading.

<sup>2</sup> The Smith Estate was Plaintiff in Civil Action No. 04-2930-DV prior to consolidation.

<sup>3</sup> Individually and on behalf of a class pursuant to [Fed.R.Civ. P. 23\(a\),\(b\)\(2\)-\(3\)](#).

Plaintiffs allege that between June 1, 1988, and March 31, 2001, ("Class Period"), the moving Defendants, directly or through their subsidiaries and/or affiliates, produced Copper Plumbing Tubes (hereinafter, "copper tubing") and sold them throughout the United States. Compl. PP 22, 24, 25, 28, 30, and 43. Copper tubing includes both plain copper plumbing tubes and plastic-coated copper tubal fixtures used in dwelling structures to transfer water, heat, and gas. *Id.* at P 5. Copper tubing is used in residential and office buildings and throughout the transportation [\*9] industry. *Id.* at PP 47-48.

Plaintiffs rely to a great extent on a September 3, 2004 European Commission ("EC") press release for its facts. This press release detailed the EC's imposition of fines against named European copper tubing manufacturers, some of whom are moving Defendants. *Id.* at P 53. EC fines were levied against Boliden Group (Sweden), Halcor S.A. (Greece), HME Nederland BV (The Netherlands), the IMI Group (United Kingdom), the KME Group (Germany, Italy, and France), Mueller Industries, Inc. (U.S., United Kingdom, and France), Outokumpu Industries, Inc., (Finland), and Wieland Werke AG (Germany). The EC investigation led to uncovering the operation of a European cartel to fix prices of copper tubing between June, 1988, and March, 2001 "throughout most of the European Economic Area . . . in violation of EU Treaty 81 and EEA Agreement Article 53." *Id.*

Plaintiffs aver that on September 29, 1989, European manufacturers, some of whom are also named Defendants, met in Zurich, Switzerland (dubbed the "Airport Forum") and made statements expressing an intent to keep the price of copper tubing high in "high price level countries." *Id.* at P 56. Plaintiffs assert [\*10] that a cartel grew into "a 'group of five' [of the] largest European producers of copper plumbing tubes" with the intent to fix prices in the global copper tubing market. *Id.* at P 57.

## II. LEGAL STANDARD

A 12(b)(6) motion tests whether a plaintiff has plead a cognizable claim. *Scheid v. Fanny Farmer Candy Shops, Inc.*, 859 F.2d 434, 436 (6th Cir. 1988). Essentially, it allows the court to dismiss meritless cases and claims which would otherwise waste judicial resources and result in unnecessary discovery. See, e.g., *Neitzke v. Williams*, 490 U.S. 319, 326-27, 109 S. Ct. 1827, 104 L. Ed. 2d 338 (1989). A court, however, is to presume that well plead allegations are true, resolve all doubts and inferences in favor of the pleader, and view the pleading in the light most favorable to the non-moving party. *Re/Max Int'l, Inc. v. Smythe, Cramer, Co.*, 265 F.Supp. 2d 882, 886 (6th Cir. 2003).

"A complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." *Conley v. Gibson*, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 (1957); see also [\*11] *Neitzke*, 490 U.S. at 326-27; *Lewis v. ACB Bus. Servs.*, 135 F.3d 389, 405 (6th Cir. 1997). The standard to be applied when evaluating a motion to dismiss for failure to state a claim is very liberal in favor of the party opposing the motion. *Westlake v. Lucas*, 537 F.2d 857, 858 (6th Cir. 1976). Even if the plaintiff's chances of success are remote or unlikely, a motion to dismiss should be denied.

Before deciding to grant a motion to dismiss, the court must first examine the complaint. The complaint must contain "a short and plain statement of the claim showing that the pleader is entitled to relief." *Fed.R.Civ. P. 8(a)*. The complaint must provide the defendant with "fair notice of what the plaintiff's claim is and the grounds upon which it rests." *Conley*, 355 U.S. at 47; *Westlake*, 537 F.2d at 858. The plaintiff must allege the essential material facts of the case. *Scheid*, 859 F.2d at 436-37. Where there are conflicting interpretations of the facts, they must be construed in the plaintiff's favor. *Sinay v. Lamson & Sessions Co.*, 948 F.2d 1037, 1039-40 (6th Cir. 1991). [\*12] However, in considering a 12(b)(6) motion, the court must not accept plaintiff's legal conclusions or unwarranted factual inferences as true. *Lewis*, 135 F.3d at 405-06.

## III. ANALYSIS

To state a [§ 1](#) Sherman Act claim in a private antitrust action, a plaintiff must aver three essential elements: (1) the existence of a conspiracy (2) affecting interstate commerce (3) that imposes an unreasonable restraint on trade. [Richter Concrete Corp. v. Hilltop Concrete Corp.](#), 691 F.2d 818, 827 (6th Cir. 1982); [Davis-Watkins Co. v. Service Merchandise](#), 686 F.2d 1190, 1195-96 (6th Cir. 1982).

The basic objective of the Sherman Act is to prevent or suppress devices or practices that create monopolies or restrain trade or commerce in the United States. See [United States v. American Linseed Oil Co.](#), 262 U.S. 371, 388, 43 S. Ct. 607, 67 L. Ed. 1035 (1923); [Sugar Institute, Inc. v. United States](#), 297 U.S. 553, 597, 56 S. Ct. 629, 80 L. Ed. 859 (1936). "The Sherman Act was conceived as a weapon against monopolies, trusts, and conspiracies that use[] agreement instead of financial consolidation to achieve the same results." [Northwest Power Products, Inc. v. Omkar Industries, Inc.](#), 576 F.2d 83, 89 (5th Cir. 1978), [\*13] rehearing denied, 579 F.2d 643, cert. denied, 439 U.S. 1116, 99 S. Ct. 1021, 59 L. Ed. 2d 75 (1979). Although the Sherman Act, by its terms, prohibits every agreement "in restraint of trade," Congress' intent was to outlaw only unreasonable restraints. See [15 U.S.C. § 1](#): see, e.g., [State Oil Co. v. Khan](#), 522 U.S. 3, 10, 118 S. Ct. 275, 139 L. Ed. 2d 199 (1997).

Two major threads of antitrust judicial analysis are employed to determine whether there has been a violation of the Sherman Act: (1) *per se* unreasonable restraint on trade, derived from judicial experience with certain forms of egregious, anti-competitive restraints, and (2) "rule of reason," which entails a closer scrutiny of a plaintiff's allegations against the antitrust statute and its case law. Congress "expected the courts to give shape to the statute's broad mandate by drawing on common-law tradition." [Nat'l Soc'y of Prof. Engineers v. United States](#), 435 U.S. 679, 688, 98 S. Ct. 1355, 55 L. Ed. 2d 637 (1978).

Judicial antitrust common law has established price-fixing as one of the *per se* unreasonable restraints on trade. See [United States v. Nat'l Ass'n of Real Estate Boards](#), 339 U.S. 485, 489, 70 S. Ct. 711, 94 L. Ed. 1007 (1950) [\*14] ("An agreement, shown either by adherence to a price schedule or by proof of consensual action fixing the uniform or minimum price, is itself illegal under the Sherman Act, no matter what end it was designed to serve. That is the teaching of an unbroken line of decisions"). Where a *per se* unreasonable restraint on trade is not shown, a court's analysis must be based on an application of the rule of reason. This involves the initial showing of a relevant product and geographic market, as well as an injury to competition.

For purposes of a [12\(b\)\(6\)](#) motion, it is not a court's function to rule on the weight of the evidence or the issue of credibility, [Anderson v. Liberty Lobby](#), 477 U.S. 242, 249, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986); however, failure of a plaintiff to aver either of the essential statutory elements justifies dismissal of an antitrust claim. Furthermore, while the pleading standard under the federal rules is very liberal, see [Fed.R.Civ. P. 8](#), the essential elements of a private antitrust claim must be alleged in more than vague and conclusory terms to prevent a [12\(b\)\(6\)](#) dismissal. See [Crane & Shovel Sales Corp. v. Bucyrus-Erie Co.](#), 854 F.2d 802, 805 (6th Cir. 1988).

## [\*15] 1. Conspiracy

A claim under [Section 1](#) of the Sherman Act requires that a plaintiff "establish that the defendants combined or conspired with an intent to unreasonably restrain trade." [Smith v. Northern Mich. Hosps.](#), 703 F.2d 942, 949 (6th Cir. 1983). The moving Defendants argue that Plaintiffs' allegations of an illegal agreement are vague and conclusory and do not sufficiently allege a conspiracy under [Section 1](#) of the Sherman Act. The moving Defendants cite this Court's opinion in [Cupp v. Alberto-Culver USA, Inc.](#), 310 F. Supp. 2d 963 (W.D. Tenn. 2004), for the proposition that vague and conclusory statements of collusive activity are insufficient to survive a [Rule 12\(b\)\(6\)](#) motion. [Cupp v. Alberto-Culver USA, Inc.](#), 310 F. Supp. 2d at 972 (citing [Crane & Shovel Sales Corp. v. Bucyrus-Erie Co.](#), 854 F.2d at 805). The moving Defendants' reliance on [Cupp](#) for this proposition is appropriate. The moving Defendants assert that the alleged conspiracy must detail the time, place, and alleged effect of the conspiracy. [Estate Constr. Co. v. Miller & Smith Holding Co.](#), 14 F.3d 213, 221-22 (4th Cir. 1994) [\*16] (the Fourth Circuit dismissed an antitrust claim that "merely reiterated mechanically the words of the Sherman Act"). Indeed, while the pleading standard under the federal rules is very liberal, see [Fed.R.Civ. P. 8](#), "the price of entry, even to

discovery, is for the plaintiff to allege a factual predicate concrete enough to warrant further proceedings, which may be costly and burdensome." [DM Research, Inc. v. College of Am. Pathologists, 170 F.3d 53, 55 \(1st Cir. 1999\)](#).

Estate Constr. Co. can be distinguished from the case at bar. Plaintiffs in Estate Constr. Co. merely reiterated statutory language without including any factual allegations. Plaintiffs at bar, though relying exclusively on the information and belief of facts from the EC investigation for the existence of dates, meetings, and statements, have asserted facts that point to the concerted conspiratorial acts of some of the Defendants. For purposes of this motion, all of these facts are assumed true. The moving Defendants further assert that no factual link is alleged to connect U.S. copper tubing manufacturers with the conspiratorial acts that occurred [\*17] in Europe. This is true as to the moving Defendants WTC and DENO, but not as to the remaining four moving Defendants. WTC and DENO are business entities organized solely under U.S. laws and Plaintiffs have averred no link between these entities and the activities that occurred within the EU. On the other hand, Mueller, KME, Outokumpu, and Wieland all have affiliated business entities in Europe who were identified parties to the alleged conspiracy and subject to EC anticompetitive sanctions. It is not inconceivable that knowledge of and participation in the conspiratorial acts existed among the U.S. and EU affiliated business entities and that such acts extended to the U.S. market. Though the holding of a foreign tribunal alone does not establish that antitrust activities have occurred under U.S. antitrust laws, the acts alleged are sufficient to state the conspiracy element for purposes of Section 1 of the Sherman Act against Mueller, KME, Outokumpu, and Wieland. As to Mueller, both its U.S. and EU business entities were specifically named in the EC press release that reported the copper tubing cartel. Accordingly, the Court finds that, as to Mueller, KME, Outokumpu, and Wieland, a [\*18] conspiracy has been alleged for purposes of a violation of the Sherman Act. Accordingly, the motion to dismiss as to these Defendants is not well founded as to this element.

## 2. Interstate Commerce

The second element of a § 1 Sherman Act claim is the interstate commerce requirement, which is often referred to as jurisdictional. The Supreme Court has held that there is no practical distinction between the "jurisdictional" interstate commerce inquiry and whether a complaint pleads an effect on interstate commerce sufficient to state a claim for relief under the Sherman Act. [Hosp. Bide. Co. v. Trs. of Rex Hosp., 425 U.S. 738, 742, 96 S. Ct. 1848, 48 L. Ed. 2d 338 & n. 1 \(1976\)](#) ("an analysis of challenges to antitrust claims based on the interstate commerce element under either Federal Rule of Civil Procedure 12(b)(1) or 12(b)(6) leads to the same result."). Further, the Supreme Court has held that the Sherman Act's reach is as broad as Congress' power under the Commerce Clause. [McLain v. Real Estate Bd. of New Orleans, 444 U.S. 232, 241-42, 100 S. Ct. 502, 62 L. Ed. 2d 441 \(1980\)](#).

To establish that interstate commerce has been [\*19] impacted, a plaintiff must demonstrate either (1) that the proscribed activities are actually "in" or part of interstate commerce, [Mandeville Island Farms v. American Crystal Sugar Co., 334 U.S. 219, 68 S. Ct. 996, 92 L. Ed. 1328 \(1948\)](#), or (2) that the defendant's business activities in general substantially affect interstate commerce. [McLain, 444 U.S. at 239](#).

Plaintiffs assert that the conspiracy to fix prices in the copper tubing industry was carried out with the intent to reach global markets. Additionally, Plaintiffs contend that the price of copper tubing in the U.S. during the Class Period, due to the conspiracy, resulted in the members of the Class paying substantially more for copper tubing than they would have paid in the absence of Defendants' conspiracy. Mueller alone is the leading global manufacturer of copper tubing. KME, Outokumpu, and Wieland also transact business globally and throughout the U.S. . The Court finds that for purposes of the 12(b)(6) motion to dismiss, Plaintiffs have satisfied the second element of their antitrust claim.

## 3. Restraint on Trade

*Per se* violations involve "agreements whose nature and necessary effect are so plainly anticompetitive [\*20] that no elaborate study of the industry is needed to establish their illegality." [National Soc. of Professional Engineers v. United States, 435 U.S. 679, 692, 98 S. Ct. 1355, 55 L. Ed. 2d 637 \(1978\)](#). The strict *per se* rules of modern

**antitrust law** establish a conclusive presumption that a particular kind of action has improper anticompetitive effects, and this presumption governs regardless of whether the particular conduct in its actual context has been proved to have those consequences. [State Oil Co., 522 U.S. at 10 \(1997\)](#), overruling [Albrecht v. Herald Co., 390 U.S. 145, 88 S. Ct. 869, 19 L. Ed. 2d 998 \(1968\)](#).

Here, Plaintiffs contends that EU-based business entities conspired to fix copper tubing prices, not just within the EU, but also in the U.S. This, Plaintiffs assert, constitutes a *per se* violation against the moving Defendants. The Court agrees. Price fixing is *per se* anticompetitive and does not require a rule of reason analysis to determine whether restraint on trade has been adequately averred by a showing of the relevant product and geographic markets or injury to competition. For purposes of this motion, Mueller, KME, Outokumpu, and Wieland's alleged participation in a horizontal [\*21] restraint on trade by conspiring to fix prices in the copper tubing industry constitutes a *per se* restraint on trade for purposes of a [12\(b\)\(6\)](#) motion to dismiss. Because there is nothing to link WTC and DENO to the concerted acts that occurred in Europe, a claim of *per se* restraint has not been sufficiently averred against them. Accordingly, the Court finds that Plaintiffs have adequately alleged facts of a *per se* restraint on trade against Mueller, KME, Outokumpu, and Wieland for purposes of surviving a motion to dismiss.

#### 4. Statute of Limitations

The moving Defendants argue that Plaintiffs' complaint for damages for acts that occurred more than four years from the time the Sherman Act claim accrued is defeated by the statute of limitations. The Sherman Act's limitation of action establishes that:

[a]ny action to enforce any cause of action under [Section 15, 15a](#), or [15c](#) of this title shall be forever barred unless commenced within four years after the cause of action accrued. No cause of action barred under existing law on the effective date of this Act shall be revived by this Act.

#### [15 U.S.C. § 15b.](#)

A Sherman Act claim [\*22] accrues when the defendant commits an act that injures the plaintiffs' business. [Zenith Radio Corp. v. Hazeltine Research, Inc., 401 U.S. 321, 338, 91 S. Ct. 795, 28 L. Ed. 2d 77 \(1971\)](#)("each time a plaintiff is injured by an act of the defendant a cause of action accrues to him to recover the damages caused by that act and, as to those damages, the statute of limitations runs from the commission of the act"). Plaintiffs allege that the moving Defendants' violation of the Sherman Act began "at least as early as June 1, 1988, and continu[ed] until no earlier than March 31, 2001." Compl. P 61. Defendants assert that, to the extent Plaintiffs seek to recover damages for injuries that occurred more than four years preceding the commencement of this action (i.e., September 24, 2000), Plaintiffs' claim is time-barred and should be dismissed. Plaintiffs argue that the statute of limitations is tolled by Defendants' acts of fraudulent concealment. To establish fraudulent concealment, a plaintiff must allege:

(1) wrongful concealment of their actions by the defendants; (2) failure of the plaintiff to discover the operative facts that are the basis of his cause of action within the limitations period; [\*23] and (3) plaintiff's due diligence until discovery of the facts.

#### [Dayco Corp. v. Goodyear Tire & Rubber Co., 523 F.2d 389, 394 \(6th Cir. 1975\).](#)

Additionally, [Fed.R.Civ. P. 9\(b\)](#) requires that a party alleging fraudulent concealment "plead the circumstances giving rise to it with particularity." [Dayco Corp., 523 F.2d at 394](#); see also, [Campbell v. Upjohn Co., 676 F.2d 1122, 1126 \(6th Cir. 1982\)](#). Plaintiffs in the case at bar allege that the conspiracy "was inherently self-concealing." Compl. P 71. See [Dry Cleaning & Laundry Inst. of Detroit, Inc. v. Flom's Corp., 841 F. Supp. 212, 217 \(E.D. Mich. 1993\)](#)(citing [Pinney Dock](#) and rejecting the contention that because the price-fixing conspiracy was inherently "self-concealing," plaintiffs do not need to prove affirmative acts of concealment") (emphasis added).

In Dayco Corp., the Sixth Circuit held that affirmative acts of concealment by the defendant beyond the original fraud do not relieve the plaintiff of the requirement of due diligence. Dayco Corp., 523 F.2d at 394. The Supreme Court in Wood v. Carpenter, 101 U.S. (11 Otto) 135, 25 L. Ed. 807 (1879), [\*24] stated that "concealment by mere silence is not enough." Wood, 101 U.S. (11 Otto) at 143, 25 L. Ed. 807 (the circumstances of the discovery must be fully stated and proved, and the delay which has occurred must be shown to be consistent with the requisite diligence). Id.

For purposes of this motion, the Court finds that Plaintiffs have averred affirmative acts and shown diligence. Plaintiffs have averred that the means by which they discovered the alleged conspiracy was the EC press release of September 3, 2004, which sets forth the concerted conspiratorial acts. On September 24, 2004, Plaintiffs filed their original complaint in this matter. Plaintiffs argues that at this stage, it is not appropriate to determine whether their diligence was sufficient. The Court agrees. Whether their diligence was reasonably sufficient will be measured at the evidentiary stage.

Furthermore, in spite of the fact that the only known concerted acts of conspiracy occurred in Europe, the Court finds that Plaintiffs' averment sufficiently meets the particularity requirement of Fed.R.Civ. P. 9(b) for fraudulent concealment when it avers that the first European-wide [\*25] meeting was held on September 29, 1989 at the "Airport Forum" in Zurich, Switzerland. According to the complaint, at this meeting Defendants agreed to meet again less than a month later in the negotiation room of the Amsterdam airport to continue their plan to fix prices. Accordingly, Plaintiffs should be allowed to proceed as to all claims against Mueller, KME, Outokumpu, and Wieland since, for purposes of a 12(b)(6) motion, Plaintiffs have alleged wrongful concealment and Plaintiffs could not have discovered the concealment. Furthermore, Plaintiffs' discovery of the EC press release goes to their diligence in discovering the alleged conspiracy. For the reasons stated above, Defendants' motion to dismiss based on the statute of limitations is **DENIED**.

#### IV. CONCLUSION

Accordingly, the Court **DENIES** the motion to dismiss as to moving Defendants Mueller, KME, Outokumpu, and Wieland, and **GRANTS** the motion to dismiss against moving Defendants WTC and DENO.

**IT IS SO ORDERED** on this 6th day of July, 2005.

**BERNICE BOUIE DONALD**

**UNITED STATES DISTRICT JUDGE**

## *In re Enron Corp.*

United States Bankruptcy Court for the Southern District of New York

July 6, 2005, Decided

Chapter 11, Case No. 01 B 16034 (AJG)

**Reporter**

2005 Bankr. LEXIS 3470 \*; 2005 WL 3873899

In re: ENRON CORP., et al., Reorganized Debtors.

**Notice:** NOT FOR PUBLICATION

### **Core Terms**

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filed rate doctrine, electricity, rates, wholesale, state law claim, tariff, preemption, energy, sales, anti trust law, state law, market-based, preempted, markets, manipulation, regulation, interstate, anti-competitive, refunds, transactions, violations, cases, state **antitrust law**, Sherman Act, antitrust, argues, courts, exclusive jurisdiction, field preemption, energy crisis

### **LexisNexis® Headnotes**

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Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

#### **HN1** [] **Regulated Practices, Price Fixing & Restraints of Trade**

The Cartwright Act, [Cal. Bus. & Prof. Code § 16720\(b\)](#), prohibits agreements to limit or reduce the production, or increase the price of merchandise or of any commodity.

Banking Law > Federal Acts > Federal Trade Commission Act > Unfair Competition & Practices

#### **HN2** [] **Federal Trade Commission Act, Unfair Competition & Practices**

The Unfair Competition Law, [Cal. Bus. & Prof. Code § 17200](#), prohibits unlawful, unfair, or fraudulent business acts and practices.

Constitutional Law > Supremacy Clause > Federal Preemption

#### **HN3** [] **Supremacy Clause, Federal Preemption**

Federal preemption of state law is rooted in the [Supremacy Clause, U.S. Const. art. VI, cl. 2.](#) Where Congress manifests an intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted.

Constitutional Law > Supremacy Clause > General Overview

#### [\*\*HN4\*\*](#) Constitutional Law, Supremacy Clause

In the absence of an express preemption by Congress, state law is preempted (1) when Congress intends that federal law occupy a given field, (field preemption), and (2) to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

#### [\*\*HN5\*\*](#) Electric Power Industry, Federal Power Act

Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states. The Federal Power Act, 16 U.S.C.S. § 824-824m.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### [\*\*HN6\*\*](#) Federal Power Act, Federal Rate Regulation

See [16 U.S.C.S. § 824e.](#)

Energy & Utilities Law > Electric Power Industry > Federal Power Act > Judicial Review

#### [\*\*HN7\*\*](#) Federal Power Act, Judicial Review

The Federal Energy Regulatory Commission (FERC) possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rule making rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. [16 U.S.C.S. §§ 824d, 824e; 42 U.S.C.S. § 7173\(c\).](#)

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### [\*\*HN8\*\*](#) Federal Power Act, Federal Rate Regulation

Anomalous market behavior is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include (a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; (b) unexplained or unusual redeclarations of availability; (c) unusual

trades or transactions; (d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### [HN9](#) [down] **Electric Power Rates, Filed Rate Doctrine**

The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### [HN10](#) [down] **Electric Power Rates, Filed Rate Doctrine**

While market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

#### [HN11](#) [down] **Complaints, Requirements for Complaint**

Injury implies violation of a legal right.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### [HN12](#) [down] **Electric Power Rates, Filed Rate Doctrine**

Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### [HN13](#) [down] **Electric Power Rates, Filed Rate Doctrine**

The filed rate doctrine may bar a court from awarding monetary damages in a Federal Energy Regulatory Commission rate case.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

**HN14[] Electric Power Rates, Filed Rate Doctrine**

Injunctive relief may be barred by the filed rate doctrine and preemption principle where remedies for breach and non-performance of Federal Energy Regulatory Commission (FERC)-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC.

**Counsel:** [\*1] For Reorganized Debtors, Special Counsel: Edward A. Smith, Esq., Of Counsel, CADWALADER, WICKERSHAM & TAFT LLP, New York, NY; Mark C. Ellenberg, Esq., David F. Williams, Esq., Of Counsel, Washington, DC.

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**Judges:** Arthur J. Gonzalez, UNITED STATES BANKRUPTCY JUDGE.

**Opinion by:** Arthur J. Gonzalez

## **Opinion**

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OPINION SUSTAINING DEBTORS' OBJECTION TO PROOFS OF CLAIM NOS. 22630 THROUGH 22632 REGARDING STATE LAW CLAIMS IN ELECTRICITY MARKET FILED BY SOUTHERN CALIFORNIA EDISON COMPANY ARTHUR J. GONZALEZ United States Bankruptcy Judge

ARTHUR J. GONZALEZ

United States Bankruptcy Judge

Southern California Edison Company ("Edison") filed proofs of claim regarding manipulation in the electricity market in the State of the California in unliquidated amounts against Enron Corporation and certain of its affiliated entities, (collectively, the "Debtors") in the following cases: Enron Corp. (Claim No. 22630); Enron Energy Services, Inc. (Claim No. 22631); and Enron Power Marketing, Inc. (Claim No. 22632) (collectively, the "Claims"). The Claims allege that [\*2] the Debtors violated state antitrust and competition laws as a result of their improper and illegal manipulation in the California power market.

The issue before the Court is whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine. The Court finds that because the Federal Energy Regulatory Commission ("FERC") has exclusive jurisdiction over interstate sales of wholesale electricity, the state law claims sought to be enforced by Edison in the prosecution of the Claims are preempted by the FPA. Further, the filed rate doctrine precludes consideration of such Claims.

### **I. FACTUAL AND PROCEDURAL HISTORY**

#### **A. The Debtors**

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the "Plan") in these cases. The Plan became effective on November 17, 2004.

#### **B. The Claims**

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, [\*3] the California legislature had passed Assembly Bill 1890<sup>1</sup> (the "Bill") to create two nongovernmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. [California v. Dynegy, Inc., 375 F.3d 831, 850 \(9th Cir. 2004\)](#). The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. Edison is an investor-owned utility that purchases, transmits, generates, distributes, and sells electricity in California. Under the Bill, Edison was required to procure all electric power necessary to meet its total peak demand in excess of its generation capacity through the PX and ISO.

Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC [\*4] found that the Debtors engaged in gaming<sup>2</sup> in the form of inappropriate trading strategies and further engaged in the deliberate submission of false information or the deliberate omission of material information. [Enron Power Mktg., Inc., et al., 106 FERC ¶ 61,024 \(2004\)](#). Both proceedings are ongoing, including the determination of remedies by FERC.

On March 6, 2003, Edison filed the Claims against the Debtors. Edison alleges that the Debtors manipulated energy markets in California and overcharged for energy through unlawful and anti-competitive acts during the western power crisis of 2000 and 2001. Edison maintains the alleged manipulation in the electricity market constitutes a violation of state **antitrust law**, specifically, the Cartwright Act,<sup>3</sup> and the Unfair Competition Law<sup>4</sup> and seeks disgorgement, restitution, [\*5] actual and treble damages together with interest and injunctive relief.

On March 9, 2005 and May 16, 2005, the Debtors filed separate objections to Edison's state law claims, seeking to disallow the Claims on the ground that the FPA preempts state law and the filed rate doctrine precludes consideration of these Claims, and that Edison's state law claims are duplicative of the claims filed by the California Attorney General.

On May 2, 2005, Edison filed its response to the Debtors' objection. Citing case law, Edison contends the FPA does not preclude operation of other state laws, or judicial adjudication of certain issues relating to wholesale energy markets regulated by FERC. Edison maintains that the Court may decide whether the Debtors' various fraudulent gaming and market manipulation activities violated state laws without having to determine a nonmanipulated rate. In addition, Edison [\*6] argues that the filed rate doctrine should not apply unless rates are properly filed; therefore, because the filed rates are not at issue before this Court, the filed rate doctrine should not preclude the state law claims.

A hearing on this matter was held before the Court on May 18, 2005 (the "Hearing").

## II. DISCUSSION

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<sup>1</sup> 1996 Cal. Stat. 854

<sup>2</sup> The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule ... to the detriment of the efficiency of, and of consumers in, the ISO markets." *Am. Electric Power Service Corp., et al., 103 FERC at ¶ 62,330 (2003)*.

<sup>3</sup> [HN1](#) The Cartwright Acts prohibits agreements "to limit or reduce the production, or increase the price of merchandise or of any commodity." [Cal. Bus. & Prof. Code § 16720\(b\)](#).

<sup>4</sup> [HN2](#) The Unfair Competition Law prohibits unlawful, unfair, or fraudulent business acts and practices. [Cal. Bus. & Prof. Code § 17200](#).

## A. Legal Standard of Preemption

[HN3](#) [↑] "Federal preemption of state law is rooted in the [\*Supremacy Clause, Article VI, clause 2, of the United States Constitution.\*](#)" *Transmission Agency of Cal. v. Sierra Pacific Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests an intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted ("Complete Preemption"). [\*Metro. Life Ins. Co. v. Taylor, 481 U.S. 58, 63-64, 107 S. Ct. 1542, 95 L. Ed. 2d 55 \(1987\)\*](#). Federal courts have rarely identified legislation which has been found to completely preempt state jurisdiction. [\*Caterpillar, Inc. v. Williams, 482 U.S. 386, 393, 107 S. Ct. 2425, 96 L. Ed. 2d 318 \(1987\)\*](#). Here, the Court agrees with Edison that there is no evidence in the record that would support the conclusion that Congress intended for complete preemption to apply in this case. The Court does not need to identify a "clear and [<sup>7</sup>] manifest" congressional intent to preempt state laws in an entire field under the FPA because the Debtors do not argue that complete preemption is applicable here. [HN4](#) [↑] In the absence of an express preemption by Congress, state law is preempted (1) "when Congress intends that federal law occupy a given field," [\*Silkwood v. Kerr-McGee Corp., 464 U.S. 238, 248, 104 S. Ct. 615, 78 L. Ed. 2d 443 \(1984\)\*](#) ("Field Preemption"), and (2) "to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* ("Conflict Preemption").

## B. Preemption

### 1) Field Preemption

The Debtors, in support of their position that the state law claims should be barred by FERC's exclusive jurisdiction, cite to [\*Grays Harbor v. Idacorp Inc., 379 F.3d 641 \(9th Cir. 2004\)\*](#), [\*Dynegy, and Snohomish County v. Dynegy Power Marketing Inc., 384 F.3d 756 \(9th Cir. 2004\)\*](#). These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The Debtors argue that Edison's claims alleging violations of state antitrust and unfair competition [<sup>8</sup>] law are nearly identical to those involved in the cited cases, and field preemption is applicable here for the same reasoning set forth in those cases.

The *Dynegy* court ruled that "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." [375 F.3d at 852](#).

The Court finds that the statute's framework under the FPA supports the conclusion in *Dynegy* that FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The Court disagrees with Edison that FPA's savings clause allows the application of state law claims in the instant case because the statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states . . . . [<sup>9</sup>] [HN5](#) [↑] Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states." Federal Power Act, [16 U.S.C. § 824-824m](#). Edison does not dispute that the transactions at issue involved wholesale interstate sales. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute should be characterized as either retail sales of electricity or wholesale intrastate sales.

The FPA further provides that upon a determination by FERC that [HN6](#) [↑] "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract* affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the Commission shall determine the just

and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order." Federal Power Act, [16 U.S.C. § 824e](#) (emphasis added).

Moreover, pursuant to the FPA, [HN7](#) FERC possesses broad remedial authority to address [\*10] anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, §§ 205, [206\(a\)](#), as amended, [16 U.S.C.A. §§ 824d, 824e](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.A. § 7173\(c\)](#).

In addition, after the deregulation of California energy markets, the central transactions, the wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded that "FERC is doing enough regulation to justify federal preemption of state laws under the market-based system of setting wholesale electricity rates." [Snohomish, 384 F.3d at 760-61](#). For instance,

(1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and [\*11] the ISO. FERC approved the market-based tariffs only upon a showing that the seller lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under FPA §205(c) [16 U.S.C. §824d\(c\)](#). (3) FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, "[e]ach participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market." *Id.*

The Court also notes that a mechanism for FERC to enforce anti-competitive acts is in place. "[E]ntities that transact through the ISO or [the] PX and engage in improper practices<sup>5</sup> are in violation of filed tariffs . . . . FERC and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement." [103 FERC at ¶ 62,334](#). Edison was required to procure all electric power necessary to meet its total peak demand in excess of its generation capacity through the PX and ISO during the western energy crisis. Thus, FERC has an enforcement [\*12] power over the alleged transactions and practices by the Debtors occurring in the ISO and PX markets.

Edison argues that field preemption is not applicable because courts have referred the state law claims related to filed rates before regulatory commissions. In supporting its assertion, Edison cites [\*13] the Supreme Court's decision in [Otter Tail Power Co. v. United States, 410 U.S. 366, 93 S. Ct. 1022, 35 L. Ed. 2d 359 \(1973\)](#). The Supreme Court found that Congress does not intend to bar governments from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions.

Having reviewed the case, the Court disagrees with Edison's argument and finds that two important differences exist. First, a critical distinction between the instant matter and the cited case is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC. In contrast, the Court in *Otter Tails Power* found that the limited authority of the Federal Power Commission (the "FPC") to order interconnections was not intended to be a substitute for the Sherman Act. [410 U.S. at 375](#). In *Otter Tails Power*, the FPA does not authorize

<sup>5</sup> Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. [HN8](#) "Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges." *Am. Elec. Power Serv. Corp., et al., 103 FERC at ¶ 62,332 (2003)*.

the FPC to order a power company to wheel electric power over its transmission lines; accordingly, enforcing the Sherman Act against anticompetitive and monopolistic practices on interconnections by the district court did not conflict with authority of the FPC. *Id. at 376-77*. However, here as the Court discussed above, the statute under 16 U.S.C.A. §§ 824d, 824e(a) [\*14] provides FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." 103 FERC at ¶62,331. Further, "implicit in Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority." 106 FERC ¶61,024.

Second, *Otter Tail Power* discussed issues of the interaction between federal administrative law and federal antitrust law; no state law preemption issue was presented in that case. In *Otter Tail Power*, the government brought [\*15] an action against an electric power company to enjoin violations of the Sherman Act, 15 U.S.C.A. §2. 410 U.S. at 368. In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws.

Edison argues that state and federal antitrust law would be impacted the same way. Edison cites a Seventh Circuit case, which asserts that "when state antitrust law only mirrors federal antitrust law, there is no reason to conclude that Congress intended to preempt the state law." State of Ill., ex rel. Burris v. Panhandle Eastern Pipe Line Co., 935 F.2d 1469, 1479 (7th Cir. 1991). In *Panhandle Eastern*, the court found that the Illinois Antitrust Act mirrored the Sherman Act based upon the evidence that "the state law claims . . . were modeled after the Sherman Act and Illinois law provides that its courts should use the construction of federal antitrust law by federal courts to guide their construction of those state antitrust laws that are substantially similar to federal antitrust law." *Id. at 1480*.<sup>6</sup> The Court notes that "California has long held that the federal antitrust act—Sherman Act and the Cartwright Act are similar and that Sherman Act cases [\*16] apply, [although not binding], in construing the Cartwright Act." Derish v. San Mateo-Burlingame Board of Realtors, 724 F.2d 1347, 1350 (9th Cir. 1983). However, the Court also recognizes the decision made by the Supreme Court in Connell Construction Company, Inc., v. Plumbers and Steamfitters Local Union No. 100, etc. 421 U.S. 616, 635-36, 95 S. Ct. 1830, 44 L. Ed. 2d 418 (1975). The Supreme Court held that a party's agreement was subject to the federal antitrust laws, but it did not follow that state antitrust law may apply as well because "[p]ermitting state antitrust law . . . could frustrate the basic federal policies . . . and interfere with the detailed system Congress has created for regulating organizational techniques." *Id.* Here, Congress through the FPA, made clear that the interstate "transmission" or "sale" of wholesale energy pursuant to a federal tariff, not merely the "rates," falls within FERC's exclusive jurisdiction. Federal Power Act, 16 U.S.C. § 824e. A bright-line distinction is drawn between wholesale sales, which fall within FERC's plenary jurisdiction, and retail sales or wholesale intrastate sales, over which the states exercise jurisdiction. Duke Energy Trading and Mktg, L.L.C. v. Davis, 267 F.3d 1042, 1056 (9th Cir. 2001). [\*17] Allowing state law claims in the wholesale interstate electricity market would encroach upon the authority Congress entrusted exclusively to FERC.

Edison further argues that state law claims related to wholesale energy have been allowed by the court in Gulf States Util. Co. v. Alabama Power Co., 824 F.2d 1465 (5th Cir. 1987). The court in that case concluded that state law claims concerning contractual disputes were not within the scope of FERC's jurisdiction. The viability of the

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<sup>6</sup>The Court notes that the Ninth Circuit in *Snohomish* and *Dynegy* did not discuss the issue of the similarity between California antitrust law and the Sherman Act. In *Snohomish*, a consumer utility in Washington sued generators and traders of wholesale electricity, for violations of California state antitrust and consumer protection laws. 384 F.3d 756. In *Dynegy*, the Attorney General of the State of California brought state court actions against wholesale electricity suppliers for violations of California's unfair business practices law. 375 F.3d 831. Although the Court does not know whether the issue was raised in either case, it is clear that the issue was not addressed therein.

Edison's comparison depends on [\*18] the substantial similarity of facts between the case before the Court and the cited case. The Court finds that the facts here are distinguishable. First, the state law claims in the cited case were related to contractual issues, which exclusively fall within a state's jurisdiction. The court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. [824 F.2d at 1474](#). Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily intrude upon the rate-setting jurisdiction of FERC. [Grays Harbor, 379 F.3d at 653](#). Therefore, field preemption bars Edison from pursuing its state law claims before the Court.

## 2) Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court disagrees with Edison that the FPA only provides FERC with authority to determine the "just and reasonable" rates for wholesale power. Instead, FERC has broad authority concerning anti-competitive activities related to the filed rate. Accordingly, conflict preemption also bars Edison from pursuing its [\*19] state law claims before the Court.

### C. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. [HN9](#)[<sup>↑</sup>] The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. [E. & J. Gallo Winery v. Encana Energy Servs., Inc., Case No. CV F 03-5412 AWILJO, 2004 U.S. Dist. LEXIS 29383 at \\*29-30](#). The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority." [Ark. L.A. Gas Co. v. Frank Hall, 453 U.S. 571, 577-78, 101 S. Ct. 2925, 69 L. Ed. 2d 856 \(1981\)](#). The Court also acknowledges that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant." [City of Cleveland v. FPC, 525 F.2d 845, 854, 174 U.S. App. D.C. 1 \(D.C. Cir. 1976\)](#).

The [\*20] first argument made by Edison is that the filed rate doctrine is inapplicable because no properly filed rates were on file during the period when the alleged conduct occurred. However, Edison relied on the following finding in [California v. FERC, 383 F.3d 1006, 1016 \(9th Cir. 2004\)](#) to support its position "without the required filings, neither FERC nor any affected party may challenge the rate. Pragmatically, under such circumstances, there is no filed tariff in place at all." *Id.* This argument, however, inappropriately equates the Debtors' alleged violation of the filing requirements with no-filed tariffs. FERC required each seller to file quarterly reports pursuant to FPA §205(c) [16 U.S.C. §824d\(c\)](#) on transaction-specific information about its sales and purchases at market-based rates. The court in *Grays Harbor* concluded, [HN10](#)[<sup>↑</sup>] "while market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine." [379 F.3d at 651](#).

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that "the reporting requirements are an integral part of a tariff, with FERC's implied enforcement [\*21] mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [383 F.3d at 1016](#). On August 13, 2002, FERC's Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of

material information.<sup>7</sup> Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. [106 FERC ¶ 61,024](#). As noted by FERC,

implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market shares) that reflect a departure from the characteristics that the FERC relied upon in granting [\*22] market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. [383 F.3d at 1016](#). Without the availability of retroactive refunds, "[p]arties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

The second argument made by Edison is that the filed rate doctrine is not applicable because the issue presented before the Court is distinguishable from those in *Grays Harbor* and *Snohomish*. The plaintiff in *Snohomish* brought an action against a company that engaged in market manipulation during the energy crisis in violation of [\*23] state antitrust and unfair competition law. The court confirmed that the filed rate doctrine applies because the court could not determine the rates that "would have been achieved in a competitive market." [384 F.3d at 761](#). Similarly, the court in *Grays Harbor* rejected the request from the plaintiff for a determination of the "fair price." [379 F.3d at 645](#). Here, Edison argues that it is not asserting a price which should be paid in a competitive market as the benchmark for a calculation of a remedy. Rather, Edison maintains that the remedy would be unrelated to the ISO tariff and the Court would not have to determine a non-manipulated rate because FERC has done so. Edison argues that it is merely requesting the Court to determine liability, and thereafter, remand to FERC for a determination of remedies.

The Ninth Circuit in *California v. FERC* examined the substance of the law and remanded to FERC for the determination of remedies. The court there declined to order refunds to a state because the court reasoned it was more appropriate for FERC to consider its remedial options in the first instance. [383 F.3d at 1018](#). The substantive law examined by the court in *California v. FERC* concerned [\*24] whether retroactive refunds were legally available. *Id.* As such, no liability issue was raised and determined by that court. Further, the Court finds that determining the liability or the legal right of Edison against the Debtors for violation of the antitrust laws would have to be measured by the tariff. Therefore, the filed rate doctrine would be applicable.

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in [Keogh v. Chicago & N.W.R.Y. Co., 260 U.S. 156, 43 S. Ct. 47, 67 L. Ed. 183 \(1922\)](#), stated that [HN11](#) [↑] "[i]njury implies violation of a legal right." [Id. at 163](#). The Supreme Court concluded that "the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff." [Id. at 163](#). Justice Brandeis explained "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce. Under Section 8 of the latter act . . . the exaction of any illegal rate makes the carrier liable to the 'person injured thereby for the full amount of damages sustained [\*25] in consequence of any such violation.'" [Id. at 162](#). Thus, the finding of liability in antitrust laws would be integral to the Court's determination of whether the Debtors are liable due to their violations of state **antitrust law** and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

<sup>7</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, as required under their market-based rate authorization. [106 FERC ¶ 61,024](#).

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. "In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company." [453 U.S. at 579](#). The Supreme Court rejected this argument by reasoning that "the mere fact that respondents brought this suit under state law would not rescue it, for when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce . . . [HN12](#)[] Under the filed rate doctrine, FERC alone is empowered to make that judgment, [\*26] and until it has done so, no rate other than the one on file may be charged." [Id. at 580-84](#).

Moreover, to award monetary relief, the Court would have to determine a "fair price." Thus, [HN13](#)[] the filed rate doctrine bars the Court from awarding monetary damages sought by Edison. Nonetheless, the Court finds that injunctive relief would also be unavailable to Edison. The Court agrees with the Ninth Circuit's decision in *Snohomish*, which declined to grant [HN14](#)[] injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. [384 F.3d at 762](#). "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC." [Dynegy, 375 F.3d at 836](#).

The decisions from the Second Circuit in [Sun City Taxpayers' Association v. Citizens Utilities Co., 45 F.3d 58 \(2d Cir. 1995\)](#) and [Wegoland Ltd. v. NYNEX Corp., 27 F.3d 17 \(2d Cir. 1994\)](#), provide an additional basis for dismissal of the Claims sought by Edison. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the [\*27] filed rate doctrine. In determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. [Sun City Taxpayers' Ass'n v. Citizens Utils. Co., 847 F.Supp.281, 291 \(D. Conn. 1994\)](#). The Second Circuit in *Wegoland* recognized that the filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. [27 F.3d at 21](#).

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects Edison's challenge to the application of the filed rate doctrine. [\*28] Accordingly, the filed rate doctrine bars the relief sought by Edison.

### III. Conclusion

For the foregoing reasons, the Court concludes that the state law claims sought by Edison concerning electricity market manipulation are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims filed by Edison.

Counsel for the Debtors is directed to settle an order consistent with this Court's Opinion.

Dated: New York, New York

July 6, 2005

**/s/ Arthur J. Gonzalez**

UNITED STATES BANKRUPTCY JUDGE

## Sickles v. Cabot Corp.

Superior Court of New Jersey, Appellate Division

June 8, 2005, Submitted ; July 7, 2005, Decided

DOCKET NO. A-3129-04T53129-04T5

**Reporter**

379 N.J. Super. 100 \*; 877 A.2d 267 \*\*; 2005 N.J. Super. LEXIS 217 \*\*\*; 2005-1 Trade Cas. (CCH) P74,858

LOUIS SICKLES, PLAINTIFF-RESPONDENT, v. CABOT CORPORATION, PHELPS DODGE CORPORATION, COLUMBIAN CHEMICALS COMPANY, DEGUSSA ENGINEERED CARBONS, LP, DEGUSSA AG, AND DEGUSSA CORPORATION, DEFENDANTS-APPELLANTS.

**Subsequent History:** [\*\*\*1] Approved For Publication July 7, 2005.

Certification denied by *Sickles v. Cabot Corp.*, 185 N.J. 297, 884 A.2d 1267, 2005 N.J. LEXIS 1408 (N.J., Oct. 18, 2005)

**Prior History:** On appeal from the Superior Court of New Jersey, Law Division, Camden County, L-6230-03.

## **Core Terms**

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purchasers, indirect, antitrust, carbon black, defendants', manufacture, consumers, anti trust law, unconscionable, tires, antitrust violation, motion to dismiss, damages, consumer fraud, price-fixing, overcharge, practices, putative class, interpretations, products, block, tape, cause of action, treble-damages, ingredient, deception, pass-on, chain, Shoe

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN1[ Motions to Dismiss, Failure to State Claim**

A motion to dismiss under *N.J. Ct. R. 4:6-2(e)* should be approached with great caution and should only be granted in the rarest of instances. Courts must view the allegations with great liberality and without concern for a plaintiff's ability to prove the facts alleged in the complaint.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

## **HN2** Motions to Dismiss, Failure to State Claim

A court must dismiss a plaintiff's complaint if it has failed to articulate a legal basis entitling the plaintiff to relief.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

## **HN3** Motions to Dismiss, Failure to State Claim

A motion to dismiss a complaint under N.J. [R. 4:6-2\(e\)](#) for failure to state a claim upon which relief can be granted must be evaluated in light of the legal sufficiency of the facts alleged in the complaint.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

## **HN4** Motions to Dismiss, Failure to State Claim

A plaintiff's obligation on a motion to dismiss is not to prove the case, but only to make allegations, which, if proven, would constitute a valid cause of action.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

Civil Procedure > Appeals > Standards of Review > General Overview

## **HN5** Motions to Dismiss, Failure to State Claim

Appellate courts review a motion to dismiss by the same standard applied by a trial court; thus, considering and accepting as true the facts alleged in the complaint, the appellate courts determine whether they set forth a claim upon which relief can be granted.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **HN6** Regulated Practices, Price Fixing & Restraints of Trade

See [N.J. Stat. Ann. § 56:9-12](#).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Governments > Courts > Judicial Precedent

379 N.J. Super. 100, \*100L<sup>2005</sup> A.2d 267, \*\*267L<sup>2005</sup> N.J. Super. LEXIS 217, \*\*\*1

## **[HN7](#)[] Regulated Practices, Price Fixing & Restraints of Trade**

New Jersey courts follow federal **antitrust law** in interpreting their own antitrust statute.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Governments > Courts > Judicial Precedent

## **[HN8](#)[] Regulated Practices, Price Fixing & Restraints of Trade**

See [N.J. Stat. Ann. § 56:9-18.](#)

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Governments > Courts > Judicial Precedent

## **[HN9](#)[] Regulated Practices, Price Fixing & Restraints of Trade**

Federal court interpretations of federal law constitute persuasive authority as to the meaning of the particular state antitrust enactments.

Antitrust & Trade Law > Sherman Act > General Overview

## **[HN10](#)[] Antitrust & Trade Law, Sherman Act**

See [15 U.S.C.S. § 1.](#)

Antitrust & Trade Law > Clayton Act > General Overview

## **[HN11](#)[] Antitrust & Trade Law, Clayton Act**

See [15 U.S.C.S. § 15.](#)

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **[HN12](#)[] Purchasers, Direct Purchasers**

The private right of action under the Clayton Act does not extend to indirect purchasers, as only overcharged direct purchasers, and not others in the chain of manufacture or distribution, are parties injured in their business or property within the meaning of the Clayton Act.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

### [HN13](#) [ ] **Private Actions, Standing**

The entire antitrust remedy belongs to, and only to, direct purchasers, i.e., those who purchased an affected product directly from the defendants; indirect or pass-through purchasers, i.e., those who purchased the defendants' product further down the distribution chain, have no standing under federal antitrust law.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

### [HN14](#) [ ] **Purchasers, Direct Purchasers**

The United States Supreme Court has upheld the right of states to allow suits by indirect purchasers under their own antitrust statutes, notwithstanding the federal rule limiting federal antitrust recoveries to direct purchasers.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Governments > Legislation > Statutory Remedies & Rights

Antitrust & Trade Law > Regulated Practices > Private Actions > State Regulation

### [HN15](#) [ ] **Private Actions, Standing**

In a standing context for a private cause of action, given the long history of state common-law and statutory remedies against monopolies and unfair business practices, it is plain that this is an area traditionally regulated by the states.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

### [HN16](#) [ ] **Private Actions, Standing**

In a standing context, nothing in Illinois Brick suggests that it would be contrary to congressional purposes for states to allow indirect purchasers to recover under their own antitrust laws.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN17** [blue icon] Consumer Protection, Deceptive & Unfair Trade Practices

The New Jersey Consumer Fraud Act, [N.J. Stat. Ann. § 56:8-1](#) to -20, should be applied broadly to accomplish its remedial purpose, namely to root out consumer fraud.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN18** [blue icon] Consumer Protection, Deceptive & Unfair Trade Practices

A claim for unconscionable commercial practices must demonstrate a capacity to mislead, a fundamental predicate for maintaining a claim under the New Jersey Consumer Fraud Act, [N.J. Stat. Ann. § 56:8-1](#) to -20.

Governments > Legislation > Interpretation

## **HN19** [blue icon] Legislation, Interpretation

It is basic in the construction of legislation that every effort should be made to harmonize the law relating to the same subject matter.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN20** [blue icon] Private Actions, Standing

The New Jersey Antitrust Act (ATA), [N.J. Stat. Ann. § 56:9-1](#) to -19, does not expressly restrict the right of action to direct purchasers injured by antitrust violations. It is clear, however, based on the holding in Illinois Brick, the harmonization clause of [N.J. Stat. Ann. § 56:9-18](#), and the failed attempt by the New Jersey Legislature to amend the ATA with an Illinois Brick repealer, that an indirect purchaser is precluded from suing for antitrust violations under the ATA.

Antitrust & Trade Law > Clayton Act > Claims

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > Damages

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **HN21** [blue icon] Clayton Act, Claims

Indirect or pass-through purchasers, i.e., those who purchased a manufacturer's product further down the distribution chain, have no standing under federal antitrust laws for damages caused by price-fixing. The indirect purchasers are not parties "injured in their business or property" under Section 4 of the Clayton Act, [15 U.S.C.S. § 15](#).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Governments > Legislation > Interpretation

## [\*\*HN22\*\*](#) [L] **Regulated Practices, Trade Practices & Unfair Competition**

In an antitrust context, [N.J. Stat. Ann. § 56:9-18](#) is a mandatory, not a permissive statute.

Antitrust & Trade Law > Sherman Act > General Overview

Governments > Courts > Judicial Precedent

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [\*\*HN23\*\*](#) [L] **Antitrust & Trade Law, Sherman Act**

As New Jersey's antitrust act was patterned after the Sherman Act, courts have consistently acknowledged the significance of federal antitrust decisions in the interpretation of the state [antitrust law](#).

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > State Regulation

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [\*\*HN24\*\*](#) [L] **Purchasers, Direct Purchasers**

The language of the New Jersey Antitrust Act, [N.J. Stat. Ann. § 56:9-1](#) to -19, conferring the right to treble-damage recovery on any person who shall be injured in his business or property by antitrust violations, [N.J. Stat. Ann. § 56:9-12](#), is identical to Section 4 of the Clayton Act, [15 U.S.C.S. § 15](#).

Governments > Legislation > Interpretation

## [\*\*HN25\*\*](#) [L] **Legislation, Interpretation**

Caution must be exercised in using the action of a legislature on proposed amendments as an interpretative aid in discerning legislative intent.

379 N.J. Super. 100, \*100L<sup>2005</sup> A.2d 267, \*\*267L<sup>2005</sup> N.J. Super. LEXIS 217, \*\*\*1

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Governments > Legislation > Interpretation

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN26**[ **Private Actions, Standing**

In the absence of an Illinois Brick repealer or other language by the New Jersey Legislature evidencing an intent to permit indirect, as well as direct purchasers, to recover for antitrust violations, it is clear New Jersey courts are directed to follow the Illinois Brick holding limiting federal antitrust recoveries to direct purchasers.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Legal Ethics > Legal Services Marketing > Advertising

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN27**[ **Private Actions, Standing**

The New Jersey Consumer Fraud Act, [N.J. Stat. Ann. § 56:8-1](#) to -20, empowers private plaintiffs to recover for treble damages, attorneys fees, and costs upon a demonstration of an ascertainable loss of moneys or property, real or personal, as a result of an unlawful practice as defined by the act. [N.J. Stat. Ann. § 56:8-19](#).

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN28**[ **Consumer Protection, Deceptive & Unfair Trade Practices**

See [N.J. Stat. Ann. § 56:8-2](#).

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Commercial Law (UCC) > General Provisions (Article 1) > Definitions & Interpretation > Good Faith & Fair Dealing

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN29**[ **Consumer Protection, Deceptive & Unfair Trade Practices**

In an antitrust context, the phrase "unconscionable commercial practice," added to [N.J. Stat. Ann. § 56:8-2](#)'s definition of "unlawful practice" in 1971, has been defined as acts lacking good faith, honesty in fact, and observance of fair dealing. Capacity to mislead is the prime ingredient of deception or an unconscionable commercial practice.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### **HN30** [blue icon] Consumer Protection, Deceptive & Unfair Trade Practices

The New Jersey Consumer Fraud Act, [N.J. Stat. Ann. § 56:8-1](#) to -20, was enacted to help eradicate consumer fraud, not to advance public policy in favor of competition and prevent practices that deprive consumers of the benefit of competitive markets, which is the overriding purpose of the New Jersey Antitrust Act, [N.J. Stat. Ann. § 56:9-1](#) to -19.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Contracts Law > Statute of Frauds > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Governments > Legislation > Interpretation

### **HN31** [blue icon] Consumer Protection, Deceptive & Unfair Trade Practices

Although New Jersey's antitrust and consumer fraud statutes are to be liberally interpreted, their remedial provisions are not without limit.

**Counsel:** *Brown and Connery and Jennifer L. Merzon* (*Jones Day*) of the Washington DC bar, admitted pro hac vice, attorneys for appellant Cabot Corporation (*Michael J. Vassalotti and Ms. Merzon*, on the joint brief).

*Dechert and Gary W. Kubek* (*Debevoise & Plimpton*) of the New York bar, admitted pro hac vice, attorneys for appellants Phelps Dodge Corporation and Columbian Chemicals Company (*Michelangelo Troisi*, of counsel; *Michelle Hart Yearly and Mr. Kubek*, on the joint brief).

*Campbell, Campbell, Edwards & Conroy and Hima Vatti* (*O'Melveny & Myers*) of the Washington DC bar, admitted pro hac vice, attorneys for Degussa Engineered Carbons, LP, Degussa AG, and Degussa Corporation (*C. Scott Toomey, William A. Rupert and Ms. Vatti*, on the joint brief).

*Sufrin Zucker Steinberg Sonstein & Wixted, Krishna B. Narine*, of the Pennsylvania bar, admitted pro hac vice, *Steven E. Connolly* (*Schiff & Waide*) of the Pennsylvania bar, admitted pro hac vice, and *Isaac L. Diel*, admitted pro hac vice, of the Kansas bar, attorneys for respondent (*Ms. Narine, Mr. Connolly and Mr. Diel*, of counsel; *David W. Sufrin*, on the brief).

**Judges:** Before Judges NEWMAN, AXELRAD and BILDER. The opinion of the court was delivered by AXELRAD, J.T.C. (temporarily assigned).

**Opinion by:** AXELRAD

## Opinion

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[\*103] [\*\*268] The opinion of the court was delivered by

[\*\*269] AXELRAD, J.T.C. (temporarily assigned).

A purchaser of Goodyear tires filed a class action suit against companies which produce, manufacture and sell carbon black, a primary ingredient in tires. At issue in this appeal is whether an [\*104] indirect purchaser of an allegedly price-fixed product may state a claim for antitrust violations under the New Jersey Antitrust Act (ATA), [N.J.S.A. 56:9-1 to -19](#), and the New Jersey Consumer Fraud Act (CFA), [N.J.S.A. 56:8-1 to -20](#). We hold that neither statute provides a cause of action to a pass-through purchaser such as the putative class plaintiff, and reverse the order of the Law Division denying defendants' motion to dismiss plaintiff's complaint under [Rule 4:6-2\(e\)](#).

In November and December 2001, plaintiff Louis Sickles purchased from the Goodyear Auto Service Center in Cherry Hill, New Jersey, two Goodyear tires [\*\*\*3] (P215/70R15 97S S1 Regatta 2 XNWRPTL) for his wife's vehicle and one Goodyear tire (P205/65 R15 92H S1 Eagle HP VSBLRPTL) for his vehicle. He then filed an action alleging violations of the ATA and CFA, seeking damages on behalf of

[a]ll persons residing in the state of New Jersey who purchased any product that was manufactured using Carbon Black sold by Defendants from January 1999 through November 2002.

Defendants are Cabot Corporation (Cabot); Phelps Dodge Corporation (Phelps Dodge); Columbian Chemicals Company (Columbian); Degussa Engineered Carbons, LP (DEC); Degussa AG; and Degussa Corporation. Cabot, a Delaware corporation with its principal place of business in Massachusetts, is the world's largest producer of carbon black, accounting for one-quarter of the worldwide production capacity and market share. Phelps Dodge is a New York corporation with its principal place of business in Arizona and wholly owns the subsidiary Columbian, which is engaged in the manufacture and sale of carbon black within the United States and throughout the world and maintains a carbon black facility in Ulysses, Kansas. DEC, a limited partnership with its principal place of business in [\*\*\*4] New Jersey, is co-owned by Degussa AG and engages in the manufacture and sale of carbon black throughout the world.

Carbon black is a mixture of partially burned hydrocarbons produced by a combustion of natural gas. It is used as a reinforcing agent in rubber products such as tires, tubes, cables [\*105] and conveyor belts and is the primary ingredient in car and truck tires. It is also used as an ingredient in countless other products such as dry-cell batteries, electrical conductors, and carbon brushes, and as a pigment in printing, carbon paper, typewriter ribbon inks, paints, photocopier toner and record discs.

The complaint alleged that defendants and their co-conspirators engaged in anti-competitive activities in violation of the ATA to artificially raise, stabilize, and maintain the price of carbon black sold by defendants from January 1999 through November 2002, resulting in plaintiff and other similarly situated consumers paying more for tires containing carbon black than they would have in the absence of defendants' alleged unlawful conduct. Plaintiff further claimed that defendants coordinated and cooperated with one another to implement output restrictions and price increases [\*\*\*5] and agreed not to compete against one another to increase their respective market shares. Plaintiff also alleged these acts constituted an unconscionable practice under the CFA.

By order of November 29, 2004, the trial court denied defendants' motion to dismiss [\*\*270] plaintiff's complaint for failure to state a claim. On February 24, 2005, we granted defendants' motion for leave to appeal. Defendants raise the following issues on appeal:

*POINT I*

THE [ATA] DISALLOWS INDIRECT PURCHASER CLAIMS.

1. The Harmonization Provision of the [ATA] Directs Conformity To Federal Antitrust Precedents, and Thus Prohibits Plaintiff's Claims.

2. The New Jersey Legislature Rejected An *Illinois Brick* Repealer Bill.

3. The Trial Court Erred in Failing To Follow *Illinois Brick* and in Misapplying *ARC America*.

#### *POINT II*

THE []CFA DOES NOT ALLOW PLAINTIFF'S CLAIM.

1. The []CFA Does Not Cover Any Antitrust Claims Whatsoever.

2. The []CFA Cannot Be Used To Make An End Run Around the [ATA's] Bar of Indirect Purchaser Claims.

We find these arguments persuasive.

#### I

We recognize the indulgent standard that applies to review of complaints in [\*\*\*6] the context of a motion to dismiss for [\*106] failure to state a claim. *Printing Mart-Morristown v. Sharp Electronics Corp.*, 116 N.J. 739, 771-72, 563 A.2d 31 (1989). [HN1](#) A motion to dismiss under *Rule 4:6-2(e)* should be "approach[ed] with great caution" and should only be granted in "the rarest of instances." *Ibid.* We must view the allegations with great liberality and without concern for the plaintiff's ability to prove the facts alleged in the complaint. *Id. at 746, 563 A.2d 31*.

However, [HN2](#) a court must dismiss the plaintiff's complaint if it has failed to articulate a legal basis entitling plaintiff to relief. *Camden County Energy Recovery Assocs., L.P. v. New Jersey Dep't of Envtl. Prot.*, 320 N.J. Super. 59, 64, 726 A.2d 968 (App.Div.1999). [HN3](#) "A motion to dismiss a complaint under *Rule 4:6-2(e)* for failure to state a claim upon which relief can be granted must be evaluated in light of the legal sufficiency of the facts alleged in the complaint." *Donato v. Moldow*, 374 N.J. Super. 475, 482, 865 A.2d 711 (App.Div.2005). [HN4](#) The plaintiff's obligation on a motion to dismiss [\*\*\*7] is "not to prove the case but only to make allegations, which, if proven, would constitute a valid cause of action." *Leon v. Rite Aid Corp.*, 340 N.J. Super. 462, 472, 774 A.2d 674 (App.Div.2001).

[HN5](#) We review such a motion by the same standard applied by the trial court; thus, considering and accepting as true the facts alleged in the complaint, we determine whether they set forth a claim upon which relief can be granted. *Donato, supra, 374 N.J. Super. at 483, 865 A.2d 711*.

#### II

The ATA was passed in 1970 "to promote the unhampered growth of commerce and industry throughout the State by prohibiting restraints of trade which are secured through monopolistic practices and which act or tend to act to decrease competition between and among persons engaged in commerce and trade." *N.J.S.A. 56:9-1* (Historical and Statutory Notes). Under the ATA, [HN6](#) "[a]ny person who shall be injured in his business or [\*107] property by reason of a violation of the provisions of this act may sue therefor and shall recover threefold the damages sustained by him, together with reasonable attorneys' fees, filing fees and reasonable costs of suit." *N.J.S.A. 56:9-12*.

[\*\*\*8] [HN7](#) We follow federal *antitrust law* in interpreting our own antitrust statute. [\*\*271] See *N.J.S.A. 56:9-18* [HN8](#) ("This act shall be construed in harmony with ruling judicial interpretations of comparable Federal antitrust statutes and to effectuate, insofar as practicable, a uniformity in the laws of those states which enact it."). See also *Pomanowski v. Monmouth County Bd. of Realtors*, 89 N.J. 306, 313, 446 A.2d 83 (1982) (Because the ATA is patterned after the *Sherman Antitrust Act*, courts have "concluded that [HN9](#) federal court interpretations of federal law constitute persuasive authority as to the meaning of the particular state enactments.") (quoting *State v. Lawn King, Inc.*, 84 N.J. 179, 192, 417 A.2d 1025 (1980)).

Passed by Congress in 1890, the Sherman Act, *15 U.S.C.A. § 1*, declares illegal [HN10](#) "[e]very contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations. . ." Section 4 of the Clayton Act, *15 U.S.C.A. § 15*, provides a private right of action

to [HN11](#) "any person who shall be injured in his business [\*\*\*9] or property by reason of anything forbidden in the antitrust laws."

[HN12](#) This private right, however, does not extend to indirect purchasers, as only overcharged direct purchasers, and not others in the chain of manufacture or distribution, are parties "injured in [their] business or property" within the meaning of the Clayton Act. [\*Illinois Brick Co. v. Illinois\*, 431 U.S. 720, 97 S. Ct. 2061, 52 L. Ed. 2d 707](#), *reh'g denied*, 434 U.S. 881, 98 S. Ct. 243, 54 L. Ed. 2d 164 (1977). In *Illinois Brick* the State of Illinois, on behalf of itself and 700 municipalities who were indirect purchasers of concrete block, brought an antitrust action under [Section 4 of the Clayton Act](#), alleging concrete block manufacturers and distributors had fixed prices of the concrete block in violation of [Section 1 of the Sherman Act](#). [\*Id. at 726-27, 97 S. Ct. at 2065, 52 L. Ed. 2d at 713\*](#). As in the present case, the plaintiffs did not purchase the products directly from the defendants. Rather, the plaintiffs "[sought] to demonstrate that masonry contractors, who incorporated [defendants'] block into walls and other masonry structures, passed on the alleged [\*\*\*10] overcharge on the block to general contractors, who incorporated the masonry structures into entire buildings, and that the general contractors in turn passed on the overcharge to [plaintiffs] in the bids submitted for those buildings." [\*Id. at 735, 97 S. Ct. at 2069, 52 L. Ed. 2d at 718\*](#). Thus, the block passed through two separate levels in the chain of distribution before reaching the plaintiffs. [\*Id. at 726, 97 S. Ct. at 2065, 52 L. Ed. 2d at 713\*](#).

The Supreme Court held that [HN13](#) the entire antitrust remedy belongs to, and only to, direct purchasers, i.e., those who purchased the affected product directly from the defendants, and that indirect or pass-through purchasers, i.e., those who purchased the defendants' product further down the distribution chain, have no standing under federal [antitrust law](#). As the Court reasoned,

[p]ermitting the use of pass-on theories under [S. 4](#) essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge from direct purchasers to middlemen to ultimate consumers. . . . [This] would add whole [\*\*\*11] new dimensions of complexity to the treble-damages suits and undermine their effectiveness.

[\*\[Id. at 737, 97 S. Ct. at 2070, 52 L. Ed. 2d at 719.\]\*](#)

This rationale was consistent with the Court's holding in [\*Hanover Shoe, Inc. v. United Shoe Machinery Corp.\*, 392 U.S. 481, 88 S. Ct. 2224, 20 L. Ed. 2d 1231 \(1968\)](#), an antitrust action brought under [Section 4 of the Clayton Act](#) [\[\\*\\*272\]](#) against a manufacturer of shoe machinery by one of its customers, a manufacturer of shoes. The Court rejected as a matter of law the defense that the retailer plaintiff as a direct purchaser had not been injured in its business as required by the statute because it had passed on the claimed illegal overcharge to its customers who were indirect purchasers of defendant's shoe machinery. [\*Id. at 494, 88 S. Ct. at 2232, 20 L. Ed. 2d at 1241-42\*](#).

[\[\\*109\]](#) In *Illinois Brick*, the Supreme Court reaffirmed its holding in *Hanover Shoe*, concluding the rationale in that case could not justify unequal treatment of plaintiffs and defendants with respect to the permissibility of pass-on arguments:

The principal basis for the decision in *Hanover Shoe* was the [\[\\*12\]](#) Court's perception of the uncertainties and difficulties in analyzing price and output decisions "in the real economic world rather than an economist's hypothetical model," . . . and of the costs to the judicial system and the efficient enforcement of the antitrust laws of attempting to reconstruct those decisions in the courtroom. This perception that the attempt to trace the complex economic adjustments to a change in the cost of a particular factor of production would greatly complicate and reduce the effectiveness of already protracted treble-damages proceedings applies with no less force to the assertion of pass-on theories by plaintiffs than it does to the assertion by defendants. . . . Indeed, the evidentiary complexities and uncertainties involved in the defensive use of pass-on against a direct purchaser are multiplied in the offensive use of pass-on by a plaintiff several steps removed from the defendant in the chain of distribution. The demonstration of how much of the overcharge was passed on by the first

purchaser must be repeated at each point at which the price-fixed goods changed hands before they reached the plaintiff.

[\*\*\*13] [*Illinois Brick, supra, 431 U.S. at 731-33; 97 S. Ct. at 2067-68, 52 L. Ed. 2d at 716-17* (internal citation omitted).]

Additionally, the Court reasoned if both direct and indirect purchasers were permitted to recover, antitrust defendants would be exposed to duplicate damages for the same injury. *Id. at 746-47, 97 S. Ct. at 2075, 52 L. Ed. 2d at 725-26*.

In response to *Illinois Brick*, several state legislatures amended their antitrust acts to include a so-called "Illinois Brick repealer" expressly granting standing in antitrust treble-damage actions to indirect purchasers, including the ultimate consumers.<sup>1</sup> In [\*\*273] *California [\*110] v. ARC America Corp., 490 U.S. 93, 109 S. Ct. 1661, 104 L. Ed. 2d 86 (1989)*, HN14<sup>↑</sup> the Supreme Court upheld the right of states to allow suits by indirect purchasers under their own antitrust statutes, notwithstanding the federal rule limiting federal antitrust recoveries to direct purchasers. The Court found that HN15<sup>↑</sup> "[g]iven the long history of state common-law and statutory remedies against monopolies and unfair business practices, it is plain that this is an area traditionally regulated by the States." *Id. at 101, 490 U.S. 93, 109 S. Ct. 1661, 104 L. Ed. 2d at 94-95* [\*\*\*14] (footnote omitted). In concluding that state indirect purchaser statutes were not pre-empted by federal law, the Court stated, HN16<sup>↑</sup> "nothing in *Illinois Brick* suggests that it would be contrary to congressional purposes for States to allow indirect purchasers to recover under their own antitrust laws." *Id. at 103, 109 S. Ct. at 1666, 104 L. Ed. 2d at 96*.

[\*\*\*15] Not only has our Legislature not enacted a repealer amendment in response to *Illinois Brick*, but when an attempt was made, the bill was never reported out of committee. (Assembly Bill No. 4629, March 11, 1991). The bill proposed to amend N.J.S.A. 56:9-12 of the ATA to allow recovery to "[a]ny person who shall be injured directly or indirectly in his business or property by reason of a violation of the provisions of this act." The statement [\*111] accompanying the bill expressly referenced the *Illinois Brick* holding and stated it was intended to clarify that under the [ATA], indirect purchasers of goods and services are permitted to seek damages in antitrust cases. The bill would create a presumption that in the absence of a preponderance of evidence to the contrary, the final indirect purchaser of goods and services is the party actually injured in the antitrust violation. [Statement to Assembly Bill No. 4629 (March 11, 1991).]

In the present case, the trial judge recognized our courts' obligation to follow federal law in construing the ATA and, under *Illinois Brick*, that federal antitrust law prohibits indirect purchaser suits. [\*\*\*16] He further acknowledged that our Legislature declined to pass an *Illinois Brick* repealer. The judge concluded, however, that a claim asserting

<sup>1</sup> Twenty-three states and the District of Columbia have adopted *Illinois Brick* repealer statutes: Alabama, Ala. Code § 6-5-60(a) 2005; Alaska, Alaska Stat. § 45.50.577 (Michie 2004); California, Cal. Bus. & Prof. Code § 16750(a) (West 2005); Colorado, Colo. Rev. Stat. Ann. § 6-4-111(2) (West 2005) (authorizing the state attorney general to bring suit for indirect injury to any government or public entity); District of Columbia, D.C. Code Ann. § 28-4509 (2005); Hawaii, Haw. Rev. Stat. Ann. §§ 480-3, -13, and -14 (Michie 2004) (allowing the state attorney general to file class action suit on behalf of indirect purchasers); Idaho, Idaho Code § 48-108(2) (Michie 2004) (permitting the state attorney general as parens patriae to bring suit); Illinois, 740 Ill. Comp. Stat. Ann. 10/7(2) (West 2005); Kansas, Kan. Stat. Ann. § 50-161(b) (2004); Maine, Me. Rev. Stat. Ann. tit. 10, § 1104(1) (West 2005); Maryland, Md. Code Ann., Com. Law II § 11-209(b)(2)(ii) (2005) (allowing the state and its subdivisions to bring indirect purchaser suits); Michigan, Mich. Comp. Laws § 445.778(2) (2005); Minnesota, Minn. Stat. Ann. § 325D.57 (West 2005); Mississippi, Miss. Code Ann. § 75-21-9 (2005); Nebraska, Neb. Rev. Stat. § 59-821 (2005); Nevada, Nev. Rev. Stat. 598A.210(2) (2005); New Mexico, N.M. Stat. Ann. § 57-1-3(A) (Michie 2005); New York, N.Y. Gen. Bus. Law § 340(6) (McKinney 2005); North Dakota, N.D. Cent. Code § 51-08.1-08(3) (2003); Oregon, Ore. Rev. Stat. § 646.775(1) (2005) (allowing attorney general to sue on behalf of indirect purchasers); Rhode Island, R.I. Gen. Laws § 6-36-12 (2004) (allowing attorney general to sue on behalf of indirect purchasers); South Dakota, S.D. Codified Laws § 37-1-33 (Michie 2005); Vermont, Vt. Stat. Ann. tit. 9, § 2465(b) (2004); Wisconsin, Wis. Stat. Ann. § 133.18(1)(a) (West 2005). See Bunker's Glass Co., v. Pilkington PLC, 206 Ariz. 9, 75 P.3d 99, 104 n. 4 (2003).

an antitrust violation by an indirect purchaser, such as plaintiff, is cognizable under both the ATA and CFA. His rationale was based on the Supreme Court's ruling in *ARC America* permitting states to allow indirect purchaser suits, the broad language of [N.J.S.A. 56:9-12](#) which grants standing to "[a]ny person who shall be injured in his business or property" to bring an action under the ATA for an antitrust violation, and the absence of express statutory language prohibiting indirect purchasers from suing under the ATA. (Emphasis added). The judge further concluded that plaintiffs "put forth a cause of action based on defendants' alleged price fixing, which . . . can be construed as . . . an unconscionable commercial practice" under the CFA.

We decline to adopt this rationale. We are persuaded, instead, by the logic and analysis of Judge Miniman in [Island Mortgages of New Jersey v. 3M](#), 373 N.J. Super. 172, 860 A.2d 1013 (Law Div. 2004), denying standing to a putative class of purchasers of invisible and [\*\*\*17] transparent tape products [\*\*274] to assert an antitrust claim against 3M, a tape manufacturer, under the CFA. The plaintiffs, who purchased 3M products through independent retailers, alleged that "3M engaged in a course of unconscionable conduct aimed at restricting the access of plaintiffs and the class to lower-priced transparent tape offered by 3-M competitors" [\*112] through tactics such as a rebate structure which rewarded retailers for refusing to carry private label Scotch tape and providing cash incentives for entering into exclusive arrangements with defendant. [Id. at 175-76, 860 A.2d 1013](#). According to the plaintiffs, "[t]he effect of such arrangements was to prevent retailers from offering lower cost private label Scotch tape to plaintiffs and the class" causing "significant harm to class members by increasing the price they have paid for transparent tape above competitive levels and/or by denying them a free choice in a competitive market, as well as the benefits of innovation." [Id. at 176, 860 A.2d 1013](#). As in the present case, the plaintiffs rested their CFA claim on the legal theory that 3M's alleged monopolistic conduct was, by itself, an unconscionable commercial practice actionable [\*\*\*18] under the CFA. [Id. at 177, 860 A.2d 1013](#).

The court acknowledged [HN17](#)[<sup>17</sup>] the CFA should be "applied broadly to accomplish its remedial purpose, namely to root out consumer fraud." [Id. at 176, 860 A.2d 1013](#) (quoting [Lemelledo v. Beneficial Mgmt. Corp. of Am.](#), 150 N.J. 255, 264, 696 A.2d 546 (1997)). Nevertheless, the court granted the defendants' motion to dismiss under [Rule 4:6-2\(e\)](#), concluding the plaintiffs had "failed to set forth any factual allegation that would satisfy the requirement that [HN18](#)[<sup>18</sup>] a claim for unconscionable commercial practices demonstrate 'a capacity to mislead[,]' a fundamental predicate for maintaining a claim under the CFA. [Island Mortgages, supra](#), 373 N.J. Super. at 177, 860 A.2d 1013 (citing [Fenwick v. Kay America Jeep, Inc.](#), 72 N.J. 372, 378, 371 A.2d 13 (1977); [New Jersey Citizen Action v. Schering-Plough Corp.](#), 367 N.J. Super. 8, 13, 842 A.2d 174 (App.Div.), certif. denied, 178 N.J. 249, 837 A.2d 1092 (2003); and [Leon v. Rite Aid Corp.](#), 340 N.J. Super. 462, 470-72, 774 A.2d 674 (App.Div. 2001)).

Alternatively, the court dismissed the plaintiffs' [\*\*\*19] complaint on the grounds that, as indirect purchasers, they lacked standing to pursue antitrust claims under the CFA. [Island Mortgages, supra](#), 373 N.J. Super. at 177-78, 860 A.2d 1013. The court reasoned that indirect purchasers would lack standing to pursue claims under [\*113] the ATA based on the harmonizing provision of [N.J.S.A. 56:9-18](#) and the Supreme Court's holding in *Illinois Brick*, which deprives indirect consumers of standing under the Clayton Act. [Id. at 179-80, 860 A.2d 1013](#). Accordingly, the plaintiffs were precluded from attempting to recast the very same antitrust conduct as a CFA claim. *Ibid.* The court insightfully stated:

This court finds that plaintiffs' attempt to bring suit under the [CFA] is in direct conflict with the well-founded policies interpreting federal and New Jersey [antitrust law](#). Plaintiffs in this case allege conduct that is traditionally classified under [antitrust law](#). Although the CFA should be broadly applied, in this instance, allowing plaintiffs to move forward with their suit would undermine the standing requirements of the [ATA]. [HN19](#)[<sup>19</sup>] "It is basic in the construction of legislation that every effort should [\*\*\*20] be made to harmonize the law relating to the same subject matter." [State v. Green](#), 62 N.J. 547, 554, 303 A.2d 312, 316 (1973).

[[Id. at 180, 860 A.2d 1013](#).]

We recognize that [HN20](#)[<sup>20</sup>] the ATA does not expressly restrict the right of action to [\*\*275] direct purchasers injured by antitrust violations. It is clear, however, based on the holding in *Illinois Brick*, the harmonization clause of

N.J.S.A. 56:9-18, and the failed attempt by our Legislature to amend the ATA with an *Illinois Brick* repealer, that an indirect purchaser is precluded from suing for antitrust violations under the ATA. The United States Supreme Court unequivocally held in *Illinois Brick* that HN21 [indirect or pass-through purchasers, i.e., those who purchased a manufacturer's product further down the distribution chain, have no standing under federal antitrust laws for damages caused by price-fixing. The Court expressly found that indirect purchasers were not parties "injured in [their] business or property" under Section 4 of the Clayton Act. *Illinois Brick, supra*, 431 U.S. at 728-29, 97 S. Ct. at 2061, 52 L. Ed. 2d at 714-15. In ARC California, the [\*\*\*21] Court merely held that state indirect purchaser laws, so-called *Illinois Brick* repealers, were not pre-empted by federal law, notwithstanding the *Illinois Brick* rule limiting federal antitrust recoveries under the Clayton Act to direct purchasers. The decision did not create a cause of action for indirect purchasers to pursue.

Our Legislature specifically incorporated federal precedent, providing in N.J.S.A. 56:9-18 that the ATA "shall be construed [\*114] in harmony with ruling judicial interpretations of comparable Federal antitrust statutes. . . ." HN22 [This is a mandatory, not a permissive statute. HN23] As our antitrust act was patterned after the Sherman Act, we have consistently "acknowledged the significance of federal antitrust decisions in the interpretation of our State antitrust law." *Monmouth Chrysler-Plymouth, Inc. v. Chrysler Corp.*, 102 N.J. 485, 494, 509 A.2d 161 (1986) (citing *Pomanowski, supra*, 89 N.J. at 313, 446 A.2d 83; *Lawn King, supra*, 84 N.J. at 179, 417 A.2d 1025). HN24 [The language of our ATA conferring the right to treble-damage recovery on "[a]ny person who shall be injured in his business or property" by antitrust [\*\*\*22] violations, N.J.S.A. 56:9-12, is identical to Section 4 of the Clayton Act.

In *Illinois Brick*, the United States Supreme Court rendered a decision directly on point construing that language and limiting federal antitrust recoveries to direct purchasers. Although we recognize that a piece of legislation may not be reported out of committee for a variety of reasons unrelated to its substance and that legislative inaction is not conclusive, the fact that in 1991 our Legislature expressly considered, and rejected, an *Illinois Brick* repealer amendment to the ATA, clearly signals its agreement with *Illinois Brick*. See, e.g., *Garden State Farms, Inc. v. Bay*, 77 N.J. 439, 453, 390 A.2d 1177 (quoting 2A *Sutherland Statutory Construction*, § 48.18 at 225 (Sands ed., 4th ed. 1973)) HN25 [("Caution must be exercised in using the action of the legislature on proposed amendments as an interpretative aid' in discerning legislative intent."). Thus, HN26 [in the absence of an *Illinois Brick* repealer or other language by our Legislature evidencing an intent to permit indirect, as well as direct purchasers, to recover for antitrust violations, [\*\*\*23] it is clear New Jersey courts are directed to follow the *Illinois Brick* holding.<sup>2</sup>

[\*115] [\*\*276] Plaintiff brought this antitrust action seeking to recover treble damages under the ATA on behalf of all residents [\*\*\*24] of New Jersey "who purchased any product that was manufactured using Carbon Black sold by Defendants from January 1999 through November 2002." As the pleadings clearly indicate that plaintiff's putative class is comprised of indirect or pass-through purchasers, plaintiff has no standing to bring suit against defendants under N.J.S.A. 56:9-12 for alleged antitrust violations. Accordingly, defendants' motion to dismiss the complaint for failure to state a claim under Rule 4:6-2(e) should have been granted.

### III

Nor can this putative class plaintiff maintain an action seeking damages for monopolization, price-fixing, and other anticompetitive activities under the CFA. Enacted in 1960, the CFA "was passed in response to widespread complaints about selling practices which victimized consumers." *Fenwick, supra*, 72 N.J. at 376, 371 A.2d 13. It was

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<sup>2</sup> Of the twenty-six states and District of Columbia that allow some form of indirect purchaser actions for antitrust violations, only four of the states have done so by judicial construction of their statutes in the absence of an *Illinois Brick* repealer: Arizona, *Bunker's Glass Co. v. Pilkington, PLC*, 206 Ariz. 9, 75 P.3d 99, 106-08 (2003); Iowa, *Comes v. Microsoft Corp.*, 646 N.W.2d 440, 451 (Iowa 2002); North Carolina, *Hyde v. Abbott Labs., Inc.*, 123 N.C. App. 572, 473 S.E.2d 680, 684 (1996); and Tennessee, *Blake v. Abbott Labs., Inc.*, 894 F. Supp. 327, 329 (E.D.Tenn.1995). We note that Arizona's antitrust statute is phrased permissively, rather than mandatorily. *Bunker's Glass Co., supra*, 75 P.3d at 105.

intended to "root out consumer fraud" and protect consumers by eliminating "sharp practices and dealings in the marketing of merchandise and real estate whereby the consumer could be victimized by being lured into a purchase through fraudulent, deceptive or other similar [\*\*\*25] kind of selling or advertising practices." *Lemelledo, supra, 150 N.J. at 266, 696 A.2d 546* (quoting *Daaleman v. Elizabethtown Gas Co., 77 N.J. 267, 271, 390 A.2d 566 (1978)*). **HN27**[<sup>↑</sup>] The CFA empowers private plaintiffs to recover for treble damages, attorneys fees and costs upon a demonstration of an "ascertainable loss of moneys or property, real or personal" as a result of an unlawful practice as defined by the act. *N.J.S.A. 56:8-19*. The CFA declares the following to be an unlawful practice:

[\*116] **HN28**[<sup>↑</sup>] The act, use or employment by any person of any unconscionable commercial practice, deception, fraud, false pretense, false promise, misrepresentation, or the knowing, concealment, suppression, or omission of any material fact with intent that others rely upon such concealment, suppression or omission, in connection with the sale or advertisement of any merchandise or real estate, or with the subsequent performance of such person as aforesaid, whether or not any person has in fact been misled, deceived or damaged thereby. . . .

[*N.J.S.A. 56:8-2*.]

**HN29**[<sup>↑</sup>] The phrase "unconscionable commercial practice[.]" [\*\*\*26] added to the definition of "unlawful practice" in 1971, *N.J.S.A. 56:8-2*, L. 1971, c. 247, § 1 (June 29, 1971), has been defined by our Supreme Court as acts lacking "good faith, honesty in fact, and observance of fair dealing." *Cox vs. Sears Roebuck & Co., 138 N.J. 2, 18, 647 A.2d 454 (1994)*. "[C]apacity to mislead is the prime ingredient of deception or an unconscionable commercial practice." *Fenwick, supra, 72 N.J. at 378, 371 A.2d 13*.

Plaintiff's complaint is bereft of any allegation that defendants used deception, fraud or misrepresentation or concealed material facts concerning the sale of carbon black to the putative class of consumers. Plaintiff does not allege that defendant carbon black manufacturers made any misrepresentations to him, fraudulently concealed any carbon black pricing information from him, or had communication or contact of any kind with him. Nor does he assert that defendants' price-fixing of carbon black, an ingredient in tires, lured [\*\*277] him into, or even influenced, his decision to purchase Goodyear tires. Even with every reasonable inference of fact and the most liberal construction, *Printing Mart-Morristown, supra, 116 N.J. at 746, 563 A.2d 31*, [\*\*\*27] these claims cannot be read into plaintiff's lawsuit. Plaintiff's sole legal theory under the CFA is that defendants' alleged monopolistic conduct constitutes an unconscionable commercial practice. Plaintiff has failed to set forth any factual allegations to demonstrate "a capacity to mislead" as there is nothing inherently misleading in defendants' alleged acts of controlling the supply and overcharging for the price-fixed products.

Moreover, the putative class plaintiff lacks standing to pursue his CFA claim. **HN30**[<sup>↑</sup>] The CFA was enacted to help eradicate [\*117] consumer fraud, not to "advance public policy in favor of competition and prevent practices which deprive consumers of the benefit of competitive markets" which is the "overriding purpose of the *New Jersey Antitrust Act*." *Ideal Dairy Farms, Inc. v. Farmland Dairy Farms, Inc., 282 N.J. Super. 140, 175, 659 A.2d 904 (App.Div.)*, certif. denied, 141 N.J. 99, 660 A.2d 1197 (1995). Plaintiff alleges only that defendants' price-fixing and monopolistic conduct resulted in higher-priced tires. Thus, for us to permit an indirect purchaser, such as plaintiff, to recast his antitrust claim as a consumer fraud violation would undermine [\*\*\*28] the standing requirements of the ATA and would "essentially permit an end run around the policies allowing only direct purchasers to recover under the *Antitrust Act*." *Abbott Labs., Inc. v. Segura, 907 S.W.2d 503, 506, (Texas 1995)*; see also *Blewett v. Abbott Labs., 86 Wn. App. 782, 938 P.2d 842 (1997)*, review denied, 133 Wn.2d 1029, 950 P.2d 475 (1998) (denying an indirect purchaser standing to recover for antitrust conduct through a lawsuit under its consumer fraud act). Cf. *Mack v. Bristol-Myers Squibb Co., 673 So.2d 100 (Fla.Dist.Ct.App.1996)*, review dismissed, 689 So.2d 1068 (1977) (permitting indirect purchasers to sue under Florida's consumer protection statute which contained language protecting consumers from "unfair methods of competition" in addition to unconscionable, deceptive and unfair acts).

**HN31**[<sup>↑</sup>] Although we recognize our antitrust and consumer fraud statutes are to be liberally interpreted, their remedial provisions are not without limit. In analyzing and interpreting these statutes in light of their context,

historical background, policy considerations, legislative [\*\*\*29] history, case law, and policy considerations, we are satisfied our holding advances the intent and spirit of the ATA and CFA.

As plaintiffs, indirect consumers, do not have a valid cause of action against defendants under either the ATA or the CFA, defendants' motion to dismiss plaintiff's complaint under Rule 4:6-2(e) should not have been denied by the trial court.

[\*118] Accordingly, the order of November 29, 2004 is reversed and plaintiff's complaint is dismissed with prejudice.

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End of Document



## Chase Med., LP v. CHF Techs., Inc.

United States District Court for the Northern District of Texas, Dallas Division

July 11, 2005, Decided ; July 11, 2005, Filed

Civil Action No. 3:04-CV-2570-M

### **Reporter**

2005 U.S. Dist. LEXIS 13731 \*; 2005 WL 1638976

CHASE MEDICAL, LP, Plaintiff, v. CHF TECHNOLOGIES, INC., and ENDOSCOPIC TECHNOLOGIES, INC., Defendants.

**Subsequent History:** Appeal dismissed by [Chase Med., Inc. v. CHF Techs., Inc., 2008 U.S. App. LEXIS 14161 \(Fed. Cir., June 17, 2008\)](#)

## **Core Terms**

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affirmative defense, Counterclaims, motion to strike, argues, allegations, patent, redundant, portions, amend

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

### **HN1 [?] Amendment of Pleadings, Leave of Court**

Under [Fed. R. Civ. P. 15\(a\)](#), a court has discretion to grant defendant's request to amend his answer, and it should do so unless the court uncovers a substantial reason for refusing amendment. [Fed. R. Civ. P. 15\(a\)](#) requires the trial court to grant leave to amend freely, and the language of this rule evinces a bias in favor of granting leave to amend.

Civil Procedure > ... > Pleadings > Counterclaims > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrers & Objections > General Overview

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > General Overview

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > Immaterial Matters

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > Redundant Matters

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > Scandalous Matters

## [\*\*HN2\*\*](#) [down arrow] **Pleadings, Counterclaims**

Under [\*Fed. R. Civ. P. 13\(f\)\*](#), a court may strike from a pleading any insufficient defense or any redundant, immaterial, impertinent or scandalous matter. However, motions to strike are disfavored, and when the contents of a pleading are legally sufficient, but improper for some other reason, a motion to strike should be granted only when the moving party shows that the inclusion of the disputed claims or defenses would cause it prejudice. If the moving party does not show prejudice, the court should defer action on the motion and leave the sufficiency of the allegations for determination on the merits.

[Antitrust & Trade Law](#) > ... > [Private Actions](#) > [Remedies](#) > [General Overview](#)

[Civil Procedure](#) > ... > [Pleadings](#) > [Heightened Pleading Requirements](#) > [General Overview](#)

[Civil Procedure](#) > ... > [Pleadings](#) > [Complaints](#) > [Requirements for Complaint](#)

## [\*\*HN3\*\*](#) [down arrow] **Private Actions, Remedies**

Antitrust claims are not held to a heightened pleading standard, and the plaintiff need only include a short and plain statement of the claim showing an entitlement to relief.

[Civil Procedure](#) > ... > [Pleadings](#) > [Counterclaims](#) > [General Overview](#)

[Civil Procedure](#) > ... > [Defenses, Demurrsers & Objections](#) > [Affirmative Defenses](#) > [General Overview](#)

[Civil Procedure](#) > ... > [Defenses, Demurrsers & Objections](#) > [Motions to Strike](#) > [General Overview](#)

[Civil Procedure](#) > ... > [Defenses, Demurrsers & Objections](#) > [Motions to Strike](#) > [Immaterial Matters](#)

[Civil Procedure](#) > ... > [Defenses, Demurrsers & Objections](#) > [Motions to Strike](#) > [Redundant Matters](#)

[Civil Procedure](#) > ... > [Defenses, Demurrsers & Objections](#) > [Motions to Strike](#) > [Scandalous Matters](#)

## [\*\*HN4\*\*](#) [down arrow] **Pleadings, Counterclaims**

[\*Fed. R. Civ. P. 13\(f\)\*](#) is facially limited to what a court deems to be an insufficient defense, or a redundant, immaterial, impertinent or scandalous matter.

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**Judges:** Barbara M. G. Lynn, UNITED STATES DISTRICT JUDGE.

**Opinion by:** Barbara M. G. Lynn

## Opinion

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### **MEMORANDUM OPINION AND ORDER**

Before the Court are: (I) Plaintiff's Motion to Strike portions of the Answer and Counterclaims of Defendant Endoscopic Technologies, Inc. ("Estech"); (II) Estech's Motion for Leave to Amend its Answer and Counterclaims; and (III) Plaintiff's Motion to Strike portions of the [\*2] Answer and Counterclaims of Defendant CHF Technologies, Inc. ("CHF"). Defendants have requested oral argument of these Motions. The Court finds oral argument unnecessary. For the following reasons, the Court DENIES Plaintiff's Motions to Strike, and GRANTS Estech's Motion for Leave to Amend its Answer and Counterclaims.

Plaintiff filed its Motion to Strike Estech's Answer and Counterclaims on March 10, 2005. In that Motion, Plaintiff argues the Answer does not properly plead Estech's assertion that Plaintiff engaged in fraud and inequitable conduct. See [FED. R. CIV. P. 9\(b\)](#) (requiring allegations of fraud to be pled with particularity). In Response to the Motion to Strike, Estech requests leave to amend its Answer and Counterclaims, so it may withdraw its allegations of fraud and inequitable conduct.

**HN1**[] Under [FED. R. CIV. P. 15\(a\)](#), the Court has discretion to grant Estech's request, and it should do so unless the Court uncovers a "substantial reason" for refusing amendment. [Lyn-Lea Travel Corp. v. American Airlines, Inc., 283 F.3d 282, 286 \(5th Cir. 2002\)](#) ([Rule 15\(a\)](#)) "requires the trial [\*3] court to grant leave to amend freely, and the language of this rule evinces a bias in favor of granting leave to amend."). Plaintiff has not asserted any such "substantial reason", and the Court does not find one. Therefore, the Court grants Estech leave to file its Amended Answer and Counterclaims.

Plaintiff, in its Reply, anticipates that the Court will grant Estech's request for leave, and raises new arguments for striking portions of Estech's Amended Answer and Counterclaims. Simultaneously, Plaintiff asserts a Motion to Strike analogous portions of the Answer and Counterclaims filed by CHF Technologies, Inc. ("CHF"). In both filings, Plaintiff argues Defendants have insufficiently pled their affirmative defenses of equitable estoppel, patent misuse, and unclean hands, as well as their counterclaims arising under federal and state antitrust laws.<sup>1</sup>

[\*4] **HN2**[] Under [FED. R. CIV. P. 13\(f\)](#), the Court may strike from a pleading "any insufficient defense or any redundant, immaterial, impertinent or scandalous matter." However, motions to strike are disfavored, and when the contents of a pleading are legally sufficient, but improper for some other reason, a motion to strike should be granted only when the moving party shows that the inclusion of the disputed claims or defenses would cause it prejudice. See [U.S. v. Cushman & Wakefield, Inc., 275 F. Supp.2d 763, 767-68 \(N.D. Tex. 2002\)](#). If the moving party does not show prejudice, the Court should "defer action on the motion and leave the sufficiency of the allegations for determination on the merits." [Id. at 768 n.3](#), citing [Augustus v. Board of Public Instruction of Escambia County, Fla., 306 F.2d 862 \(5th Cir. 1962\)](#).

Plaintiff first argues Defendants' affirmative defenses should be stricken as legally insufficient. Plaintiff asserts that "it is unknown" whether Defendants' counterclaims and affirmative defenses are based on an unstated allegation that Plaintiff has engaged in fraudulent conduct, and if [\*5] they are based on such allegations, they are not pled with particularity, as required by [FED. R. CIV. P. 9\(b\)](#). However, the Court does not find any allegations of fraudulent conduct on the face of CHF's Answer and Estech's Amended Answer. Moreover, Defendants, in their

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<sup>1</sup> It would ordinarily be improper for the Court to consider arguments raised for the first time in a Reply Brief. See [Senior Unsecured Creditors' Comm. of First Republic Bank Corp. v. FDIC, 749 F. Supp. 758, 772 \(N.D. Tex. 1990\)](#). In this case, however, Estech acquiesced to the Court considering Plaintiffs new arguments by joining in Defendants' Response to Plaintiffs Motion to Strike CHF's Answer.

consolidated Response to Plaintiff's Motion to Strike CHF's Answer, admit that neither Defendant is currently alleging fraud as part of their counterclaims or affirmative defenses. Defendants have thus abandoned any allegations of fraudulent conduct that might be in their current pleadings. See [Vela v. City of Houston, 276 F.3d 659, 678 \(5th Cir. 2001\)](#). Therefore, Defendants' affirmative defenses and counterclaims need not be pled in accordance with [FED. R. CIV. P. 9\(b\)](#). See also, [Apani Southwest, Inc. v. Coca-Cola Enterprises, Inc., 300 F.3d 620, 631 \(5th Cir. 2002\)](#) **HN3**[ (antitrust claims are not held to a heightened pleading standard, and the plaintiff need only include a short and plain statement of the claim showing an entitlement to relief).

Alternatively, Plaintiff argues that Defendants' affirmative defenses [\*6] are legally insufficient because they do not satisfy the general pleading requirements of [FED. R. CIV. P. 8](#). It argues the Defendants do not allege any facts in support their affirmative defenses of equitable estoppel, patent misuse, and unclean hands. The Court disagrees. Defendants' Answers, when viewed in their entirety, make clear that Defendants' affirmative defenses rely on factual allegations asserted within their counterclaims, including allegations that: (1) Plaintiff initiated this suit in bad faith with the intention of using it as an "anticompetitive weapon"; (2) Plaintiff misrepresented the scope of its patent in a press release, with the intention of excluding its competitors from the relevant market; and (3) Plaintiff tortiously interfered with Defendants' business relationships. Plaintiff argues it should not be required to "guess as to what facts alleged in the Amended Complaint purportedly support the asserted defenses", and that Defendants should be required to directly reference the factual allegations that pertain to each affirmative defense. The Court finds the link between the above-referenced factual allegations and Defendants' [\*7] affirmative defenses to be reasonably clear. See [FED. R. CIV. P. 8\(f\)](#) (requiring the Court to construe pleadings so as to do "substantial justice"). If Plaintiff requires further detail, it may seek it in discovery.

Plaintiff next argues that several phrases in Defendants' Answers should be stricken because they "create placeholders so that Defendants can assert new causes of action in the future without repleading." For instance, Plaintiff protests that in Defendants' affirmative defenses and counterclaims, Defendants accuse Plaintiff of violating "general principles" of patent law and [antitrust law](#), and Defendants twice use the phrase "among other things" to broaden the scope of the conduct which they allege makes Plaintiff's patent unenforceable. Plaintiff argues the vagueness of these phrases prejudices its preparation of its legal strategies. However, Plaintiff does not cite any authority that portions of an affirmative defense or counterclaim can be stricken on account of imprecision. **HN4**[ [Rule 13\(f\)](#) is facially limited to what the Court deems to be an insufficient defense, or a redundant, immaterial, impertinent or scandalous matter. The [\*8] Court finds the phrases at issue do not render Defendants' affirmative defenses insufficient, and they are not redundant or scandalous. At most, they are vague or surplusage, and are not "so unrelated to plaintiff's claims as to be unworthy of any consideration as a defense." [F.D.I.C. v. Niblo, 821 F. Supp. 441, 449 \(N.D. Tex. 1993\)](#). Again, discovery should be used to obtain further detail.

Finally, Plaintiff argues that portions of Defendants' seventh affirmative defense should be stricken as redundant. Defendants, in their fifth affirmative defense, allege Plaintiff's claims are barred by equitable estoppel and unclean hands. In their sixth affirmative defense, Defendants allege Plaintiff's claims are barred by misuse. Plaintiff argues the seventh affirmative defense, which alleges Plaintiff's patent is unenforceable, is redundant because the purported unenforceability is explicitly predicated on alleged "misuse of the patent . . . and the doctrines of unclean hands and equitable estoppel". However, Plaintiff has not alleged, or produced any evidence that this purported redundancy causes it prejudice. Therefore, the Court denies Plaintiff's Motion to Strike the [\*9] seventh affirmative defense. See [Cushman & Wakefield, 275 F. Supp.2d at 767-68](#).

For these reasons, Plaintiff's Motions to Strike are DENIED, and Estech's Motion for Leave is GRANTED. The Clerk of Court is directed to file a copy of Estech's Amended Answer and Counterclaims.

**SO ORDERED.**

**DATED:** July 11, 2005.

Barbara M. G. Lynn

UNITED STATES DISTRICT JUDGE

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## *In re Enron Corp.*

United States Bankruptcy Court for the Southern District of New York

July 11, 2005, Decided

Chapter 11, Case No. 01 B 16034(AJG), (Confirmed)

**Reporter**

326 B.R. 257 \*; 2005 Bankr. LEXIS 1278 \*\*; 44 Bankr. Ct. Dec. 280

In re: ENRON CORP., et al., Reorganized Debtors.

### **Core Terms**

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filed rate doctrine, rates, anti trust law, energy, electricity, tariff, market-based, cases, regulations, manipulation, wholesale, markets, refunds, federal law claim, file a tariff, interstate, violations, antitrust, courts, crisis

### **LexisNexis® Headnotes**

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Administrative Law > Separation of Powers > Jurisdiction

Business & Corporate Compliance > ... > Industry Practices > Federal Regulations > Antitrust Regulations

Administrative Law > Separation of Powers > Primary Jurisdiction

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Antitrust & Trade Law > Procedural Matters > Jurisdiction > Primary Jurisdiction

Governments > Federal Government > Claims By & Against

#### **HN1 [down arrow] Separation of Powers, Jurisdiction**

The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant. Courts have consistently held that the filed rate doctrine applies to federal antitrust actions relating to rates established by federal agencies.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > Exclusive Jurisdiction

Energy & Utilities Law > ... > US Federal Energy Regulatory Commission > Civil Actions > Jurisdiction

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

## **HN2** Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

Under the filed rate doctrine, once the Federal Energy Regulatory Commission determines that a rate is "just and reasonable," the courts cannot authorize a departure from that rate.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## **HN3** Exemptions & Immunities, Filed Rate Doctrine

While market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

## **HN4** Energy & Utilities Law, Antitrust Issues

The reporting requirements are an integral part of a tariff, with Federal Energy Regulatory Commission's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates.

Administrative Law > Separation of Powers > Legislative Controls > Implicit Delegation of Authority

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Antitrust Issues > General Overview

## **HN5** Legislative Controls, Implicit Delegation of Authority

Implicit in Federal Energy Regulatory Commission (FERC) orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Transportation Law > Carrier Duties & Liabilities > Damages

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > Restraints of Trade

#### **HN6** Common Carrier Duties & Liabilities, Rates & Tariffs

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the United States Supreme Court has stated that injury implies violation of a legal right. The Supreme Court concluded that the legal rights of a shipper as against a carrier in respect to a rate are measured by the published tariff. A rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Antitrust Act. What rates are legal is determined by the Act to Regulate Commerce. Under § 8 of the latter act, the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation.

Contracts Law > Remedies > Equitable Relief > Injunctions

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Administrative Proceedings > Preemption

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Oil, Gas & Mineral Interests > Purchase Contracts > Remedies for Breach

#### **HN7** Equitable Relief, Injunctions

Remedies for breach and non-performance of operating agreements approved by the Federal Energy Regulatory Commission (FERC) in the interstate wholesale electricity market fall within the exclusive domain of FERC.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

#### **HN8** Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make a judgment regarding rates, and until it has done so, no rate other than the one on file may be charged.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Energy & Utilities Law > Regulators > Public Utility Commissions > Ratemaking Procedures

#### **HN9** [blue] Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

The filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that: (1) legislatively appointed regulatory bodies have institutional competence to address rate-making issues; (2) courts lack the competence to set utility rates; and (3) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime.

Antitrust & Trade Law > Procedural Matters > Jurisdiction > Exclusive Jurisdiction

Energy & Utilities Law > Antitrust Issues > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > US Federal Energy Regulatory Commission

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Energy & Utilities Law > Administrative Proceedings > Preemption

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### **HN10** [blue] Jurisdiction, Exclusive Jurisdiction

The Federal Power Act (FPA) provides the Federal Energy Regulatory Commission (FERC) with broad remedial authority to address anti-competitive behavior. Congress through the FPA, made clear that the interstate "transmission" or "sale" of wholesale energy pursuant to a federal tariff, not merely the "rates," falls within FERC's exclusive jurisdiction. [16 U.S.C.S. § 824e](#).

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**Judges:** ARTHUR J. GONZALEZ, United States Bankruptcy Judge.

**Opinion by:** ARTHUR J. GONZALEZ

## **Opinion**

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[\*259] OPINION SUSTAINING DEBTORS' OBJECTION TO PROOFS OF CLAIM NOS. 12172-12174 AND 12252-12257 FILED BY BILL LOCKYER, ATTORNEY GENERAL OF THE STATE OF CALIFORNIA; TO PROOFS OF CLAIM NOS. 12498, 12500, 24685, AND 24687 FILED [\*2] BY CALIFORNIA DEPARTMENT OF WATER RESOURCES; AND TO PROOFS OF CLAIM NOS. 22630-22632 FILED BY SOUTHERN CALIFORNIA EDISON COMPANY REGARDING FEDERAL LAW CLAIMS IN ELECTRICITY MARKET

On October 11, 2002, the Attorney General of the State of California (the "State") filed separate proofs of claim in unliquidated amounts on behalf of the People of the State of California against Enron Corporation ("Enron") and certain of its affiliated entities (collectively, the "Debtors") in the following nine cases: Enron (Claim No. 12173); Enron North America Corp. ("ENA") (Claim No. 12172); Enron Power Marketing, Inc. ("EPMI") (Claim No. 12174); Enron Energy Services, Inc. ("EESI") (Claim No. 12255); Enron Energy Services, LLC (Claim No. 12254); Enron Energy Services Operations, Inc. (Claim No. 12257); Enron Energy Marketing Corp. (Claim No. 12256); and Enron Capital & Trade Resources International Corp. (Claim No. 12253). The Attorney General also filed proofs of claim on behalf of the California Department of Water Resources ("CDWR") in unliquidated amounts against the Debtors in the following cases: Enron (Claim No. 12500); ENA (Claim No. 12498); EPMI (Claim No. 24685); and EESI (Claim No. 24687). [\*3] On March 6, 2003, Southern California Edison Company ("Edison") filed proofs of claim in unliquidated amounts against the Debtors in the following cases: Enron (Claim No. 22630); EESI (Claim No. 22631); and EPMI (Claim No. 22632).

The State, CDWR and Edison (collectively, the "Claimants") allege that the Debtors manipulated energy markets in California and overcharged for energy through unlawful and anti -- competitive acts during the western power crisis of 2000 and 2001. They maintain the alleged manipulation in the electricity market constitutes a violation of the federal antitrust law and regulations, and seek disgorgement, restitution, actual and treble damages together with interest and injunctive relief. On March 10 2005, the Debtors filed objections to the Claimants' federal law claims and argued that the Federal Power Act (the "FPA") preempts the federal laws and the filed rate doctrine precludes consideration of these claims.

The issues before the Court are whether (i) the federal law claims are preempted by the FPA; and (ii) whether such claims are precluded by the filed rate doctrine. The Court finds that because the Federal Energy Regulatory Commission ("FERC") has exclusive [\*4] jurisdiction over interstate sales of wholesale electricity, the filed rate doctrine precludes consideration of such federal law claims. For the reasons set below, the Court will not determine the preemption issue.

### I. BACKGROUND

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the [\*260] "Plan") in these cases. The Plan became effective on November 17, 2004.

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, the California legislature had passed Assembly Bill 1890 <sup>1</sup> (the "Bill") to create two non-governmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. [California v. Dynegy, Inc., 375 F.3d 831, 850 \(9th Cir. 2004\)](#). The central transactions, [\*\*5] wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC found that the Debtors engaged in gaming <sup>2</sup> in the form of inappropriate trading strategies and further engaged in the deliberate submission of false information or the deliberate omission of material information. [Enron Power Mktg., Inc., et al., 106 FERC P 61,024 \(2004\)](#). Both proceedings are ongoing, including the determination of remedies by FERC.

## [\*\*6] II. DISCUSSION

The threshold question regarding the filed rate doctrine before the Court is whether the Court would have to determine a tariff. [HN1](#) The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. [E& J. Gallo Winery v. EnCana Energy Servs., Inc., 2005 U.S. Dist. LEXIS 24240, \\*29, Case No. CV F 03-5412 AWLJO](#). The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority." [Ark. L.A. Gas Co. v. Frank Hall, 453 U.S. 571, 577-78, 69 L. Ed. 2d 856, 101 S. Ct. 2925 \(1981\)](#). The Court also recognizes that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant. [\*\*7] " [City of Cleveland v. FPC, 174 U.S. App. D.C. 1, 525 F.2d 845, 854 \(D.C. Cir. 1976\)](#). Courts have consistently held that the filed rate doctrine applies to federal antitrust actions relating to rates established by federal agencies. [Ark. L.A. Gas 453 U.S. 571, at 580; County of Stanislaus v. Pacific Gas and Elec. Co., 114 F.3d 858, 863 \(9th Cir. 1997\); In re Western States Wholesale Natural Gas Antitrust Litig., 368 F. Supp. 2d 1110, 1114-45 \(D. Nev. 2005\).](#)

The Debtors argue that FERC has exclusive jurisdiction over whether wholesale [\*261] electricity price is "just and reasonable." The Debtors assert that the federal law claims necessarily require the Court to determine whether rates were reasonable or whether the Debtors violated applicable FERC approved tariffs. [HN2](#) Under the filed rate doctrine, once FERC determines that a rate is "just and reasonable," the courts cannot authorize a departure from that rate. The Claimants do not contest such assertion by the Debtors. Instead, the Claimants raise two arguments to support that the filed rate doctrine is not applicable here.

The first argument made by the Claimants is that the filed rate doctrine [\*\*8] is inapplicable because no properly filed rates were on file during the period when the alleged conduct occurred. However, the Claimants relied on the

<sup>1</sup> 1996 Cal. Stat. 854

<sup>2</sup> The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule . . . to the detriment of the efficiency of, and of consumers in, the ISO markets." [Am. Electric Power Service Corp., et al., 103 FERC P 61,346 \(2003\)](#).

following finding in *California v. FERC*, 383 F.3d 1006, 1016 (9th Cir. 2004) to support its position "without the required filings, neither FERC nor any affected party may challenge the rate. Pragmatically, under such circumstances, there is no filed tariff in place at all." *Id.* This argument, however, inappropriately equates the Debtors' alleged violation of the filing requirements with no-filed tariffs. FERC required each seller to file quarterly reports pursuant to FPA § 205(c) [16 U.S.C. § 824d\(c\)](#) on transaction-specific information about its sales and purchases at market-based rates. The court in *Public Util. Dist. No 1 v. IDACORP Inc.*, 379 F.3d 641, 651 (9th Cir. 2004), concluded, [HN3](#)<sup>↑</sup> "while market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine."

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that [HN4](#)<sup>↑</sup> "the reporting requirements are an [\*\*9] integral part of a tariff, with FERC's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [383 F.3d at 1016](#). On August 13, 2002, FERC's Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.<sup>3</sup> Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. [106 FERC P 61,024](#). As noted by FERC,

[HN5](#)<sup>↑</sup> implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market [\*\*10] shares) that reflect a departure from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. [383 F.3d at 1016](#). Without the availability of retroactive refunds, "parties [\*262] aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

The second [\*\*11] argument made by the Claimants is that the filed rate doctrine is not applicable because the issue presented before the Court is distinguishable from those in *Grays Harbor* and *Public Util. Dist. No. 1 v. Dynegy Power Mktg., Inc.*, 384 F.3d 756 (9th Cir. 2004). The plaintiff in *Snohomish* brought an action against a company that engaged in market manipulation during the energy crisis in violation of state antitrust and unfair competition law. The court confirmed that the filed rate doctrine applies because the court could not determine the rates that "would have been achieved in a competitive market." [Id. at 761](#). Similarly, the court in *Grays Harbor* rejected the request from the plaintiff for a determination of the "fair price." [379 F.3d at 645](#). Here, the Claimants argue that they are not asserting a price which should be paid in a competitive market as the benchmark for a calculation of a remedy. Rather, the Claimants maintain that the remedy would be unrelated to the ISO tariff and the Court would not have to determine a non-manipulated rate because FERC has done so. The Claimants argue that it is merely requesting the Court to determine [\*\*12] liability, and thereafter, remand to FERC for a determination of remedies.

The Ninth Circuit in *California v. FERC* examined the substance of the law and remanded to FERC for the determination of remedies. The court there declined to order refunds to a state because the court reasoned it was more appropriate for FERC to consider its remedial options in the first instance. [383 F.3d at 1018](#). The substantive law examined by the court in *California v. FERC* concerned whether retroactive refunds were legally available. *Id.*

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<sup>3</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, as required under their market-based rate authorization. [106 FERC P 61,024](#).

As such, no liability issue was raised and determined by that court. Further, the Court finds that determining the liability or the legal right of the Claimants against the Debtors for violation of the federal **antitrust law** would have to be measured by the tariff.

**HN6** [↑] In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in *Keogh v. Chicago & N. W.R. Y. Co.*, 260 U.S. 156, 67 L. Ed. 183, 43 S. Ct. 47 (1922), stated that "injury implies violation of a legal right." *Id. at 163*. The Supreme Court concluded that "the legal rights of [a] shipper as [\*\*13] against [a] carrier in respect to a rate are measured by the published tariff." *Id. at 163*. Justice Brandeis explained "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce. Under Section 8 of the latter act . . . the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation." *Id. at 162*. Thus, the finding of liability in antitrust laws would be integral to the Court's determination of whether the Debtors are liable due to their violations of the federal **antitrust law** and regulations. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

Moreover, to award monetary relief, the Court would have to determine a "fair price." Thus, the filed rate doctrine bars [\*263] the Court from awarding monetary damages sought by the Claimants. Nonetheless, the Court finds that injunctive [\*\*14] relief would also be unavailable to the Claimants. The Court agrees with the Ninth Circuit's decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine. *384 F.3d at 762*. **HN7** [↑] "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC." *Dynegy*, 375 F.3d at 836.

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. **HN8** [↑] "Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged." 453 U.S. 571, at 580-84. The decisions from the Second Circuit in *Sun City Taxpayers' Association v. Citizens Utilities Co.*, 45 F.3d 58 (2d Cir. 1995) and *Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17 (2d Cir. 1994), provide an additional basis for dismissal of the Claims sought by the Claimants. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which [\*\*15] had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. *Sun City Taxpayers' Ass'n v. Citizens Utils. Co.*, 847 F.Supp.281, 291 (D. Conn. 1994). The Second Circuit in *Wegoland* recognized that **HN9** [↑] the filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. *27 F.3d at 21*.

Therefore, having considered the policy objectives, the Court finds that granting the relief sought to Claimants would frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine [\*\*16] the filed rate doctrine. The Court, therefore, rejects the Claimants' challenge to the application of the filed rate doctrine. Accordingly, the Court finds that the filed rate doctrine bars the relief sought by the Claimants.

The Debtors argue that the **antitrust law** and regulations are preempted by the FPA. However, the Debtors primarily focus on the argument against state **antitrust law** claims. By comparison, the Claimants argue that the federal **antitrust law** and regulations are not preempted by the FPA because courts have referred the federal **antitrust law** claims related to filed tariffs determined by regulatory commissions. In supporting its assertion, the Claimants cite the Supreme Court's decisions in *Otter Tail Power Co. v. United States*, 410 U.S. 366, 35 L. Ed. 2d 359, 93 S. Ct. 1022 (1973), and *California v. Federal Power Commission*, 369 U.S. 482, 8 L. Ed. 2d 54, 82 S. Ct.

901 (1962). In both cases, the Supreme Court found that Congress does not intend to bar the government from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions.

Having reviewed these cases, the Court disagrees with the Claimants' argument and finds them distinguishable from the instant case. **[\*\*17]** In *California v. Federal Power Commission*, a gas company filed a **[\*264]** motion to dismiss the antitrust suit pursuant to the Clayton Act, § 7 as amended 15 U.S.C.A. § 18, or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's assets pursuant to the Natural Gas Act (the "NGA"), § 7(c) as amended 15 U.S.C.A. § 717f(c), before the Power Energy Commission. 369 U.S. at 483. In *Otter Tail Power*, the government brought an action against an electric power company to enjoin violations of the Sherman Act, 15 U.S.C.A. § 2. 410 U.S. at 368. In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws.

However, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC in the instant case. In contrast, the court in *California v. Federal Power Commission* concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the **[\*\*18]** Clayton Act. 369 U.S. at 485. "The Commission's standard, set forth in § 7 of the NGA, will serve the public convenience and necessity.' If existing natural gas companies violate the antitrust laws, the Commission is directed by § 20(a) to transmit such evidence' to the Attorney General." Id. at 486. Similarly, the Court in *Otter Tail Power* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the Sherman Act. 410 U.S. at 375. In *Otter Tail Power*, the FPA does not authorize the FPC to order a power company to wheel electric power over its transmission lines; accordingly, enforcing the Sherman Act against anticompetitive and monopolistic practices on interconnections by the district court did not conflict with authority of the FPC. Id. at 376-77. Moreover, the Supreme Court in Carnation Co. v. Pacific Westbound Conference, 383 U.S. 213, 383 U.S. 932, 15 L. Ed. 2d 709, 86 S. Ct. 781 (1966) declined to grant antitrust immunity to a shipping company because "the provisions of the Shipping Act, 46 U.S.C.A. § 801, can not reasonably be construed as **[\*\*19]** an implied repeal of antitrust regulation of the shipping industry's rate-making activities." Id. at 217. The Shipping Act does not give the Federal Maritime Commission (the "FMC") any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. Square D Co. v. Niagara Frontier Tariff Bureau, 476 U.S. 409, 422, 90 L. Ed. 2d 413, 106 S. Ct. 1922 (1986).

Here, **HN10**↑ the FPA provides FERC with broad remedial authority to address anti-competitive behavior. Congress through the FPA, made clear that the interstate "transmission" or "sale" of wholesale energy pursuant to a federal tariff, not merely the "rates," falls within FERC's exclusive jurisdiction. Federal Power Act, 16 U.S.C. § 824e. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally **[\*\*20]** order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." 103 FERC P 61,346. Further, "implicit in Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority." **[\*265]** 106 FERC P 61,024. Under the preemption analysis, allowing the federal antitrust law claims in the wholesale interstate electricity market would appear to encroach upon the authority Congress entrusted exclusively to FERC. Thus, the cited cases by the Claimants are not controlling in the instant case. Because the parties do not substantially further develop their argument on preemption, and as a result of the Court's determination regarding the filed rate doctrine, the Court will not determine the preemption issue.

### III. CONCLUSION

For the foregoing reasons, the Court concludes that the federal antitrust law claims sought by the Claimants concerning electricity market manipulation are precluded by the filed rate doctrine. Therefore, [\*\*21] the Court sustains the Debtors' objection to those claims filed by the Claimants.

Counsel for the Debtors is directed to settle an order consistent with this Court's Opinion.

Dated: New York, New York

July 11, 2005

**Arthur J. Gonzalez**

UNITED STATES BANKRUPTCY JUDGE

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## Jackson, Tenn. Hosp. Co. v. W. Tenn. Healthcare, Inc.

United States Court of Appeals for the Sixth Circuit

March 10, 2005, Argued ; July 11, 2005, Decided ; July 11, 2005, Filed

File Name: 05a0292p.06:

No. 04-5387

### **Reporter**

414 F.3d 608 \*; 2005 U.S. App. LEXIS 13799 \*\*; 2005 FED App. 0292P (6th Cir.) \*\*\*; 2005-1 Trade Cas. (CCH) P74,857

JACKSON, TENNESSEE HOSPITAL COMPANY, LLC, Plaintiff-Appellant, v. WEST TENNESSEE HEALTHCARE, INC., JACKSON-MADISON COUNTY GENERAL HOSPITAL DISTRICT, and BLUECROSS BLUESHIELD OF TENNESSEE, INC., Defendants-Appellees.

**Subsequent History:** Rehearing denied by, Rehearing, en banc, denied by [Jackson, Tenn. Hosp. Co., LLC v. W. Tenn. Healthcare, Inc., 2005 U.S. App. LEXIS 22937 \(6th Cir., Oct. 19, 2005\)](#)

**Prior History:** [\[\\*1\]](#) Appeal from the United States District Court for the Western District of Tennessee at Jackson. No. 03-01166. James D. Todd, Chief District Judge.

[Jackson v. W. Tenn. Healthcare, Inc., 2004 U.S. Dist. LEXIS 4571 \(W.D. Tenn., Feb. 27, 2004\)](#)

## **Core Terms**

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powers, hospital authority, anticompetitive, state action doctrine, anti trust law, authorization, antitrust liability, healthcare, antitrust

## **LexisNexis® Headnotes**

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Governments > State & Territorial Governments > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Healthcare Law > Business Administration & Organization > Covenants not to Compete > General Overview

### [\*\*HN1\*\*](#) **[] Governments, State & Territorial Governments**

The state action doctrine protects subdivisions of a state government from antitrust liability when there is a clearly expressed state policy authorizing anticompetitive acts.

414 F.3d 608, \*608L<sup>2005</sup> U.S. App. LEXIS 13799, \*\*1L<sup>2005</sup> FED App. 0292P (6th Cir.), \*\*\*Cir.)

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## **HN2** [down] Standards of Review, De Novo Review

The United States Court of Appeals for the Sixth Circuit reviews the district court's grant of a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss de novo.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

## **HN3** [down] Exemptions & Immunities, Noerr-Pennington Doctrine

On a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion, all factual allegations are taken to be true, and the court draws all reasonable inferences in favor of the plaintiff. A [Rule 12\(b\)\(6\)](#) motion should only be granted if it appears beyond doubt that the plaintiffs can prove no set of facts in support of their claim which would entitle them to relief.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

Governments > State & Territorial Governments > Claims By & Against

Public Contracts Law > Contract Provisions > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Governments > Federal Government > Claims By & Against

Governments > Local Governments > Claims By & Against

## **HN4** [down] Exemptions & Immunities, Parker State Action Doctrine

Under the so-called "state action doctrine," it is well established that [antitrust law](#) does not apply to states acting as sovereigns. Principles of federalism and state sovereignty provide blanket protection for states, but political subdivisions of the states are not automatically immune from antitrust liability. Political subdivisions of states are beyond the reach of the antitrust laws only when they act pursuant to a clearly expressed state policy. The state legislature need not explicitly authorize anticompetitive conduct, as long as anticompetitive effect would logically result from the authority granted by the state. Applying these principles, the United States Court of Appeals for the Sixth Circuit holds that Michigan law implicitly authorizes anticompetitive conduct when it empowers prisons to grant public contracts for the provision of telephone services. The issues of implied authority and "foreseeable" anticompetitive effects are recurring ones in the case law, but, obviously, are relevant only when there is no express authorization for anticompetitive conduct.

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

## **HN5** [down] Antitrust Actions, Facilities

See [Tenn. Code Ann. § 7-57-502\(c\).](#)

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

## **HN6** [+] **Robinson-Patman Act, Claims**

The phrase "competitive consequences" is commonly used in antitrust and competition law. The United States Court of Appeals for the Sixth Circuit is not aware of any other context in which this phrase is commonly used. The antitrust laws protect competition and are concerned with competitive consequences; thus, permission to act "regardless of competitive consequences" is most sensibly read as an authorization to act without regard for the antitrust laws for purposes of the state action doctrine.

**Counsel:** ARGUED: Harry M. Reasoner, VINSON & ELKINS, Houston, Texas, for Appellant.

David Marx, Jr., McDERMOTT, WILL & EMERY, Chicago, Illinois, Kevin D. McDonald, JONES DAY, Washington, D.C., for Appellees.

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**Judges:** Before: BOGGS, Chief Judge; and COOK and BRIGHT, Circuit Judges. \*

**Opinion by:** BOGGS

## **Opinion**

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**[\*609] [\*\*2]** BOGGS, Chief Judge. Although this is an antitrust case, it turns on the proper interpretation of a Tennessee statute. The plaintiff alleges that the Jackson-Madison County General Hospital District (the "Hospital District"), which is a political subdivision of the state of Tennessee, and the other defendants have committed antitrust violations. The district court dismissed the suit, finding that the state action doctrine protects the defendants from antitrust liability. **HN1** [+] The state action doctrine protects subdivisions of a state government from antitrust liability when there is a clearly expressed state policy authorizing anticompetitive acts. [Town of Hallie v. City of Eau Claire, 471 U.S. 34, 40, 85 L. Ed. 2d 24, 105 S. Ct. 1713 \(1985\)](#). The issue, then, is whether Tennessee law authorizes the Hospital District to engage in anticompetitive actions. We conclude that it does, and therefore affirm.

I

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\* The Honorable Myron H. Bright, United States Circuit Judge for the Eighth Circuit, sitting by designation.

The Hospital District is a "private act" [\*610] hospital authority" [\*3] <sup>1</sup> ("hospital authority) created by the Tennessee Legislature.<sup>2</sup> The Hospital District was created in 1949 to own, manage, and operate hospital facilities. The original rationale for the Hospital District was to serve indigent and low-income patients, although it has since expanded into a full-service healthcare operation. The Hospital District is a political subdivisions of the state of Tennessee.

The Tennessee Legislature recently reformed the statutory framework governing hospital authorities. In Acts passed in 1995 and 1996 ("the Acts"), the legislature gave hospital authorities [\*4] far greater freedom of operation.<sup>3</sup> The Acts granted hospital authorities broad powers, including the ability to: [\*\*\*3]

- . Borrow, issue bonds, or take on other forms of debt
- . Own and operate subsidiaries such as outpatient departments, clinics, etc.
- . Participate as a shareholder or partner in any lawful form of business
- . Set fees to be charged to patients
- . Hire and fire all employees, as well as set the terms of compensation
- . Set rules governing physicians and other providers operating within the authority
- . Set criteria for admission of patients
- . Sue and be sued
- . Invest any excess funds
- . Acquire or improve any real property

Tenn. Code Ann. § 7-57-502(a)-(b). And, just in case anything was missed, the list ends with a catch-all provision: the hospital authority shall "have and exercise *all powers necessary or convenient to effect any or all the purposes* for which a private act metropolitan hospital authority is organized." Tenn. Code Ann. § 7-57-502(b)(10) (emphasis added). In short, after the Acts, a hospital authority has broad powers to do almost [\*5] anything plausibly related to its mission of providing healthcare services.

[\*\*6] At the heart of this dispute is the final provision in the "Powers Granted" section:

In the exercise of its powers, including, without limitation, the powers in this section, any other provision of this part and of any other law a private act metropolitan hospital authority may acquire, [\*611] manage, lease, purchase, sell, contract for or otherwise participate solely or with others in the ownership or operation of hospital, medical or health program properties and facilities and properties, facilities, and programs supporting or relating thereto of any kind and nature whatsoever and in any form of ownership whenever the board of

<sup>1</sup> Tenn. Code Ann. § 7-57-602:

For the purpose of this part, "private act hospital authority" is any hospital owned or operated by one (1) or more local governments or any hospital, hospital authority or hospital district created or authorized by a private act of the general assembly.

<sup>2</sup> Another named defendant, West Tennessee Healthcare, is a wholly-owned subsidiary of the Hospital District.

<sup>3</sup> The stated purpose of the Acts was:

The general assembly hereby finds that the demand for hospital, medical and health care services is rapidly changing as is the way and manner in which such services are purchased and delivered; that the market for hospital and health care services is becoming increasingly competitive; and that the hospital and other health care providers need flexibility to be able to respond to changing conditions by having the power to develop efficient and cost-effective methods to provide for hospital, medical and health care needs. The general assembly also finds that the increasing competition and changing conditions force hospitals and other health care providers to develop market strategies and strategic plans to effectively compete. The general assembly further finds that public hospitals in metropolitan areas are presently at a competitive disadvantage, and that significant investments in the public assets of private act metropolitan hospital authorities could be jeopardized by inability to compete with private hospitals because of legal constraints upon the scope of their operations and limitations upon the power granted to public hospitals under existing law.

Tenn. Code Ann. § 7-57-501(b).

trustees in its discretion shall determine it is consistent with the purposes and policies of this part or any private act applicable to it, and *may exercise such powers regardless of the competitive consequences thereof.*

Tenn. Code Ann. § 7-57-502(c) (emphasis added). The meaning of the last two lines is in dispute.

On July 6, 2003, Jackson, Tennessee Hospital Company ("THC"), which operates a private hospital in Jackson-Madison County, filed suit in federal district court against the Hospital District, West Tennessee [\*\*7] Healthcare, and BlueCross BlueShield ("BlueCross") alleging violations of state and federal antitrust laws. THC alleges that the defendants engaged in various anticompetitive acts to monopolize the local healthcare market. Among the acts alleged were exclusive contracting with doctors and insurance companies, acquiring real estate around the private hospital to block expansion, charging prices that were too low or too high, acquiring other healthcare providers, and bundling its services. On February 27, 2004, the district court granted the defendants' Fed. R. Civ. P. 12(b)(6) motion to dismiss on the grounds that the state action doctrine barred antitrust liability.

[\*\*\*4] II

HN2 [↑] We review the district court's grant of a Fed. R. Civ. P. 12(b)(6) motion to dismiss *de novo*. AirTrans, Inc. v. Mead, 389 F.3d 594, 597 (6th Cir. 2004). HN3 [↑] All factual allegations are taken to be true, and we draw all reasonable inferences in favor of the plaintiff. *Ibid.* "A Rule 12(b)(6) motion should only be granted if it appears beyond doubt that the plaintiffs can prove no set of facts in support [\*\*8] of [their] claim which would entitle [them] to relief." *Ibid.* (quotation marks omitted).

The defendants argue that the state action doctrine bars liability on any of the antitrust claims raised by the plaintiff. BlueCross also argues, in the alternative, that it is protected from antitrust liability by the *Noerr-Pennington* doctrine. Because we conclude that the state action doctrine bars antitrust liability for all the defendants, including BlueCross, we do not reach this alternative argument.

## A

HN4 [↑] Under the so-called "state action doctrine," it is well established that antitrust law does not apply to states acting as sovereigns.<sup>4</sup> [\*\*10] Parker v. Brown, 317 U.S. 341, 87 L. Ed. 315, 63 S. Ct. 307 (1943). The Supreme Court has determined that principles of federalism and state sovereignty provide blanket protection for states, but political subdivisions of the states are not automatically immune from antitrust liability. City of Columbia v. Omni Outdoor Advertising, Inc., 499 U.S. 365, 370, 113 L. Ed. 2d 382, 111 S. Ct. 1344 (1991). Political subdivisions of states are beyond the reach of the antitrust laws only when they act pursuant to a "clearly expressed" [\*612] state policy. [\*\*9] " <sup>5</sup> Town of Hallie v. City of Eau Claire, 471 U.S. 34, 40, 85 L. Ed. 2d 24, 105 S. Ct. 1713 (1985). The state legislature need not explicitly authorize anticompetitive conduct, as long as anticompetitive effect would logically result from the authority granted by the state. Columbia, 499 U.S. at 372-73 ("it is enough, we have held, if suppression of competition is the 'foreseeable result' of what the statute authorizes"); Hallie, 471 U.S. at 41-42. Applying these principles, we recently held that Michigan law implicitly authorized anticompetitive conduct when it empowered prisons to grant public contracts for the provision of telephone services. Michigan Paytel Joint Venture v. City of Detroit, 287 F.3d 527 (6th Cir. 2002). The issues of implied authority and "foreseeable" anticompetitive effects are recurring ones in the case law, but, obviously, are relevant only when there is no express authorization for anticompetitive conduct.

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<sup>4</sup> The parties do not contest that the state action doctrine, if applicable, protects both the government entity - the hospital authority - and the private parties with whom it contracts - BlueCross. This is sensible, as the protection would be worthless in many cases if a plaintiff could simply sue private parties that contracted with the government.

<sup>5</sup> After *Hallie*, the only requirement for sovereign immunity for political subdivisions is a clearly articulated state policy. Id. at 46. At one time, there was also an "active state supervision requirement," but in *Hallie* the Supreme Court noted that this was primarily evidentiary and discarded this part of the test unless "regulation by a private party" is involved. *Ibid.*

**B**

Defendants hold the trump in this case: plain statutory language. The crux is the following sentence, which appears after the long list of specific and general powers granted by the Acts: [HN5](#) "[hospital authorities] may exercise such powers *regardless of the competitive consequences* thereof." [Tenn. Code Ann. § 7-57-502\(c\)](#) (emphasis added). [HN6](#) The phrase "competitive consequences" is commonly used in antitrust and competition law. See, e.g., [Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.](#), 509 U.S. 209, 251, 125 L. Ed. 2d 168, 113 S. Ct. 2578 (1993) ("[an element] of the violation is the competitive consequences of predatory conduct."); [Texaco Inc. v. Hasbrouck](#), 496 U.S. 543, 557, 110 L. Ed. 2d 492, 110 S. Ct. 2535 (1990) [\*\*11] ("[the [Robinson-Patman Act](#)] plainly reveals a concern with competitive consequences [\*\*\*5] . . . ."). We are not aware of any other context in which this phrase is commonly used, and the plaintiff has not provided any authority suggesting an alternative meaning. The antitrust laws protect competition and are concerned with competitive consequences; thus, permission to act "regardless of competitive consequences" is most sensibly read as an authorization to act without regard for the antitrust laws.

Although no Tennessee court has addressed this issue,<sup>6</sup> [\[\\*12\]](#) the Tennessee Attorney [\[\\*613\]](#) General reached the same conclusion in a 1995 Opinion. Around the time the 1995 Act was passed, the Tennessee Attorney General opined that "the exercise of the increased powers and privileges set forth in the Act qualifies for state action immunity from the federal [antitrust law](#)."<sup>7</sup> In his analysis, the Attorney General concluded that the Act "contemplates and expresses an intent to displace competition." In this litigation, the current Attorney General takes a different view, but we think the original position, issued without the prospect of litigation, expresses the better view of the language.

The primary response of plaintiff and its *amici* is to argue that the Tennessee legislature intended to promote competition in the healthcare market, and favors competition generally. See [Tenn. Const. Art. I, § 22](#) ("That perpetuities and monopolies are contrary to the genius of a free State, and shall not be allowed."); [Tenn. Code Ann. § 68-11-1625\(b\)](#) ("It is the policy of the state of Tennessee that: . . . The state's health care resources should be developed to address the needs of Tennesseans while encouraging competitive markets, economic efficiencies and the continued development of the state's health care industry"). The plaintiff also notes that the statement of purpose for the 1995 Act expresses a desire to enable public hospitals to compete with private hospitals. See [\[\\*13\]](#) *supra* n.3. In the face of a clear public policy favoring competition, plaintiff argues, the "regardless of" phrase cannot be interpreted to grant antitrust immunity. Defendants and their *amici* dispute whether Tennessee is in fact uniformly hostile to monopoly, and advance the view that, although the legislature was somewhat concerned with competitive effects, it was determined to advance the interests of hospital authorities even at the expense of competition.

<sup>6</sup> Both parties rely upon the opinion of the Tennessee Supreme Court in [City of Cookeville ex rel. Cookeville Regional Med. Ctr. v. Humphrey](#), 126 S.W.3d 897 (Tenn. 2004). The Cookeville court faced the issue of whether the statute authorized a hospital authority to close its imaging department and then enter into an exclusive contract with a private provider. The Tennessee Supreme Court stated:

[Tennessee statute] provides in pertinent part that a metropolitan hospital authority, in the exercise of its powers, may "contract for or otherwise participate solely or with others" in furtherance of the hospital's operation. Additionally, the plain language of this statute permits private act metropolitan hospitals to enter into a contract "*regardless of the competitive consequences [of the contract]*." Therefore, it is clear that private act metropolitan hospital authorities are statutorily authorized to execute exclusive provider contracts.

[\*Id. at 902\*](#) (citations omitted)(emphasis in original). Cookeville does confirm that the "regardless of" clause applies to all the powers granted in [§ 7-57-502\(a\)-\(b\)](#) and that those powers are quite broad. However, Cookeville did not involve an antitrust claim, and is therefore of limited usefulness in determining whether the "regardless of" phrase was meant to create an exemption from the antitrust laws.

<sup>7</sup> This opinion was actually issued six days before the 1995 Act was passed (the then-draft language was the same as the enacted version). It therefore serves a dual role as legislative history and as the opinion of the Tennessee Attorney General at the time the bill was passed.

More importantly, the plaintiff's argument is at odds with a basic principle of interpretation: the specific trumps the general. It is no doubt true that Tennessee prefers competition as a general matter, but this is true of the federal government and probably every other state as well. Despite this, our various federal and state governments regularly carve out exceptions. Indeed, the appropriate level of competition in health care is a policy question that is regularly revisited at both [\*\*\*6] the federal and state levels. Here, the language of the statute clearly indicates the desire to create an exception to the antitrust laws, and the general preference for competition is therefore superseded.

When the plaintiff [\*\*14] turns to the "regardless of" language, it is only to dismiss it as a "tag-line phrase." It argues that the language only authorizes hospital authorities to enter into contracts and exercise their powers even if such actions disadvantage competing hospitals and doctors: the "regardless of" phrase "thus recognized that the 'competitive consequences' of making public hospitals more competitive was that individual competitors might be harmed. This type of harm, however is the essence of competition." Pl.'s Br. at 24-25. This reading, however, would render the language hortatory. Obviously, any government entity's actions will have an effect, sometimes negative, on private [\*614] actors. Moreover, the "regardless of" clause appears in a section of the Act granting powers to hospital authorities, and this would be an odd place for the legislature to add a "tag-line" phrase that simply notes a possible consequence of its enactment. Finally, the plaintiff does not cite any examples or authority for this limited reading of the phrase "competitive consequences," and it is contrary to the common legal usage.

In sum, we read the legislative language and surrounding circumstances as demonstrating that [\*\*15] the Tennessee legislature invested public hospital corporations with very broad powers to ensure their continued viability; authorized them to exercise many powers, such as contracting for services and acquiring property, that could easily lead to anti-competitive consequences; and then specifically stated that such activities could be undertaken without regard to the effects of such activity on competition. This constitutes the authorization necessary to invoke the state action doctrine.

### III

For the foregoing reasons, we AFFIRM the judgment of the district court.

## Sanderson v. Culligan Int'l Co.

United States Court of Appeals for the Seventh Circuit

April 1, 2005, Argued ; July 11, 2005, Decided

No. 04-3253

**Reporter**

415 F.3d 620 \*; 2005 U.S. App. LEXIS 13969 \*\*; 2005-1 Trade Cas. (CCH) P74,853

CHARLES H. SANDERSON, Plaintiff-Appellant, v. CULLIGAN INTERNATIONAL COMPANY, Defendant-Appellee.

**Prior History:** [\*\*1] Appeal from the United States District Court for the Southern District of Indiana, Indianapolis Division. No. IP 00-0459-C H/K. David F. Hamilton, Judge.

[Sanderson v. Ind. Soft Water Servs., 2004 U.S. Dist. LEXIS 15671 \(S.D. Ind., July 23, 2004\)](#)

## **Core Terms**

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magnetic, anti trust law, producers, products, rivals, distributors, advertising, antitrust

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

### **HN1[ Motions to Dismiss, Failure to State Claim]**

On a motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#), even highly unlikely propositions must be taken as given.

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Evidence > Inferences & Presumptions > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

### **HN2[ Summary Judgment, Opposing Materials]**

The party opposing summary judgment receives the benefit of all reasonable inferences.

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### **HN3[ Pleadings, Rule Application & Interpretation]**

Complaints need not allege facts or legal theories.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

Antitrust & Trade Law > Consumer Protection > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### [\*\*HN4\*\*](#) [] **Private Actions, Remedies**

The antitrust laws protect consumers, not producers. They favor competition of all kinds, whether or not some other producer thinks the competition "fair." Much competition is unfair, or at least ungentlemanly; it is designed to take sales away from one's rivals. There is no obligation to be kindly or cooperative toward other producers. Some laws, including the Lanham Act, condemn particular tactics deemed unfair; the Sherman Act is not among these laws.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Preliminary Considerations > Venue > General Overview

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### [\*\*HN5\*\*](#) [] **Antitrust & Trade Law, Sherman Act**

**Antitrust law** condemns practices that drive up prices by curtailing output. False statements about a rival's goods do not curtail output in either the short or the long run. They just set the stage for competition in a different venue: the advertising market.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Consumer Protection > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

#### [\*\*HN6\*\*](#) [] **Private Actions, Remedies**

Warfare among suppliers and their different products is competition. **Antitrust law** does not compel a competitor to praise your product or sponsor the work of others. To require cooperation or friendliness among rivals is to undercut the intellectual foundations of **antitrust law**. Unless one group of suppliers diminishes another's ability to peddle its wares (technically, reduces rivals' elasticity of supply), there is not even the beginning of an antitrust case, no reason to investigate further to determine whether the restraint is reasonable.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

415 F.3d 620, \*620L<sup>2005 U.S. App. LEXIS 13969, \*\*1</sup>

Torts > Intentional Torts > Defamation > General Overview

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN7** Private Actions, Remedies

What producers say about each others' goods in an effort to sway consumers is competition in action. Some other law may require judicial intervention in order to increase the portion of truth in advertising; the Sherman Act does not. Commercial speech is not actionable under the antitrust laws. There can be no restraint of trade without a restraint.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Governments > Legislation > Statute of Limitations > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Trademark Law > ... > Unfair Competition > Federal Unfair Competition Law > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

## **HN8** False Designation of Origin, Elements of False Designation of Origin

Section 43(a) of the Lanham Act, [15 U.S.C.S. § 1125\(a\)\(1\)\(B\)](#), covers only commercial advertising or promotion.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

## **HN9** False Designation of Origin, Elements of False Designation of Origin

Section 43(a) of the Lanham Act, [15 U.S.C.S. § 1125\(a\)](#), addresses promotional material disseminated to anonymous recipients. This leaves to state law the evaluation of oral statements and brochures at trade shows.

Business & Corporate Law > ... > Duties & Liabilities > Unlawful Acts of Agents > General Overview

Business & Corporate Law > ... > Authority to Act > Actual Authority > General Overview

## **HN10** [blue icon] Duties & Liabilities, Unlawful Acts of Agents

Unsuccessful efforts at prevention of the commission of business torts do not imply agency or an assumption of liability.

Antitrust & Trade Law > Sherman Act > Penalties

Civil Procedure > Appeals > Frivolous Appeals

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > Jurisdiction

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

## **HN11** [blue icon] Sherman Act, Penalties

Neither the Sherman Act nor the Lanham Act is designed to throw into federal courts all disputes about the efficacy of competing products.

**Counsel:** For CHARLES H. SANDERSON, SR. - Plaintiff - Appellant; Robert Hendren, Indianapolis, IN.

For CULLIGAN INTERNATIONAL COMPANY - Defendant - Appellee; Gayle A. Reindl, Indianapolis, IN.

**Judges:** Before EASTERBROOK, MANION, and ROVNER, Circuit Judges.

**Opinion by:** EASTERBROOK

## Opinion

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[\*621] EASTERBROOK, *Circuit Judge*. Magnatech Corporation sells "magnetic water conditioners." Its sole stockholder brought this suit in his own name, contending that Culligan, a manufacturer of chemical and filtration systems of water purification, violated the federal antitrust and trademark laws by asserting that magnetic systems don't work. The suit might have been dismissed immediately, for Magnatech rather than Sanderson is the appropriate plaintiff. See, e.g., [\*In re Industrial Gas Antitrust Litigation\*, 681 F.2d 514, 519-20 \(7th Cir. 1982\)](#); [\*Mid-State Fertilizer Co. v. Exchange National Bank\*, 877 F.2d 1333, 1335-36 \(7th Cir. 1989\)](#). Sanderson does not claim to be injured as a consumer; his injury (a reduction in the value of his stock) is derivative of Magnatech's. Cf. [\*Illinois Brick Co. v. Illinois\*, 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 \(1977\)](#). But Culligan did not catch this, and it is not the sort of jurisdictional [\*622] problem that a court must notice on its own. See [\*Associated General Contractors v. California State Council of Carpenters\*, 459 U.S. 519, 535, 74 L. Ed. 2d 723, 103 S. Ct. 897](#) & n.31, [\*459 U.S. 519, 74 L. Ed. 2d 723, 103 S. Ct. 897 \(1983\)\*](#); [\*Hammes v. AAMCO Transmissions, Inc.\*, 33 F.3d 774, 778 \(7th Cir. 1994\)](#).

Instead Culligan defended on the merits, prevailing in a series of decisions. First the district court dismissed the antitrust allegations for failure to state a claim on which relief may be granted. [\*2001 U.S. Dist. LEXIS 8309 \(S.D. Ind. May 29, 2001\)\*](#). Then it granted summary judgment on the [\*Lanham Act\*](#) claim to the extent that any of the statements preceded the period of limitations. [\*622] [\*2002 U.S. Dist. LEXIS 19212 \(S.D. Ind. Sept. 20, 2002\)\*](#).

Finally it terminated the case, again by summary judgment, because none of the remaining statements fits the Lanham Act's definition of advertising. [2004 U.S. Dist. LEXIS 15671 \(S.D. Ind. July 23, 2004\)](#).

Because the case ended without a trial, we must assume that magnetic systems can reduce lime scale deposits in pipes, the only benefit that Magnatech and its Superior Manufacturing Division claim for their products. (They do not contend [\*\*3] that magnetic treatment removes minerals or biological agents from water.) [HN1](#)[<sup>↑</sup>] On a motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#), even highly unlikely propositions must be taken as given. See, e.g., [Miles v. Augusta City Council, 710 F.2d 1542 \(11th Cir. 1983\)](#) (assuming, as the complaint alleged, that cats can talk). And [HN2](#)[<sup>↑</sup>] the party opposing summary judgment receives the benefit of all reasonable inferences. Some evidence in the record suggests that magnetic systems can reduce lime buildup, though whether this evidence, which has not been published in a scientific journal, meets the standard of [Fed. R. Evid. 702](#) is doubtful.

Lime deposits in plumbing are calcium carbonate (CaCO<sub>3</sub>), which is non-magnetic. Sanderson's lawyer could not explain why magnets affect nonferrous materials, and the unpublished study to which his brief refers at length does not do so either. This study finds that non-chemical devices can reduce the hardness of calcium carbonate build-up in industrial air-conditioning systems, but *only* when the water moves faster than 2.3 meters per second -- and even so the paper [\*\*4] offers Sanderson little support, for it lumps together a variety of non-chemical approaches and does not report separately on the sort of magnetic systems that Magnatech sells. See Young I. Cho, *Efficiency of physical water treatments in controlling calcium scale accumulation in recirculating open cooling water system*, American Society of Heating, Refrigerating & Air-Conditioning Engineers Research Project 1155-TRP (May 29, 2002). Positive reports about magnetic water treatment are not replicable; this plus the lack of a physical explanation for any effects are hallmarks of junk science. For a review of the literature see John S. Baker & Simon J. Judd, *Magnetic amelioration of scale formation*, 30 Water Research 247 (1996). Nonetheless, we shall indulge the assumption that adverse statements about Magnatech's products are calumnies.

Sanderson's antitrust claim rests on § 1 of the Sherman Act, [15 U.S.C. § 1](#), and fails at the threshold because Sanderson does not contend (in the complaint or anywhere else) that Culligan has conspired with other producers to set price or output, or that it possesses the sort of market power that would lead to condemnation [\*\*5] under the Rule of Reason. See [National Collegiate Athletic Ass'n v. Board of Regents, 468 U.S. 85, 82 L. Ed. 2d 70, 104 S. Ct. 2948 \(1984\)](#). Recast under § 2 it would fare no better, because Sanderson does not contend that Culligan possesses monopoly power or that bad-mouthing Magnatech's products creates a dangerous probability of monopolization. See [Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 122 L. Ed. 2d 247, 113 S. Ct. 884 \(1993\)](#).

The problem is not that the pleading is short, as [Fed. R. Civ. P. 8](#) contemplates. [HN3](#)[<sup>↑</sup>] Complaints need not allege facts or legal theories. See [Swierkiewicz v. Sorema N.A., 534 U.S. 506, 152 L. Ed. 2d 1, 122 S. Ct. 992 \(2002\)](#); [Bartholet v. Reishauer A.G. \(Zurich\), 953 F.2d 1073 \(7th Cir. 1992\)](#). Sanderson's problem, rather, is that his complaint and other papers demonstrate [\*623] that the claim rests on a belief that the antitrust laws forbid all "unfair" business tactics, without regard to the likelihood that the adversary will achieve and retain a monopoly at consumers' expense. Not at all. [HN4](#)[<sup>↑</sup>] The antitrust laws protect consumers, not producers. They favor competition of all kinds, whether or not some other [\*\*6] producer thinks the competition "fair." Much competition is unfair, or at least ungentlemanly; it is designed to take sales away from one's rivals. There is no obligation to be kindly or cooperative toward other producers. See, e.g., [Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 157 L. Ed. 2d 823, 124 S. Ct. 872 \(2004\)](#). Some laws, including the Lanham Act, condemn particular tactics deemed "unfair"; the Sherman Act is not among these laws.

[HN5](#)[<sup>↑</sup>] **Antitrust law** condemns practices that drive up prices by curtailing output. See, e.g., [NCAA, 468 U.S. at 103-07](#); [Broadcast Music, Inc. v. CBS, Inc., 441 U.S. 1, 19-20, 60 L. Ed. 2d 1, 99 S. Ct. 1551 \(1979\)](#). False statements about a rival's goods do not curtail output in either the short or the long run. They just set the stage for competition in a different venue: the advertising market. [Schachar v. American Academy of Ophthalmology, Inc., 870 F.2d 397 \(7th Cir. 1989\)](#), another antitrust case based on a supposed commercial falsehood, makes this point forcefully. We observed:

**HN6** Warfare among suppliers and their different products *is* competition. **Antitrust law** does not [\*\*7] compel your competitor to praise your product or sponsor your work. To require cooperation or friendliness among rivals is to undercut the intellectual foundations of **antitrust law**. Unless one group of suppliers diminishes another's ability to peddle its wares (technically, reduces rivals' elasticity of supply), there is not even the beginning of an antitrust case, no reason to investigate further to determine whether the restraint is "reasonable".

[870 F.2d at 399](#) (citations omitted; emphasis in original). Magnatech remains free to sell to all who can be persuaded that magnets reduce lime buildup; Culligan faces competition from dozens of other producers that use different, though more conventional, technologies to filter, purify, or reduce mineral content in water.

Sanderson contends that *Schachar* is incompatible with [American Society of Mechanical Engineers, Inc. v. Hydrolevel Corp., 456 U.S. 556, 72 L. Ed. 2d 330, 102 S. Ct. 1935 \(1982\)](#), but *Schachar* pointed out that *Hydrolevel* depended on something missing there (and here): an enforcement mechanism. Some producers persuaded an engineering society to write standards in such a way that only their [\*\*8] products were acceptable. Because many governmental bodies made compliance with the standards mandatory (they were incorporated into building codes and other legal mandates), this curtailed the available supply (rivals' products having been knocked out) and could have enabled the conspirators to raise prices.

Nothing comparable is alleged here. Although magnetic devices were at one time banned from some trade shows (supposedly at Culligan's behest), that ban was lifted in the mid-1990s and is outside the period of limitations, see [15 U.S.C. § 15\(b\)](#) -- and anyway is some distance from the legal restraint that led to *Hydrolevel*. Sanderson also maintains that Culligan persuaded the Water Quality Association, a trade group, to withhold its "Gold Seal" from magnetic systems. No unit of government incorporates this "Gold Seal" into any legal requirement; it is just a marketing device. Anheuser-Busch might as well claim that by selling a beer called "Blue Ribbon" Pabst has violated the antitrust laws, unless [\*624] Pabst is willing to bestow the same "Blue Ribbon" on Budweiser. **HN7** What producers say about each others' goods in an effort to sway consumers is competition in [\*\*9] action. Some other law may require judicial intervention in order to increase the portion of truth in advertising; the Sherman Act does not. Commercial speech is not actionable under the antitrust laws. As we put it in *Schachar*: "There can be no restraint of trade without a restraint." [870 F.2d at 397](#). See also [Santana Products, Inc. v. Bobrick Washroom Equipment, Inc., 401 F.3d 123, 133 \(3d Cir. 2005\)](#).

As for Sanderson's claim under § 43(a) of the Lanham Act, [15 U.S.C. § 1125\(a\)\(1\)\(B\)](#), the district court held that it founders on the federal statute's limited scope. **HN8** [Section 43\(a\)](#) covers only "commercial advertising or promotion". The district court concluded that Sanderson had just three examples of supposedly false statements within the period of limitations, and that all three were person-to-person communications at trade shows. We held in [First Health Group Corp. v. BCE Emergis Corp., 269 F.3d 800, 804 \(7th Cir. 2001\)](#), that **HN9** [§ 43\(a\)](#) addresses "promotional material disseminated to anonymous recipients". This leaves to state law the evaluation of oral statements and brochures at trade shows. Sanderson does [\*\*10] not contend that the statements of which he complains are "commercial advertising or promotion" as *First Health Group* understood that phrase. Indeed, he does not mention that opinion, though it was the mainstay of the district court's decision.

For that matter, Sanderson does not contend that any of the statements within the period of limitations was uttered by Culligan. He attributes these oral statements and handouts to its franchisees or distributors and says that Culligan must be vicariously liable because it insists that they live up to high standards of business ethics. That Culligan tries to prevent its distributors from committing business torts, and reserves the right to stop selling to anyone who does, hardly makes any of the distributors its agent for the purpose of defaming rivals. **HN10** Unsuccessful efforts at prevention do not imply agency or an assumption of liability. If Culligan told its distributors to avoid reckless driving and to obey all state laws, this would not make it vicariously liable for their auto accidents or oblige it to pay if a distributor shot his neighbor's dog for barking late at night.

Sanderson pursued some claims under state law, which for [\*\*11] reasons we have given is the only applicable body of legal norms. The district judge granted summary judgment to Culligan on all of the state-law claims, and Sanderson does not contest this decision on appeal. His arguments have been limited to the frivolous claims under

federal law. He should be thankful that Culligan has not filed a cross-appeal from the district court's order denying its motion for sanctions. [HN11](#)[] Neither the Sherman Act nor the Lanham Act is designed to throw into federal courts all disputes about the efficacy of competing products. Whether magnetic water conditioners work is a question about science, not law, and scientific disputes must be resolved by scientific means.

AFFIRMED

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## Teamsters Local Union No. 117 v. Sysco Food Servs. of Seattle, Inc.

United States District Court for the Western District of Washington

July 11, 2005, Decided ; July 11, 2005, Filed

Case No. C05-0113L

### **Reporter**

2005 U.S. Dist. LEXIS 43789 \*; 2005 WL 1643890

TEAMSTERS LOCAL UNION NO. 117, Plaintiff, v. SYSCO FOOD SERVICES OF SEATTLE, INC., et al., Defendants.

### **Core Terms**

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tortious interference, single employer, district court, collective bargaining agreement, motion to dismiss, contractual relationship, primary jurisdiction, employees, alter ego, arbitration, conspiracy, preempted, bargaining unit, non-signatory, Defendants', contractual, proceedings, parties, defer, unfair labor practice, alter ego theory, state law claim, federal court, breached

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For Sysco Food Services of Seattle Inc, a Delaware corporation, Defendant: John M Payne, LEAD ATTORNEY, Paul Milton Nordsletten, LEAD ATTORNEY, DAVIS GRIMM PAYNE & MARRA, SEATTLE, WA; Richard J. Omata, LEAD ATTORNEY, Tracy M Miller, KARR TUTTLE CAMPBELL, SEATTLE, WA.

For Sysco Food Services Inc, a Delaware corporation, Defendant: Richard J. Omata, LEAD ATTORNEY, Tracy M Miller, KARR TUTTLE CAMPBELL, SEATTLE, WA.

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**Judges:** Robert S. Lasnik, United States District Judge.

**Opinion by:** Robert S. Lasnik

### **Opinion**

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#### **ORDER REGARDING MOTIONS TO DISMISS OR TO STAY**

This matter comes before the Court on motions [\*2] filed by defendants Sysco Food Services of Seattle, Inc. ("Sysco Seattle"), Sysco Food Services, Inc. ("Sysco Post Falls"), and Sysco Corporation ("Sysco Corp.") (Dkt. # s 20, 23, & 26). Defendants move to dismiss or, in the alternative, to stay the federal court proceedings pending resolution of issues before the National Labor Relations Board ("NLRB"). For the reasons set forth below, defendants' motions are granted in part and denied in part.

## I. BACKGROUND

Sysco Post Falls and Sysco Seattle are both wholly owned subsidiaries of Sysco Corporation. Sysco Seattle operates a facility in Kent, Washington from which it distributes groceries to retail stores throughout the Pacific Northwest, including a number of locations in ORDER REGARDING MOTIONS TO DISMISS OR TO STAY eastern Washington and northern Idaho. Sysco Seattle's employees, including its drivers, are represented by Teamsters Local Union No. 117 ("Local 117").

Local 117 and Sysco Seattle have entered into a collective bargaining agreement (the "CBA") which covers the terms and conditions of employment at Sysco Seattle. Section 20.01 of the CBA, the parties agree that the work of the bargaining unit may only be performed [\*3] by employees that belong to that bargaining unit. Section 20.02 prohibits Sysco Seattle from unilaterally changing employment terms or sub-contracting work without first engaging in good-faith bargaining with Local 117 about the effects of the changes.

The dispute between the parties arose when Sysco Post Falls announced that it intended to open a new facility in Post Falls, Idaho that would supply groceries to eastern Washington and northern Idaho. When it learned of the new facility, Sysco Seattle decided to stop operating in eastern Washington and northern Idaho. Sysco Seattle informed Local 117 that 33 drivers would be laid off as a result of its decision, but also informed Local 117 that Sysco Post Falls would likely require the services of the drivers.

In late 2004, Teamsters Local 690, based in Spokane, Washington, was designated by the Joint Council of Teamsters No. 28 as the bargaining representative with exclusive jurisdiction for all drivers and warehouse employees hired at the new Post Falls facility. In January, 2005, Local 690 and Sysco Post Falls began negotiations on labor agreements to cover employees at the Post Falls facility. The Post Falls agreement, however, [\*4] has yet to be implemented.

When Local 117 learned that Sysco Seattle intended to cease operating in eastern Washington and northern Idaho, it asked Sysco Seattle to consult with it under § 20.02 of the CBA about the effects of the decision. The "effects bargaining" was scheduled for February 10, 2005. Several weeks before that meeting, however, Local 117 learned that Sysco Post Falls either had begun hiring, or intended to start hiring, employees for the new Post Falls facility. Local 117 filed this lawsuit on January 21, 2005.

After the lawsuit was filed, defendants filed several complaints with the NLRB. For instance, Sysco Post Falls filed unfair labor practice charges against Local 690, the International Brotherhood of Teamsters, and Local 117. These claims assert that Local 690 has refused to accept the negotiated labor agreement with Sysco Post Falls and that the International Brotherhood of Teamsters and Local 117 have violated [§ 8\(b\)\(1\)\(A\)](#) of the National Labor Relations Act. In addition, Sysco Seattle and Sysco Post Falls have both filed unit clarification petitions with the NLRB.

In its amended complaint, Local 117 seeks injunctive relief under § 301 of the Labor Management [\*5] Relations Act (the "LMRA"), [29 U.S.C. § 185\(a\)](#), to prevent breaches of §§ 20.01 and 20.02 of the CBA. Local 117 has asserted these claims against Sysco Seattle and against Sysco Post Falls and Sysco Corp. as "alter egos" of Sysco Seattle. In the event that Sysco Post Falls and Sysco Corp. are not alter egos of Sysco Seattle, Local 117 has filed alternative claims of tortious interference with contractual relationship (under both Washington law and federal common law), and civil conspiracy against Sysco Post Falls and Sysco Seattle. Finally, Local 117 seeks a declaratory judgment regarding its rights under the CBA.

In their respective motions to dismiss, defendants argue that the [§ 301](#) claims should be dismissed or stayed because (1) this Court lacks subject matter jurisdiction over the claims, and (2) the NLRB, not this Court, has primary jurisdiction over issues arising under [§ 301 of the LMRA](#). Sysco Post Falls and Sysco Corp. argue that the tort-based claims should be dismissed because they are preempted by both [§ 301 of the LMRA](#) and the [Garmon](#) presumption doctrine, see [San Diego Bldg. Trades Council v. Garmon](#), 359 U.S. 236, 244, 79 S. Ct. 773, 3 L. Ed. 2d

[775 \(1959\)](#). [\*6] In addition, Sysco Post Falls and Sysco Corp. argue that the Civil Conspiracy claim fails as a matter of law.<sup>1</sup>

## II. DISCUSSION

### A. Standard of Review.

In the context of a defendant's motion to dismiss for lack of jurisdiction under [Fed. R. Civ. P. 12\(b\)\(1\)](#), this Court must "take the allegations in the plaintiff's complaint as true." [Wolfe v. Strankman](#), 392 F.3d 358, 362 (9th Cir. 2004). In the context of a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss for failure to state a claim upon which relief may be granted, a court must (1) construe the complaint in the light most favorable to the plaintiff, (2) [\*7] accept all well-pleaded factual allegations as true, and (3) determine whether the plaintiff can prove any set of facts to support a claim that would merit relief. See [Cahill v. Liberty Mut. Ins. Co.](#), 80 F.3d 336, 337-38 (9th Cir. 1996).

### B. Claims under § 301 of the LMRA.

#### 1. Subject Matter Jurisdiction and Failure to Submit Claims to Arbitration.

Sysco Seattle argues that this Court lacks subject matter jurisdiction over the [§ 301](#) claims asserted against it because Local 117 never submitted the underlying breach of contract claims to arbitration. There is no dispute that the underlying question of whether Sysco Seattle has breached, or is about to breach, §§ 20.01 or 20.02 of the CBA are subject to the CBA's arbitration provision. The underlying contractual dispute, however, is not before the Court. Instead, Plaintiff's [§ 301](#) causes of action seek a "reverse Boys Markets" injunction. See [Boys Markets, Inc. v. Retail Clerks Union, Local 770](#), 398 U.S. 235, 254, 90 S. Ct. 1583, 26 L. Ed. 2d 199 (1970); see also [Newspaper & Periodical Drivers' & Helpers' Union, Local 921 v. San Francisco Newspaper Agency](#), 89 F.3d 629, 632 (9th Cir. 1996). [\*8] A "reverse Boys Markets" case is one in which "an employer makes changes in areas which are subject to the grievance arbitration procedure, and the union seeks to enjoin the employer from making the changes until the grievance is resolved through arbitration." [San Francisco Newspaper Agency](#), 89 F.3d at 632. Since the purpose of Plaintiff's [§ 301](#) claims is not to determine the parties' obligation under the CBA, but to preserve the status quo pending arbitration, Plaintiff is not required to submit the [§ 301](#) claims to arbitration.

#### 2. Dismissal or Stay in Deference to NLRB's Primary Jurisdiction.

[Section 301 of the LMRA](#) gives this Court subject matter jurisdiction over cases involving the violation of private labor agreements. See [29 U.S.C. § 185\(a\)](#); [SEIU v. St. Vincent Medical Center](#), 344 F.3d 977, 983 (9th Cir. 2003). This Court's jurisdiction, however, is concurrent with the NLRB's, and it is well-settled that "federal courts 'must tread lightly' in areas of the NLRB's primary jurisdiction and must defer to the NLRB 'when on close examination, [section 301](#) cases fall within the NLRB's primary jurisdiction.'" [\*9] [Id.](#) (quoting [United Ass'n of Journeymen & Apprentices of Plumbing & Pipefitting Indus., Local 342 v. Valley Engineers](#), 975 F.2d 611, 613-14 (9th Cir. 1992)). In determining whether to defer to the NLRB, the Court asks "whether the major issues to be decided . . . can be characterized as primarily representational or primarily contractual." [Pace v. Honolulu Disp. Serv., Inc.](#), 227 F.3d 1150, 1157 (9th Cir. 2000) (quoting [Valley Engineers](#), 975 F.2d at 614). Issues that are primarily representational should be decided by the NLRB while this Court should retain jurisdiction over issues that are primarily contractual.

Whether the issues in this dispute are primarily representational or primarily contractual turns on whether Local 117 has brought a "single employer" claim or an "alter ego" claim against defendants. In [UA Local 343 United Ass'n of Journeymen & Apprentices of Plumbing and Pipefitting Indus. of U.S. and Canada, AFL-CIO v. Nor-Cal Plumbing, Inc.](#), the Ninth Circuit noted that "the requirements of [the alter ego and single employer] theories overlap substantially. [\*10] Under both theories, the district court must . . . determine whether the two firms are a single

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<sup>1</sup> Defendants also argued that this Court lacks diversity jurisdiction over the state law claims and should not exercise pendent jurisdiction over those claims. Since, as discussed below, this Court has determined that the state law claims are preempted by the LMRA, these arguments need not be addressed.

employer be measuring the degree of common ownership, management, operations, and labor relations." [48 F.3d 1465, 1470 \(9th Cir. 1994\)](#), cert. denied, 516 U.S. 912, 116 S. Ct. 297, 133 L. Ed. 2d 203 (1995).

Once the single employer determination has been made, however, the two theories have different requirements. The single employer theory requires a showing that employees of the two firms constitute a single bargaining unit. Since the NLRB "has primary jurisdiction to determine whether the employees of both the union and non-union firms constitute an appropriate bargaining unit," a district court must defer to the NLRB when a single employer theory is raised. [Id. at 1470](#). The alter ego theory, on the other hand, does not require a showing that a single bargaining unit exists. Instead, the alter ego theory requires a plaintiff to prove, and the district court to find, that one of the firms "was being used in a sham effort to avoid collective bargaining obligations rather than for the pursuit of legitimate business objectives untainted by union animus." [Id.](#) (internal quotations [\*11] and citations omitted). As the Ninth Circuit has made clear,

The single employer and alter ego doctrines function differently. . . . To impose a labor agreement on a nonsignatory company under the single employer doctrine, the employees of both companies must be shown to constitute a single bargaining unit. Such a showing is not required under the alter ego doctrine. It focuses on whether there is an attempt to avoid the obligations of a collective bargaining agreement through a sham transaction or a technical change in operation.

[Carpenters' Local Union No. 1478 v. Stevens, 743 F.2d 1271, 1276-77 \(9th Cir. 1984\)](#) (footnotes omitted), cert. denied, 471 U.S. 1015, 105 S. Ct. 2018, 85 L. Ed. 2d 300 (1985). If the plaintiff prevails on both steps of the alter ego theory, the court can hold that a bargaining agreement covered both Sysco Seattle and Sysco Post Falls without deferring to the NLRB's primary jurisdiction. See [Nor-Cal Plumbing, 48 F.3d at 1470](#) (citing [Northwest Admrs., Inc. v. Con Iverson Trucking, Inc., 749 F.2d 1338, 1340 \(9th Cir. 1984\)](#)).

Here, it is clear that the issues before this Court do not fall under the NLRB's [\*12] primary jurisdiction. To begin, Local 117 has abandoned any claims based on a single employer theory (see Dkt. # 33, Opp. to Sysco Food Services' Mot. to Dismiss at p. 8) and chosen to proceed under an alter ego theory.<sup>2</sup> [\*13] What is more, in dismissing the unit clarification claims filed by Sysco Seattle and Sysco Post Falls, the NLRB held that "Local 117 has alleged a work dispute claim, rather than a representational claim. . . . Local 117's allegation that [Sysco Post Falls] is an alter ego of [Sysco Seattle] is a necessary component of its contractual claim . . ." <sup>3</sup> Dkt. # 65, Ex. 1, NLRB Regional Director's Decision and Order Dismissing Petitions at p. 4. Based on the holding in [Nor-Cal Plumbing](#), Local 117's abandonment of any single employer claim, and the conclusions of the NLRB's Regional Director, this Court finds that Local 117's claims are "primarily contractual" and are "properly in federal court rather than before the NLRB." [Pace, 227 F.3d at 1157](#).

### 3. Stay in Deference to NLRB's Concurrent Jurisdiction.

Defendants argue that even if the claims are not within the primary jurisdiction of the NLRB, the Court should exercise its discretion and stay this case in favor of the NLRB's concurrent jurisdiction. In cases such as this where a district court and the NLRB share concurrent jurisdiction, the district court may exercise its discretion and stay its own proceedings pending resolution of the NLRB dispute. See [Northern California Dist. Council of Hod Carriers, Bldg. and Const. Laborers, AFL-CIO v Opinski, 673 F.2d 1074, 1075 \(9th Cir. 1982\)](#). In determining whether to stay proceedings, a district court should consider, among other things, whether a decision in the case before it and a decision before the NLRB present more than a potential conflict and whether an eventual NLRB decision will have

<sup>2</sup>The fact that Local 117 has not raised a single employer claim distinguishes this case from [Valley Engineers](#). In [Valley Engineers](#), the Ninth Circuit recognized that "a single employer finding must be supplemented by a unit clarification before the terms of a collective bargaining agreement can be imposed on an nonsigning entity." [975 F.2d at 614](#). Since only the NLRB can conduct the unit clarification inquiry, the Court held that where a party asserts claims under both a single employer theory and an alter ego theory, the district court must defer to the NLRB on both issues. [Id.](#) Here, since no single employer claim has been raised, the NLRB's primary jurisdiction has not been triggered.

<sup>3</sup>Sysco Seattle and Sysco Post Falls have appealed this finding.

issue preclusive effect. See [Central Valley Typographical Union No. 46 v. McClatchy Newspapers, 762 F.2d 741, 749 \(9th Cir. 1985\)](#).

Certainly, [\*14] the unit clarification claims will not present a conflict with the issues to be decided by this Court. See [Carpenters Local Union No. 1846 of United Broth. of Carpenters and Joiners of America, AFL-CIO v. Pratt-Farnsworth, Inc., 690 F.2d 489, 517 \(5th Cir. 1982\)](#) ("Obviously, the Board will not make an alter ego finding in a unit clarification proceeding, since the alter ego theory does not raise a unit determination issue"), cert. denied, 464 U.S. 932, 104 S. Ct. 335, 78 L. Ed. 2d 305 (1983). Defendants, however, note that Sysco Post Falls has another set of claims before the NLRB. These claims assert that Local 117 and the International Brotherhood of Teamsters have committed unfair labor practices by interfering with Sysco Post Falls' efforts to enter into an agreement with Local 690. There is some potential that the unfair labor practices claims will address some of the issues raised before this Court. For instance, defendants have presented letters from the NLRB indicating that the NLRB "must make a determination on the single employer/alter ego question in order to decide these cases." See Dkt. # s 61, Ex. 2 & 62, Ex. 2.

Despite this potential conflict, a stay is not [\*15] appropriate. See [Intern'l Broth. of Elec. Workers, Local 532 v. Brink Constr. Co., 825 F.2d 207, 213 \(9th Cir. 1987\)](#) ("While the potential for conflict exists between the court's decision and the NLRB's ultimate decision, this alone does not compel a stay"). To begin, "[t]he presence of the NLRB does not place all issues of a case within the NLRB's primary jurisdiction." [SEIU v. St. Vincent Med. Ctr., 344 F.3d at 985](#). This is especially true where, as here, there is no question that the unfair labor practices claims before the NLRB "differ from the issue before the district court." See [Sheet Metal Workers Intern. Ass'n, Local No. 162 v. Jason Mfg., Inc., 900 F.2d 1392, 1401 \(9th Cir. 1990\)](#). The NLRB claims assert that Local 690, Local 117, and the International Brotherhood of Teamsters have interfered with Sysco Post Falls employees' rights to enter into a collective bargaining agreement. This suit, on the other hand, regards the applicability of a reverse [Boys Markets](#) injunction under the CBA. In addition, although the NLRB has requested information regarding whether the defendants are a single entity or alter egos, it is [\*16] far from certain that resolving the alter ego dispute is necessary to resolve the unfair labor practices claim. See [Durkin v. Shea & Gould, 92 F.3d 1510, 1516 \(9th Cir. 1996\)](#) (issue preclusion occurs where same issue is "actually and necessarily decided" in prior case).

Finally, the Court notes that the unfair labor practices claims were filed by Sysco Post Falls after Local 117 initiated this suit. A similar situation occurred in [Brink Constr.](#), where "the defendant in the [LMRA § 301](#) suit filed unfair labor practice charges after the filing of the suit." [Brink Constr., 825 F.2d at 214](#) (emphasis in original). As in [Brink Constr.](#), allowing a stay here "would frustrate the congressional intent to have the district courts resolve labor-management contract disputes," and "turn on its head the general federal court practice of avoiding conflicts of jurisdiction by the court in the subsequently filed proceeding staying its proceeding pending the outcome of the initial suit." [Id.](#) Under the circumstances, entering a stay until the NLRB claims have been resolved would not be appropriate.

## C. Claims under Washington Law. [\*17]

### 1. Civil Conspiracy and CPA Claims.

Local 117's civil conspiracy claim is based on the premise that defendants violated Section 1 of the Sherman Antitrust Act, [15 U.S.C. § 1](#), and the Washington Consumer Protection Act ("CPA"), [RCW 19.86.030](#), by creating a horizontal division of territory.

These claims fail as a matter of law. Sysco Post Falls and Sysco Seattle are wholly owned subsidiaries of Sysco Corporation. "[T]he coordinated activity of a parent and its wholly owned subsidiary must be viewed as a single enterprise for purposes of § 1 of the Sherman Act." [Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 771, 104 S. Ct. 2731, 81 L. Ed. 2d 628 \(1984\)](#). The state law conspiracy claim must fail because the defendants "cannot form a 'combination or conspiracy' for purposes of [Section 1](#)." [Boulware v. State of Nev., Dept. of Human Resources, 960 F.2d 793, 797 \(9th Cir. 1992\)](#).

Local 117's CPA claim fails for similar reasons. The CPA was drafted to "complement the body of federal law governing restraints of trade, unfair competition and unfair, deceptive, and fraudulent acts or practices. . . ." [RCW 19.86.920](#) [\*18]. "When the Legislature enacted the CPA, it anticipated our courts would be guided by the interpretation given by the federal courts to the corresponding federal statutes." [Ballo v. James S. Black Co., 39 Wn. App. 21, 25-26, 692 P.2d 182 \(1984\)](#). Washington courts, of course, are not bound to follow federal [antitrust law](#), but any departures from federal law "must be for a reason rooted in our own statutes or case law. . . ." [Blewett v. Abbot Laboratories, 86 Wn. App. 782, 788, 938 P.2d 842 \(1997\)](#), rev. denied, 133 Wn.2d 1029, 950 P.2d 475 (1998). This Court has not found, and Local 117 has not identified, any statutes or case law that would suggest departing from the [Copperweld](#) holding.

## **2. State Law Claim of Tortious Interference With Contractual Relationships.**

Defendants argue that the state law claims of tortious interference with contractual relationships against Sysco Post Falls and Sysco Corp. are preempted by [§ 301 of the LMRA](#). [Section 301](#) preempts state law claims "if resolution of the claim hinges on the court's interpretation of a CBA." [Lingle v. Norge Div. of Magic Chef, Inc., 486 U.S. 399, 413, 108 S. Ct. 1877, 100 L. Ed. 2d 410 \(1988\)](#). State law claims that are "independent" [\*19] of the CBA or do not turn on any provision of the CBA, however, are not preempted See [Lingle, 486 U.S. at 407](#); see also [Livadas v. Bradshaw, 512 U.S. 107, 114 S. Ct. 2068, 129 L. Ed. 2d 93 \(1994\)](#) ("the bare fact that a collective-bargaining agreement will be consulted in the course of state-law litigation plainly does not require the claim to be extinguished").

There is little doubt that the state tortious interference with contractual relationship claim is preempted by the NLRA. The Ninth Circuit "has generally found claims for interference with contractual relations and prospective economic advantage preempted by [section 301](#)." [Milne Employees Ass'n v. Sun Carriers, 960 F.2d 1401, 1412 \(9th Cir. 1992\)](#) (citations omitted), cert. denied, 508 U.S. 959, 113 S. Ct. 2927, 124 L. Ed. 2d 678 (1993). Such a finding is appropriate here. At its core, this claim requires the Court to determine whether the parties have breached the terms of the CBA.<sup>4</sup> The state tortious interference claim will not just require a consultation of the CBA, but will require this Court to determine what duties the parties owed to one another under the CBA and whether those duties were breached. [Section 301](#) [\*20] preemption applies to just such circumstances. See [Milne, 960 F.2d 1401, 1412 \(9th Cir. 1992\)](#) (preemption of tortious interference claim brought under California law<sup>5</sup> because the claim "will require interpretation of provisions in the collective bargaining agreements").<sup>6</sup>

## **[\*21] D. Federal Claim for Tortious Interference with Contractual Relationships.**

In its opposition to the Motion to Dismiss, Local 117 asserts that it brought tortious interference with contractual relations claims under both state and federal law. It argues that if the state law claim is preempted, then the federal law claim based on [§ 301\(a\) of the LMRA](#) and federal common law would still survive. Section 301(a), [29 U.S.C. § 185\(a\)](#), provides:

Suits for violation of contracts between an employer and a labor organization representing employees in an industry affecting commerce as defined in this chapter, or between any such labor organizations, may be

<sup>4</sup> To prove tortious interference with contractual relationships, a plaintiff must show "(1) the existence of a valid contractual relationship or business expectancy; (2) that defendants had knowledge of that relationship; (3) an intentional interference inducing or causing a breach or termination of the relationship or expectancy; (4) that defendants interfered for an improper purpose or used improper means; and (5) resultant damage." [Leingang v. Pierce County Med. Bureau, Inc., 131 Wn.2d 133, 157, 930 P.2d 288 \(1997\)](#).

<sup>5</sup> California's tortious interference with contractual relations claim is substantively identical to Washington's. Compare, [Leingang, 131 Wn.2d at 157](#) with [Pacific Gas & Elec. Co. v. Bear Stearns & Co., 50 Cal. 3d 1118, 1126, 270 Cal. Rptr. 1, 791 P.2d 587 \(1990\)](#).

<sup>6</sup> Because the tortious interference claim is preempted by [§ 301](#), this Court need not determine whether it would also be preempted under the [Garmon](#) preemption doctrine.

brought in any district court of the United States having jurisdiction of the parties, without respect to the amount in controversy or without regard to the citizenship of the parties.

The Federal Circuits that have addressed the question have split on whether [§ 301](#) confers jurisdiction to hear claims against non-signatories to a collective bargaining agreement for tortious interference with that agreement. See [Int'l Union, United Mine Workers of America v. Covenant Coal Corp., 977 F.2d 895, 897 \(1992\)](#) [\*22] (identifying split in Circuits).

Although [International Union](#) identified the Ninth Circuit as one of the Courts that allows for tortious interference claims under [§ 301](#), see [id.](#), the Ninth Circuit has, in fact, yet to explicitly rule on the issue. In [Painting and Decorating Contractors Ass'n of Sacramento v. Painters and Decorators Joint Comm. of the East Bay Counties, 707 F.2d 1067, 1071 \(9th Cir. 1983\)](#), the Ninth Circuit held that a non-signatory to a collective bargaining agreement is a proper party to a suit brought under [§ 301](#). In [Painting and Decorating](#), however, the non-signatory defendant was inextricably intertwined with the collective bargaining agreement that plaintiff claimed had been breached. Indeed, the non-signatory defendant was an association created by the collective bargaining agreement and responsible for administering and enforcing that agreement. See [id. at 1069](#). [Painting and Decorating](#) did not hold that [§ 301](#) permits a plaintiff to bring a tort claim against a non-signatory to a collective bargaining agreement. See [Wynn v. National Broadcasting Co., 234 F. Supp. 2d 1067, 1120 \(C.D. Cal. 2002\)](#) [\*23] (discussing [Painting and Decorating](#)). Although the Ninth Circuit has indicated that a district court may fashion [§ 301](#) remedies in a manner consistent with traditional tort remedies, see [Rozay's Transfer v. Local Freight Drivers, Local 208, 850 F.2d 1321 \(9th Cir. 1988\)](#), it has not held that a party may bring a tort action under [§ 301](#).

In [Wynn](#), the district court for the Central District of California, had an opportunity to address this issue. See [234 F. Supp. 2d at 1119-1121](#). After carefully analyzing the Ninth Circuit case law as well as precedent from other Circuits, the [Wynn](#) court held that [§ 301](#) did not allow for a tortious interference claim. See [id.](#) The court in [Wynn](#) cited with approval the Seventh Circuit's conclusion that "'[section 301](#) creates a right of action only for breach of a collective bargaining agreement; it is not a tort statute.'" [Id. at 1120](#) (citing [Kimbro v. Pepsico, Inc., 215 F.3d 723, 726-27 \(7th Cir. 2000\)](#)). This Court agrees with the holdings in [Wynn](#) and [Kimbro](#). Although [§ 301](#) should be read broadly, it provides jurisdiction only for breach of contract [\*24] claims. Absent a clear ruling from the Ninth Circuit holding otherwise, this Court will not extend [§ 301](#) to allow federal common law tortious interference claims.

### III. CONCLUSION

For the foregoing reasons, defendants' motions to dismiss or, in the alternative, to stay proceedings (Dkt. # s 20, 23, & 26) are GRANTED IN PART AND DENIED IN PART. Defendants' motions to dismiss the [§ 301](#) claims premised on a breach of §§ 20.01 and 20.02 of the CBA are DENIED. Defendants' motions to dismiss the state law tortious interference with contractual relations and conspiracy claims are GRANTED. Defendants' motions to dismiss the tortious interference of contractual relations claims arising under federal common law are GRANTED. Finally, defendants' requests that this Court stay proceedings pending the conclusion of NLRB proceedings are DENIED.

DATED this 11th day of July, 2005

Robert S. Lasnik

United States District Judge



## Schor v. Abbott Labs.

United States District Court for the Northern District of Illinois, Eastern Division

July 12, 2005, Decided ; July 12, 2005, Filed

No. 05 C 1592

### **Reporter**

378 F. Supp. 2d 850 \*; 2005 U.S. Dist. LEXIS 14261 \*\*; 2005-2 Trade Cas. (CCH) P74,927

GARY SCHOR, a Florida resident, on behalf and all others similarly situated, Plaintiff, v. ABBOTT LABORATORIES, an Illinois corporation, Defendant.

**Disposition:** The court granted the manufacturer's motion to dismiss.

## **Core Terms**

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patent, monopoly, boosted, Sherman Act, instant case, patentee, patent holder, anti trust law, collateral estoppel, leveraging, antitrust, motion to dismiss, antitrust liability, invention, monopoly power, patent law, manufactured, antitrust violation, anticompetitive, holder's, cases, drugs, relevant market, defense motion, final judgment, competitors, estoppel, alleges, license, denial of a motion

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

### **HN1[] Estoppel, Collateral Estoppel**

In ruling on a motion to dismiss for failure to state a claim, a court accepts the allegations of the complaint as true and views the facts in the light most favorable to the plaintiff. A complaint should not be dismissed for failure to state a claim unless there is no doubt that the plaintiff cannot prove a set of facts that would entitle her to relief based on her claim.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

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Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **[HN2](#)[] Estoppel, Collateral Estoppel**

Collateral estoppel, or issue preclusion, bars the litigation in a subsequent action of an issue that has been decided in a prior action. The United States Court of Appeals for the Seventh Circuit has held that the party invoking collateral estoppel has the burden of proving four elements: (1) that the issue sought to be precluded is identical to the issue raised in the prior action; (2) that the issue is actually litigated; (3) that determination of the issue is essential to the final judgment; and (4) that the party against whom estoppel is invoked is fully represented in the prior action. The party asserting estoppel has the burden of establishing which issues are actually determined in his favor in a prior action.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

Civil Procedure > Judgments > Relief From Judgments > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > Collateral Order Doctrine

## **[HN3](#)[] Estoppel, Collateral Estoppel**

A motion to dismiss is typically not a final judgment for the purposes of collateral estoppel, the United States Court of Appeals for the Seventh Circuit has held that there are instances in which a motion to dismiss ruling may have preclusive effect.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **[HN4](#)[] Estoppel, Collateral Estoppel**

To determine whether a decision is "final" for collateral estoppel purposes, courts are instructed to consider whether: (1) the decision is not "avowedly tentative"; (2) the hearing is adequate and the parties are fully heard; (3) the court has supported its decision with a reasoned opinion; and (4) the decision is appealable or has been appealed. The ultimate question, then, is whether the prior adjudication is determined to be sufficiently firm to be accorded conclusive effect.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > Regulated Practices > Monopolies & Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

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Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Sherman Act > Scope > General Overview

Antitrust & Trade Law > Sherman Act > Scope > Monopolization Offenses

## **HN5** Monopolies & Monopolization, Actual Monopolization

See [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > Regulated Practices > Monopolies & Monopolization > General Overview

Patent Law > General Overview

## **HN6** Regulated Practices, Monopolies & Monopolization

One consequence of the overlap between the patent and antitrust statutes and case law is that there is no easy delinement between a patent holder's permissible exercise of its rights under patent law, which grants a government-sanctioned monopoly and expressly allows the patentee to engage in exclusionary conduct, and anticompetitive behavior that violates **antitrust law**, which proscribes exclusionary conduct when coupled with monopoly power.

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Elements

Antitrust & Trade Law > Sherman Act > General Overview

## **HN7** Sherman Act, Claims

To establish a [§ 2](#) Sherman Act, [15 U.S.C.S. § 2](#), violation based on monopoly leveraging, a plaintiff must prove that the monopolist: (1) possesses monopoly power in the primary relevant market; (2) gains or attempts to gain a monopoly power in a second relevant market; and (3) willfully acquires the monopoly power by some exclusionary conduct and not through efficiency and innovation.

Antitrust & Trade Law > Sherman Act > General Overview

## **HN8** Antitrust & Trade Law, Sherman Act

To state a claim for a Sherman Act, [15 U.S.C.S. § 2](#), violation, a plaintiff must allege conduct that hurts competition in the relevant market.

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Licenses

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Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

Antitrust & Trade Law > Sherman Act > General Overview

### **HN9** [] **Ownership & Transfer of Rights, Licenses**

A patent holder does not violate the Sherman Act, [15 U.S.C.S. § 2](#), by refusing to license or sell a patented item in a second market, even when the patented product is necessary to the second market.

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > Fraud

Governments > Legislation > Statutory Remedies & Rights

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Assignments

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Patent Law > Ownership > General Overview

Trademark Law > Conveyances > General Overview

### **HN10** [] **Bad Faith, Fraud & Nonuse, Fraud**

Absent illegal tying, fraud in the Patent and Trademark Office, or sham litigation, a patentee may enforce its statutory rights "free from liability under the [antitrust law](#)." A patent holder's right to exclude extends to any relevant market that involves the use, manufacture or sale of the invention.

Copyright Law > ... > Civil Infringement Actions > Jurisdiction > General Overview

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > State Court Review

Patent Law > Infringement Actions > Exclusive Rights > General Overview

### **HN11** [] **Civil Infringement Actions, Jurisdiction**

The United States Supreme Court has significantly curtailed the Federal Circuit's jurisdiction over antitrust claims. [28 U.S.C.S. § 1338](#), the congressional grant of jurisdiction to the Federal Circuit, requires that a plaintiff's complaint "creates the cause of action."

Antitrust & Trade Law > Sherman Act > General Overview

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Patent Law > Ownership > General Overview

378 F. Supp. 2d 850, \*850L 2005 U.S. Dist. LEXIS 14261, \*\*14261

## **HN12** [blue document icon] Antitrust & Trade Law, Sherman Act

A patentee's exercise of its statutorily-granted market power does not constitute a Sherman Act, [15 U.S.C.S. § 2](#), violation, even if such conduct affects a second market.

Antitrust & Trade Law > Sherman Act > General Overview

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

Patent Law > Ownership > General Overview

## **HN13** [blue document icon] Antitrust & Trade Law, Sherman Act

A patent holder may, of course, violate the Sherman Act, [15 U.S.C.S. § 2](#), by excluding others from inventions beyond the scope of the patent.

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Assignments

Patent Law > Infringement Actions > Exclusive Rights > Manufacture, Sale & Use

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Licenses

Antitrust & Trade Law > Sherman Act > General Overview

Patent Law > Infringement Actions > Exclusive Rights > General Overview

Patent Law > Ownership > General Overview

## **HN14** [blue document icon] Ownership & Transfer of Rights, Assignments

The United States Supreme Court case law suggests that the Sherman Act, [15 U.S.C.S. § 2](#), does not limit the patent holder's right to exclude others from the protected invention to a single market, but rather that the right is coextensive with the scope of the patent grant. Thus, patent law extends to protect a patent holder from antitrust liability in a second market that is encompassed by the patent claims.

Antitrust & Trade Law > ... > Intellectual Property > Misuse of Rights > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Infringing Acts > Indirect Infringement

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

## **HN15** [blue document icon] Intellectual Property, Misuse of Rights

See [35 U.S.C.S. § 271\(d\)](#).

Business & Corporate Compliance > ... > Infringement Actions > Infringing Acts > Indirect Infringement

378 F. Supp. 2d 850, \*850L 2005 U.S. Dist. LEXIS 14261, \*\*14261

## [HN16](#) [blue document icon] Infringing Acts, Indirect Infringement

Although [35 U.S.C.S. § 271\(d\)](#) does not explicitly refer to an antitrust violation, the United States Supreme Court has frequently used the language of whether a patent holder's actions have "expanded" or "enlarged" the patent grant to analyze allegations of antitrust violation, implying that the phrase in [§ 271\(d\)](#) includes antitrust violations.

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Assignments

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Licenses

Antitrust & Trade Law > Sherman Act > General Overview

Patent Law > Ownership > Conveyances > General Overview

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

## [HN17](#) [blue document icon] Ownership & Transfer of Rights, Assignments

A court agrees with the Federal Circuit's suggestion that the statutory language of the Patent Act indicates that a patent holder is not liable for an antitrust violation for refusing sell or license a patented product within the scope of the patent grant, and that this immunity is not limited to a single market. Thus, if the product is encompassed within the patent claims, the Sherman Act, [15 U.S.C.S. § 2](#), does not limit the patent holder's refusal to license or sell that item, or limit the patent holder's right to charge a higher price, in any market.

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Assignments

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Licenses

Antitrust & Trade Law > Sherman Act > General Overview

Patent Law > Ownership > Conveyances > General Overview

## [HN18](#) [blue document icon] Ownership & Transfer of Rights, Assignments

If a product is encompassed within the patent claims, the Sherman Act, [15 U.S.C.S. § 2](#), does not limit the patent holder's refusal to license or sell that item, or limit the patent holder's right to charge a higher price, in any market.

Antitrust & Trade Law > Sherman Act > General Overview

Patent Law > Ownership > General Overview

## [HN19](#) [blue document icon] Antitrust & Trade Law, Sherman Act

The United States Supreme Court has held that the Sherman Act, [15 U.S.C.S. § 2](#), is enacted to prevent restraint of commerce, but has explicitly recognized the patent grant as an exception.

**Counsel:** <sup>[\*\*1]</sup> For Gary Schor a Florida resident, on behalf of himself and all others similarly situated, Plaintiff: Ben Barnow, Sharon Harris, Barnow & Associates, P.C., Chicago, IL.

For Abbott Laboratories an Illinois corporation, Defendant: George Carter Lombardi, David James Doyle, James F. Hurst, Samuel S Park, Winston & Strawn, Chicago, IL.

**Judges:** Judge Robert W. Gettleman.

**Opinion by:** Robert W. Gettleman

## Opinion

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### **[\*851] MEMORANDUM OPINION AND ORDER**

Plaintiff Gary Schor filed a three-count class action complaint against defendant <sup>[\*852]</sup> Abbott Laboratories ("Abbott"), alleging violations of the Sherman Antitrust Act ("Sherman Act"), [15 U.S.C. § 2](#), and the Illinois Consumer Fraud Act, [815 ILCS 505/1, et seq.](#) Plaintiff also asserts a state law claim for unjust enrichment. Plaintiff alleges that defendant used its monopoly over its patented AIDS drug Norvir to unreasonably inflate the price of competitors' drug combinations that contain Norvir.

Subject matter jurisdiction of the Sherman Act claim is based on [28 U.S.C. §§ 1331](#) and [1337](#), and [15 U.S.C. § 15](#). Jurisdiction over the state law claims is based on supplemental <sup>[\*\*2]</sup> jurisdiction pursuant to [28 U.S.C. § 1367](#).

Defendant has moved to dismiss the complaint pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#) for failure to state a claim. For the reasons discussed below, the court grants defendant's motion to dismiss Count I, and declines to exercise supplemental jurisdiction over the state law claims.

### **FACTS**

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Defendant Abbott, an Illinois corporation, is a pharmaceutical company engaged in the business of manufacturing, developing, and distributing anti-retroviral drugs worldwide, including throughout the United States. Plaintiff, a citizen of Florida, purchased one of defendant's AIDS drugs, Norvir, for his personal use.

Norvir was originally <sup>[\*\*3]</sup> marketed as a stand-alone protease inhibitor ("PI"). PIs are anti-retroviral drugs that inhibit the AIDS virus from copying itself into new cells. Plaintiff alleges that Norvir cannot be interchanged with any other drug, and therefore constitutes a product market subject to antitrust laws. Through various patents, defendant controls 100% of the Norvir market, and there are no generic versions of Norvir. Norvir causes severe side effects when used alone, but when taken in conjunction with other PIs, it boosts the effectiveness of the other drugs. These "boosted PIs" also remain effective for longer periods of time. It is important for AIDS patients to have a variety of PIs available to them because patients may build a tolerance to certain drug combinations.

Defendant produces its own boosted PI, called Kaletra, which is boosted by Norvir. At least seven other boosted PIs, not manufactured by defendant, are boosted by Norvir: Agenerase, Crixivan, Fortovase, Invirase, Lexiva, Reyataz, and Viracept. Plaintiff alleges that PIs boosted by Norvir are not interchangeable with any other drugs and are a market subject to antitrust laws. Plaintiff asserts that defendant effectively controls <sup>[\*\*4]</sup> this market for "all of

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<sup>1</sup> For the purposes of a motion to dismiss, the court accepts all well-pleaded allegations as true and draws all reasonable inferences in favor of the plaintiff. [Travel All Over the World, Inc. v. Kingdom of Saudi Arabia](#), 73 F.3d 1423, 1428 (7th Cir. 1996).

the anti-retroviral drugs dependent on a boost from Norvir in the United States," and that the United States is a proper geographical market for antitrust purposes.

Kaletra, defendant's boosted PI, began to lose its market share in 2003. In December 2003, defendant raised the price of Norvir by more than 400%. Defendant did not, however, pass this price increase on to Kaletra. As a result, Kaletra costs substantially less than other boosted PIs. Plaintiff asserts that defendant's "anticompetitive pricing scheme is designed to exclude competition for Kaletra, even though Kaletra might not be the most effective PI for a particular patient." Prior to the increase, it was projected that defendant would receive over \$ 2 billion in revenues [**\*853**] for Norvir. According to plaintiff, defendant "had no legitimate justification for the exorbitant price increase of Norvir other than to strangle the market to the detriment of AIDS victims."

## **DISCUSSION**

**HN1** In ruling on a motion to dismiss for failure to state a claim, the court accepts the allegations of the complaint as true and views the facts in the light most favorable to the plaintiff. [Travel All Over the World, 73 F.3d at 1428.](#) [\*\*5] A complaint should not be dismissed for failure to state a claim unless there is no doubt that the plaintiff cannot prove a set of facts that would entitle her to relief based on her claim. [Pressalite Corp. v. Matsushita Electric Corp. of America, 2003 U.S. Dist. LEXIS 5600, 2003 WL 1811530, at \\*2 \(N.D. Ill. Apr. 4, 2003\).](#)

### **I. Collateral estoppel**

Plaintiff argues in his response to the motion to dismiss that defendant is collaterally estopped from raising its arguments in favor of its motion to dismiss by two earlier decisions issued by Judge Wilken of the Northern District of California, [Doe v. Abbott Laboratories, C 04-1511 CW, unpub. order \(N.D. Cal. Oct. 21, 2004\)](#), and [Service Employees International Union Health and Welfare Fund v. Abbott Laboratories, 2005 WL 528323 \(N.D. Cal. Mar. 2, 2005\)](#). Like the instant case, [Doe](#) and [Service Employees](#) are class actions against defendant brought by indirect consumers of Norvir. The [Doe](#) and [Service Employees](#) plaintiffs allege violations of the Sherman Act, as well as violations of the California Business and Professions Code and state law unjust enrichment claims. Judge Wilken denied the defendant's motions [\*\*6] to dismiss in both cases, which remain pending.

In the instant case, defendant argues that collateral estoppel does not apply because a ruling on a motion to dismiss is not a "final judgment," and thus does not trigger collateral estoppel.<sup>2</sup> **HN2** Collateral estoppel, or issue preclusion, bars the litigation in a subsequent action of an issue that has been decided in a prior action. [Meyer v. Rigdon, 36 F.3d 1375, 1378 n. 1 \(7th Cir. 1994\)](#). The Seventh Circuit has held that the party invoking collateral estoppel has the burden of proving four elements: (1) that the issue sought to be precluded is identical to the issue raised in the prior action; (2) that the issue was actually litigated; (3) that determination of the issue was essential to the final judgment; and (4) that the party against whom estoppel is invoked was fully represented in the prior action. *Id.* The party asserting estoppel has the burden of establishing which issues were actually determined in his favor in a prior action. [Gilldorn Savings Ass'n. v. Commerce Savings Ass'n., 804 F.2d 390, 393 \(7th Cir. 1986\)](#).

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<sup>2</sup> Defendant also argues that collateral estoppel does not apply because the California court "did not address 'identical' issues" to those presented in the instant case. In its joinder motion filed with the Judicial Panel on Multi-District Litigation ("MDL"), however, defendant asserts that the instant case and [Doe](#) and [Service Employees](#) "are based on identical facts and allege identical legal theories." Judicial estoppel prevents a party that has taken one position in litigating a particular set of facts from later reversing its position when it is to its advantage to do so, if the party to be estopped has convinced the court to adopt its position. [Levinson v. United States, 969 F.2d 260, 264 \(7th Cir. 1992\)](#). Although at this point judicial estoppel does not strictly apply because the MDL has not ruled on the joinder and transfer motion, the court notes that defendant's positions regarding identical facts appear clearly inconsistent. *Id.*

[\*\*7] Although defendant is correct that a ruling denying [HN3](#) a motion to dismiss is typically not a final judgment for the purposes of collateral estoppel, the Seventh Circuit has [\[\\*854\]](#) held that there are instances in which a motion to dismiss ruling may have preclusive effect. For example, the [Gilldorn](#) court held that a district court's denial of a motion to dismiss was sufficiently final for purposes of collateral estoppel. [Id.](#) In [Gilldorn](#), an Illinois district court judge granted the plaintiff's motion to enjoin a pending action brought by the defendant in Texas, based on the plaintiff's argument that the Texas action should have been brought as a compulsory counterclaim in the Illinois action. The plaintiff, however, had already moved for dismissal in the Texas action, and had made the compulsory counterclaim argument, along with others, unsuccessfully. [Id. at 391](#). The Seventh Circuit held that the Illinois district court should have given collateral estoppel effect to the Texas district court's denial of the plaintiff's dismissal motion. [Id. at 395](#).

In support of its holding that a denial of a motion to dismiss may, in some cases, operate as collateral estoppel, the [\[\\*8\]](#) [Gilldorn](#) court cited the Seventh Circuit's earlier holding in [Miller Brewing Co. v. Joseph Schlitz Brewing Co., 605 F.2d 990 \(7th Cir. 1979\)](#), cert. denied, 444 U.S. 1102, 62 L. Ed. 2d 787, 100 S. Ct. 1067 (1980). [HN4](#) To determine whether a decision is "final" for collateral estoppel purposes, the [Miller](#) court instructed courts to consider whether: (1) the decision was not "avowedly tentative"; (2) the hearing was adequate and the parties were fully heard; (3) the court supported its decision with a reasoned opinion; and (4) the decision was appealable or had been appealed. [605 F.2d at 996](#). The ultimate question, then, is whether the "'prior adjudication...is determined to be sufficiently firm to be accorded conclusive effect.'" [Id.](#) (quoting [Restatement \(Second\) of Judgments § 41 comment G](#) (Tent. Draft No. 1 1973)); see also [In re Bridgestone/Firestone Inc., 333 F.3d 763, 767 \(7th Cir. 2003\)](#) ("For the purposes of issue preclusion (as distinguished from merger and bar), 'final judgement' includes any prior adjudication of an issue in another action that is determined to be sufficiently firm to be accorded conclusive [\[\\*9\]](#) effect.").

Judge Wilken's findings regarding the California plaintiffs' Sherman Act claims do not have collateral estoppel effect in the instant case.<sup>3</sup> First, most of the "holdings" listed by plaintiff in its brief are not in fact holdings. The plaintiffs in [Doe](#) and [Service Employees](#), like plaintiff in the instant case, rely on a "monopoly leveraging theory" of antitrust liability. Although the Ninth Circuit applied this theory to a patentee in [Image Technical Services, Inc. v. Eastman Kodak, Co., 125 F.3d 1195 \(9th Cir. 1997\)](#), cert. denied, 523 U.S. 1094, 140 L. Ed. 2d 792, 118 S. Ct. 1560 (1998), there is a circuit split on this question, as discussed below, and Ninth Circuit case law is not binding on this court. More damaging to plaintiff's collateral estoppel argument, Judge Wilken did not hold that defendant was liable under this theory, but only that the plaintiffs in those cases had alleged sufficient facts to survive the motions to dismiss. [Doe](#) at 6; [Service Employees, 2005 WL 528323, at \\*3](#). Similarly, the California court did not issue a final judgment or appealable ruling on the question of defendant's monopoly power in the boosted PI market, [\[\\*10\]](#) but held only that under Ninth Circuit law the plaintiffs had sufficiently pled all of the essential elements of their Sherman Act claims. [Id.](#) Such non-final holdings cannot collaterally estop defendant from advancing similar arguments here.

[\[\\*855\]](#) Second, although Judge Wilken held that the plaintiffs in [Doe](#) and [Service Employees](#) had standing as indirect consumers of Norvir to pursue their Sherman Act claims, the Seventh Circuit has held that the "denial of a motion to dismiss for lack of standing does not qualify as a final judgment." [Triad Assocs., Inc. v. Robinson, 10 F.3d 492, 496 n. 2 \(7th Cir. 1993\)](#) (citing [Crymes v. DeKalb County, Ga., 923 F.2d 1482, 1484-1485 \(11th Cir. 1991\)](#); see also [Carter v. Signode Industries, Inc., 1988 U.S. Dist. LEXIS 13456, 1988 WL 130619, at \\*1 \(N.D. Ill. Dec. 1, 1988\)](#) [\[\\*11\]](#) (noting that denial of motion to dismiss for lack of standing, absent certification of interlocutory appeal under [28 U.S.C. § 1292\(b\)](#), is "otherwise unappealable"). Because the denial of the motions to dismiss [Doe](#) and [Service Employees](#) for lack of standing were not final orders and thus not appealable, they do not have collateral estoppel effect on defendant's arguments in support of its motion to dismiss in the instant case.

## II. Sherman Act

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<sup>3</sup> Although the court does not reach plaintiff's state law claims, it is clear that Judge Wilken's rulings on the California plaintiffs' state law claims, brought under California law, do not have a collateral estoppel effect on a court applying Illinois law.

Count I of plaintiff's complaint alleges that defendant violated [§ 2 of the Sherman Act](#) by abusing its monopoly power in the U.S. market for Norvir, its patented product, to unfairly injure competition in the market for PIs boosted by Norvir.<sup>4</sup> Defendant's own boosted PI, Kaletra, competes in this second market with approximately seven other PIs boosted by Norvir. Defendant argues that Count I should be dismissed because its patents for Norvir, which cover its use as a stand-alone drug and as a booster when combined with other PIs, preclude antitrust liability. Defendant also argues that plaintiff fails to sufficiently allege defendant's market power in the boosted PI market, [\[\\*\\*12\]](#) and that plaintiff lacks standing to obtain relief under the Sherman Act because he is an indirect consumer and has failed to allege that he suffered any antitrust injuries.<sup>5</sup>

The instant case reveals the tension between antitrust laws, which discourage monopolies, and patent laws, which protect monopolies. [See Image Technical Servs., Inc. v. Eastman Kodak Co., 125 F.3d 1195, 1217 \(9th Cir. 1997\)](#) ("At the border of intellectual property monopolies and antitrust [\[\\*\\*13\]](#) markets lies a field of dissonance yet to be harmonized by statute or the Supreme Court."); [Sheet Metal Duct, Inc. v. Lindab, Inc., 2000 U.S. Dist. LEXIS 9928, 2000 WL 987865, at \\*2 \(E.D. Pa. July 18, 2000\)](#) ("patent and antitrust laws exist in tension, as the patent laws protect monopoly power, while antitrust laws seek to restrain it"); [see also](#) Patrick H. Moran, Comment, [The Federal and Ninth Circuits Square Off: Refusals to Deal - the Precarious Intersection Between Antitrust and Patent Law, 87 MARQ. L. REV. 387, 387 \(2003\)](#) ("Although both the patent and antitrust laws were designed to stimulate the economy and benefit consumers, a fundamental tension between the two has always existed."). [HN6](#)<sup>↑</sup> One consequence of the overlap between the patent and antitrust statutes and case law is that there is no easy delinement between a patent holder's permissible exercise of its rights under patent law, which grants a government-sanctioned monopoly and expressly allows the patentee to engage in exclusionary conduct, and anticompetitive behavior that [\[\\*856\]](#) violates [antitrust law](#), which proscribes exclusionary conduct when coupled with monopoly power.

Although not a model of clarity in antitrust [\[\\*\\*14\]](#) pleading, plaintiff's complaint alleges two separate markets: the Norvir market and the market of PIs boosted by Norvir. Plaintiff clarifies in his response to the motion to dismiss that he does not dispute the validity of the Norvir patents or defendant's lawful monopoly in the Norvir market. Instead, he is challenging defendant's use of its monopoly of the Norvir market to attain a monopoly in the boosted PI market. Plaintiff's Sherman Act claim is premised on an extension of the monopoly leveraging theory to patent holders, under which antitrust liability may be based on the improper use of a monopoly in one market to strengthen or create a monopoly in another market. [Virgin Atlantic Airways Ltd. v. British Airways PLC, 257 F.3d 256, 272 \(2nd Cir. 2001\); Alaska Airlines, Inc. v. United Airlines, Inc, 948 F.2d 536, 547 \(9th Cir. 1991\). HN7](#)<sup>↑</sup> To establish a [§ 2 Sherman Act](#) violation based on monopoly leveraging, a plaintiff must prove that the monopolist: (1) possesses monopoly power in the primary relevant market; (2) gained or attempted to gain a monopoly power in a second relevant market; and (3) willfully acquired the monopoly power by some exclusionary [\[\\*\\*15\]](#) conduct and not through efficiency and innovation." [Alaska Airlines, 948 F.2d at 547.](#)

The Supreme Court emphasized in [Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP, 540 U.S. 398, 415 n. 4, 157 L. Ed. 2d 823, 124 S. Ct. 872 \(2004\)](#), that a monopoly leveraging claim "presupposes anticompetitive conduct." It is well established that not all conduct that hurts competitors is anticompetitive or a violation of the antitrust laws. [See, e.g., Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 458, 122 L. Ed. 2d 247, 113 S. Ct. 884 \(1993\)](#) ("The [Sherman Act] directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself."); [Endsley v. City of Chicago, 230 F.3d 276, 283 \(7th Cir. 2000\)](#) ("Under [§ 2](#), intent to obtain a monopoly is unlawful only where an entity seeks to maintain or achieve monopoly power by anticompetitive means."); [Intergraph Corp. v. Intel Corp, 195 F.3d 1346, 1363 \(Fed. Cir. 1999\)](#) ("Precedent makes clear that a customer who is dependent on a manufacturer's supply of a component

<sup>4</sup> [HN5](#)<sup>↑</sup> Section 2 of the Sherman Act, [15 U.S.C. § 2](#), prohibits monopolization or attempts to monopolize: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony . . . ."

<sup>5</sup> In plaintiff's response to the motion to dismiss, he withdraws his claims for damages under Count I of his complaint, and now seeks only injunctive relief.

cannot on that ground force the producer to provide it; there must also be an anticompetitive [\*\*16] aspect invoking the Sherman Act [to warrant imposition of antitrust liability."]. [HN8](#)<sup>↑</sup> To state a claim for a Sherman Act violation, a plaintiff must allege conduct that hurts competition in the relevant market. [Endsley, 230 F.3d at 284](#) (affirming dismissal of plaintiff's antitrust claim because plaintiff failed to identify "any facts which point to the [defendant's] alleged anti-competitive use of its power to control the price").

There is sparse case law regarding if or how the monopoly leveraging theory applies to conduct by a patentee, and what little case law there is does not concern a price increase by a patent holder. In the instant case, both parties cite to opinions addressing whether a patentee's refusal to deal -- to license or sell its patented product -- is a violation of antitrust law. The court agrees with the parties' implicit assumption that it is appropriate to analogize refusal to deal cases with the price increase at issue here because if a patentee has the right to refuse to sell its product altogether, it has the right to raise the price. See [Zenith Laboratories, Inc. v. Carter-Wallace, Inc., 530 F.2d 508, 513 n. 9 \(3rd Cir. 1976\)](#) [\*\*17] ("a patentee is privileged to withhold [its invention] from sale at any [\*857] price, or to offer it for sale at any price he wishes, low or high") (citing 6A CORBIN, CONTRACTS § 1410 at 246 (1962)). Applying the refusal to deal case law to the instant case, however, is no easy task. There is no Supreme Court precedent, and a split exists between the Ninth and Federal Circuits regarding whether the monopoly leveraging theory may be applied to patent holders. Thus, this is a case of first impression in the Seventh Circuit whether a patent holder may be liable under the monopoly leveraging theory, and whether the Sherman Act limits a patentee's right to exclude others from more than one relevant market.

The Ninth Circuit was the first court to examine the antitrust liability of a patent holder under the monopoly leveraging theory. Sharon Brawner McCullen, Comment, [The Federal Circuit and Ninth Circuit Face-Off: Does A Patent Holder Violate the Sherman Act By Unilaterally Excluding Others From A Patented Invention In More Than One Relevant Market?, 74 TEMP. L. REV. 469, 500 \(2001\)](#). In [Image Technical Services, Inc. v. Eastman Kodak Co., 125 F.3d 1195 \(9th 1997\)](#), [\*\*18] cert. denied, 523 U.S. 1094, 140 L. Ed. 2d 792, 118 S. Ct. 1560 (1998) ("Kodak II"), the court held that patent rights do not immunize a patent holder to antitrust violations based on monopoly leveraging, and that a patent holder may be liable under the monopoly leveraging theory for using its monopoly over a patented product to affect a secondary market. The plaintiffs in Kodak II were a group of independent service organizations (ISOs) who alleged Sherman Act violations after Kodak refused to sell replacement parts, many of which were patented, to the ISOs, who serviced and repaired Kodak photocopier equipment.

In Kodak II the Ninth Circuit extended earlier monopoly leveraging precedent to antitrust cases involving patented products, and limited a patent holder's right to exclude others to a single market. [Id. at 1217-18](#). Kodak II held that Kodak violated § 2 of the Sherman Act when it refused to sell its patented parts for use by independent service organization in the secondary service market. In support of its finding, the Kodak II court relied in part on a footnote in the Supreme Court's opinion affirming the Ninth Circuit's earlier denial of summary judgment. [\*\*19] [Id. at 1215-16](#). Addressing the plaintiffs' § 2 monopolization claim, the Court rejected the argument that a manufacturer competing in the secondary service market enjoys per se immunity to antitrust laws. [Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 479 n. 29, 119 L. Ed. 2d 265, 112 S. Ct. 2072 \(1992\)](#) ("Kodak I"). The Court noted that it "has held many times that power gained through some natural and legal advantage such as a patent, copyright, or business acumen can give rise to liability if 'a seller exploits his dominant position in one market to expand his empire into the next.'" Id.

Three years later, and faced with a very similar factual situation to Kodak II, the Federal Circuit expressly rejected the Ninth Circuit's reasoning, and held that [HN9](#)<sup>↑</sup> a patent holder does not violate the Sherman Act by refusing to license or sell a patented item in a second market, even when the patented product is necessary to the second market. [In re Independent Service Organizations Antitrust Litigation CSU, L.L.C., v. Xerox, 203 F.3d 1322 \(Fed. Cir. 2000\)](#), cert. denied, 531 U.S. 1143, 148 L. Ed. 2d 954, 121 S. Ct. 1077 (2001) ("Xerox"). The Xerox plaintiffs, [\*\*20] ISO competitors in the photocopier service market, sued Xerox over its refusal to sell its patented replacement parts and other copyrighted materials to ISOs unless they were also end-users of Xerox copiers. [Id. at 1324](#). Affirming the district court's grant of summary [\*858] judgment to the defendant, the Federal Circuit held that [HN10](#)<sup>↑</sup> absent "illegal tying, fraud in the Patent and Trademark Office, or sham litigation," a patentee may enforce its statutory

rights "free from liability under the antitrust law." *Id. at 1327-28*. Contrary to the Ninth Circuit, the Federal Circuit also held that a patent holder's right to exclude extends to any relevant market that involves the use, manufacture or sale of the invention. *Id. at 1325-26*.

Defendant in the instant case incorrectly argues that Xerox is binding precedent because the instant case involves patents, and therefore the law of the Federal Circuit, rather than Seventh or Ninth Circuit law, controls. See In re Spalding Sports Worldwide, Inc., 203 F.3d 800, 803 (Fed. Cir. 2000) (Federal Circuit law applies to issues of substantive patent law). HN11[<sup>1</sup>] The Supreme Court, however, has significantly [\*\*21] curtailed the Federal Circuit's jurisdiction over antitrust claims, which had expanded during the 1990s. In Holmes Group, Inc. v. Vornado Air Circulation Systems, Inc., 535 U.S. 826, 829-830, 153 L. Ed. 2d 13, 122 S. Ct. 1889 (2002), the Court held that 28 U.S.C. § 1338, the congressional grant of jurisdiction to the Federal Circuit, requires that the plaintiff's complaint "creates the cause of action." In the instant case, defendant cites Unitherm Food Systems, Inc. v. Swift-Eckrich, Inc., 375 F.3d 1341, 1355 (Fed. Cir. 2004), in support of its argument that Federal Circuit precedent controls, but Unitherm is inapposite. The plaintiffs in Unitherm sought a declaration of patent invalidity, in addition to asserting monopolization and tortious interference claims, *Id.* In contrast, plaintiff in the instant case has disavowed any patent claims, and patent law does not create the cause of action. Federal Circuit law may nevertheless control the instant case, however, because, as discussed below, the scope of the patent is an issue.

Regardless of which circuit's law must control, for the reasons discussed below the court finds the Xerox court's reasoning [\*\*22] persuasive, and that the holding represents a sounder approach to a patentee's antitrust liability in a second market than the Ninth Circuit's opinion in Kodak II. The court agrees with the Federal Circuit that subject to narrow limitations, not at issue in the instant case, HN12[<sup>1</sup>] a patentee's exercise of its statutorily-granted market power does not constitute a Sherman Act violation, even if such conduct affects a second market. The Federal Circuit's decision is in keeping with the case law and the statutory language suggesting that a court must consider the scope of the patent grant when determining whether an antitrust violation has occurred, and properly holds that a patentee is not liable for conduct within the scope of its valid patent grant.

HN13[<sup>1</sup>] A patent holder may, of course, violate the Sherman Act by excluding others from inventions beyond the scope of the patent. Ethyl Gasoline Corp. v. United States, 309 U.S. 436, 457-58, 84 L. Ed. 852, 60 S. Ct. 618, 1940 Dec. Comm'r Pat. 758 (1940). For example, the Supreme Court has held that a patent holder exceeded the scope of its patent by conditioning a license agreement on the licensee's use of the protected invention with products not included in the patent grant, Motion Picture Patents Co. v. Universal Film Mfg. Co., 243 U.S. 502, 512, 61 L. Ed. 871, 37 S. Ct. 416, 1917 Dec. Comm'r Pat. 391 (1917). [\*\*23] on royalty payments for products not within the scope of the patented invention, Zenith Radio Corp. v. Hazeltine Research, Inc., 395 U.S. 100, 135-36, 23 L. Ed. 2d 129, 89 S. Ct. 1562 (1969), or on the purchase, use or sale of other products, Ethyl Gasoline, 309 U.S. at 447-48. As these cases indicate, the Supreme Court carefully distinguishes between the unlawful enlargement of a patent and a patentee's [\*859] lawful exercise of the right to sell others the invention within the scope of the patent. See, e.g., Ethyl Gasoline, 309 U.S. at 457-58 ("The picture here revealed is not that of a patentee exercising its right to refuse to sell or to permit his licensee to sell the patented product."). HN14[<sup>1</sup>] The Supreme Court case law suggests that the Sherman Act does not limit the patent holder's right to exclude others from the protected invention to a single market, but rather that the right is coextensive with the scope of the patent grant. Thus, patent law extends to protect a patent holder from antitrust liability in a second market that is encompassed by the patent claims.

The court agrees with the Xerox court that footnote 29 in the Supreme Court's decision in Kodak I, [\*\*24] which suggests that a patentee's expansion into a second market may be an antitrust violation, is largely inapposite to the facts of Kodak II and Xerox, and was incorrectly applied by the Ninth Circuit in Kodak II. As the Federal Circuit noted, Kodak I was a tying case when it came before the Supreme Court, and no patents had been asserted in defense of the antitrust claims against Kodak. Xerox, 203 F.3d at 1327. "Properly viewed within the framework of a tying case, the footnote can be interpreted as restating the undisputed premise that the patent holder cannot use his statutory right to refuse to sell patented parts to gain a monopoly in a market *beyond the scope of the patent*. *Id.* (emphasis in original). The Federal Circuit recognized that a patent grant may encompass multiple markets, and held that Xerox's actions fell within the statutory patent grant. *Id. at 1327*.

The Federal Circuit cited [section 271\(d\) of the Patent Act](#), which immunizes a patent holder against certain liabilities, in support of its expansion of a patentee's rights into a second market. [Xerox, 203 F.3d at 1326. HN15](#)<sup>15</sup> [Section 271\(d\)](#) states [\[\\*\\*25\]](#) that, "No patent owner otherwise entitled to relief. . .shall be denied relief or deemed guilty of misuse or *illegal extension of the patent right* by reason of his having...(4) refused to license or use any rights to the patent..." [35 U.S.C. § 271\(d\)](#) (emphasis added). [HN16](#)<sup>16</sup> Although [§ 271\(d\)](#) does not explicitly refer to an antitrust violation, the Supreme Court has frequently used the language of whether a patent holder's actions have "expanded" or "enlarged" the patent grant to analyze allegations of antitrust violation, implying that the phrase in [§ 271\(d\)](#) includes antitrust violations. [See McCullen, 74 TEMP. L. REV. 469, 494](#) (collecting cases). [HN17](#)<sup>17</sup> The court agrees with the Federal Circuit's suggestion that the statutory language of the [Patent Act](#) indicates that a patent holder is not liable for an antitrust violation for refusing sell or license a patented product within the scope of the patent grant, and that this immunity is not limited to a single market. Thus, [HN18](#)<sup>18</sup> if the product is encompassed within the patent claims, the Sherman Act does not limit the patent holder's refusal to license or sell that item, or limit the patent holder's right to [\[\\*\\*26\]](#) charge a higher price, in any market.

Lastly, the instant case is factually distinguishable from [Kodak II](#) and [Xerox](#) in aspects that support defendant's argument that it should not be subject to antitrust liability for raising the price of Norvir. First, defendant's patents cover Norvir's use in the stand-alone market as well as the boosted PI market. Plaintiff does not challenge defendant's assertion that its patents "explicitly cover the use of Norvir as a 'booster' in combination with another PIs." In [Xerox](#) and [Kodak II](#), in contrast, the second market at issue was a service and repair market, which was apparently not covered by the defendants' patent grants. Here, the alleged second market is for compound products containing the [\[\\*860\]](#) first market's product, and plaintiff does not argue that defendant's use of Norvir in Kaletra or its sale of Norvir as a booster for competitors' boosted PIs exceeds the patent grant. Unlike [Xerox](#) and [Kodak II](#), defendant's Norvir patents apply in both markets to cover Norvir's use in conjunction with drugs manufactured and sold by third parties.

Second, in [Xerox](#) the Federal Circuit determined that the defendant's refusal to [\[\\*\\*27\]](#) deal was within the scope of its patent claims and thus permissible. [203 F.3d at 1327-28](#). In the instant case, defendant has taken a less drastic measure than the defendants in [Kodak II](#) and [Xerox](#), because it has not instituted a unilateral refusal to deal, which would prevent customers or a group of customers from obtaining its product. Plaintiff does not allege that Norvir or any of the boosted PIs that depend on Norvir are unavailable, but only that they are significantly more expensive. The court is not unsympathetic to plaintiff's seemingly legitimate concerns that the drastic price increase will prevent him and other AIDS patients from receiving the best drug treatments for their disease, but antitrust laws do not impose liability for a business entity's failure to act morally or in the public interest.

To accept plaintiff's argument would seem to impose antitrust liability on any manufacturer who holds patents for a product when used alone as well as for its use as a component in products manufactured by the patentee and competitors, and raises the price it charges competitors for its patented component. Such a result runs contrary to the aims of the antitrust [\[\\*\\*28\]](#) and patent laws to encourage innovation and competition, and is not supported by the case law. [HN19](#)<sup>19</sup> The Supreme Court has held that the Sherman Act was enacted to prevent restraint of commerce, but has explicitly recognized the patent grant as an exception. [United States v. Line Material Co., 333 U.S. 287, 309, 92 L. Ed. 701, 68 S. Ct. 550 \(1948\)](#). The court is not persuaded by plaintiff's arguments in the instant case, or by the Ninth Circuit's reasoning in [Kodak II](#), that a patentee's right to exclude others, including by raising prices, is limited to the primary market only, particularly when, as here, it is not disputed that the use of the patented invention in second market is within the scope of the patent claims.

For the reasons stated above, defendant may not be held liable for a violation of [§ 2 of the Sherman Act](#) for increasing the price of its patented product, even though that price increase may affect competition in a second market. Accordingly, the court grants defendant's motion to dismiss Count I with prejudice.

Because the court grants defendant's motion to dismiss Count I, it need not reach defendant's alternative arguments that plaintiff failed to allege market power or that [\[\\*\\*29\]](#) plaintiff lacks standing as an indirect consumer to pursue injunctive relief. In addition, the court declines to exercise supplemental jurisdiction over the remaining state law claims. Accordingly, the court grants defendant's motion to dismiss Counts II and III without prejudice.

**CONCLUSION**

For the reasons stated above, the court grants defendant's motion to dismiss the complaint. Count I is dismissed with prejudice. Counts II and III are dismissed without prejudice.

**ENTER: July 12, 2005**

**Robert W. Gettleman**

**United States District Judge**

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## **Meijer, Inc. v. 3M**

United States District Court for the Eastern District of Pennsylvania

July 13, 2005, Decided

CIVIL ACTION NO. 04-5871

### **Reporter**

2005 U.S. Dist. LEXIS 13995 \*; 2005-2 Trade Cas. (CCH) P74,882

MEIJER, INC., et al. On Behalf of Itself and Others Similarly Situated v. 3M (MINNESOTA MINING AND MANUFACTURING COMPANY)

**Subsequent History:** Settled by, Motion granted by [Meijer, Inc. v. 3M, 2006 U.S. Dist. LEXIS 56744 \(E.D. Pa., Aug. 14, 2006\)](#)

## **Core Terms**

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damages, antitrust, statute of limitations, purchaser, tape, four year, overcharges, alleges, cause of action, accrue, prices, monopoly power, monopolist, argues, limitations period, speculative, transparent, motion to dismiss, antitrust action, anticompetitive, continuing violation, lawsuit, rebates, levels, injurious act, invisible

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > General Overview

### **HN1** [] **Motions to Dismiss, Failure to State Claim**

When determining a motion to dismiss pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#), the trial court may look only to the facts alleged in the complaint and its attachments. The trial court must accept as true all well pleaded allegations in the complaint and view them in the light most favorable to the plaintiff. A [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion will be granted when the plaintiff cannot prove any set of facts, consistent with the complaint, which would entitle him or her to relief. Documents integral to or explicitly relied upon in the complaint and related matters of public record may be considered on a motion to dismiss.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Affirmative Defenses > General Overview

Governments > Legislation > Statute of Limitations > Pleadings & Proof

Governments > Legislation > Statute of Limitations > General Overview

### **HN2** [] **Defenses, Demurrsers & Objections, Affirmative Defenses**

The statute of limitations is an affirmative defense, and the burden of establishing its applicability to a particular claim rests with the defendant.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Governments > Legislation > Statute of Limitations > Pleadings & Proof

Governments > Legislation > Statute of Limitations > General Overview

### **HN3** Motions to Dismiss, Failure to State Claim

When considering a motion to dismiss pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#) on statute of limitations grounds, courts must determine whether the time alleged in the statement of a claim shows that the cause of action has not been brought within the statute of limitations. The defendant bears a heavy burden in seeking to establish that the challenged claims are barred as a matter of law.

Antitrust & Trade Law > Clayton Act > Claims

Governments > Legislation > Statute of Limitations > Time Limitations

Antitrust & Trade Law > Clayton Act > General Overview

### **HN4** Clayton Act, Claims

The Clayton Act, [15 U.S.C.S. § 15b](#), which governs private antitrust actions, provides that any action to enforce any cause of action under [15 U.S.C.S. § 15, § 15a](#), or [§ 15c](#) shall be forever barred unless commenced within four years after the cause of action accrued. Generally, a cause of action accrues, and the statute begins to run, when a defendant commits an act that injures a plaintiff's business.

Antitrust & Trade Law > Regulated Practices > Private Actions > General Overview

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > Sherman Act

Governments > Legislation > Statute of Limitations > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

### **HN5** Regulated Practices, Private Actions

The four-year statute of limitations under [15 U.S.C.S. § 15b](#), does not bar recovery for later private antitrust actions if the defendant's conduct constituted a continuing violation of the Sherman Act and inflicted continuing and accumulating harm. In such situations, even if the overt act which demonstrates the antitrust violation occurs outside the statute of limitations period, an injurious act within the limitations period may serve as the basis for a timely antitrust suit.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Governments > Legislation > Statute of Limitations > Time Limitations

#### [HN6](#) [down] **Private Actions, Remedies**

While it should seem that high prices following the creation of a monopoly are mere inertial consequences one naturally expects to flow from such acts, a purchaser suing a monopolist for overcharges paid within the previous four years may satisfy the conduct prerequisite to recovery by pointing to anticompetitive actions taken before the limitations period. This principle is based on the recognition that although the business of a monopolist may be injured at the time the anticompetitive conduct occurs, a purchaser, by contrast, is not harmed until the monopolist actually exercises its illicit power to extract an excessive price. The case of predatory pricing illustrates the point clearly. As soon as the dominant firm commences such a policy, other producers, who may be driven out of the market, are injured. But, clearly, purchasers are not, for they receive the temporary boon of artificially low prices. It is only when the monopolist, having devoured its smaller rivals, enjoys the spoils of its conquest by boosting its price to excessive levels that a purchaser feels the adverse impact of the violation. And if the monopolist never consummates its scheme by taking this final step, the purchaser has no cause of action.

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Governments > Legislation > Statute of Limitations > General Overview

#### [HN7](#) [down] **Private Actions, Purchasers**

In purchaser antitrust actions, the requisite injurious act within the limitations period can include being overcharged as the result of an unlawful act which took place outside the limitations period but continues to allow the defendant to maintain market control.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Governments > Legislation > Statute of Limitations > General Overview

#### [HN8](#) [down] **Private Actions, Remedies**

The general rule of accrual in antitrust actions provides that if a plaintiff feels the adverse impact of an antitrust violation on a particular date, a cause of action immediately accrues to him to recover all damages incurred by that date and all provable damages that will flow in the future. The mere fact that damages may continue to accrue in the future, as opposed to at the time the acts are committed, does not prevent the cause of action from accruing.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Governments > Legislation > Statute of Limitations > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

## **HN9** [down] **Private Actions, Remedies**

In antitrust actions as in others, even if injury and a cause of action have accrued as of a certain date, future damages that might arise from the conduct sued on are unrecoverable if the fact of their accrual is speculative or their amount and nature unprovable. In these instances, antitrust causes of action for future damages will accrue only on the date the damages are suffered; thereafter the plaintiff may sue to recover them at any time within four years from the date they were inflicted. In purchaser antitrust actions, damages from future overcharges necessarily fall into the speculative damages exception to the four year statute of limitations. At the time a monopolist commits anticompetitive conduct it is entirely speculative how much damage that action will cause its purchasers in the future. Indeed, some of the buyers who will later feel the brunt of the violation may not even be in existence at the time. Not until the monopolist actually sets an inflated price and its customers determine the amount of their purchases can a reasonable estimate be made. The purchaser's cause of action, therefore, accrues only on the date damages are suffered.

Antitrust & Trade Law > Clayton Act > Claims

Torts > Business Torts > General Overview

Antitrust & Trade Law > Clayton Act > Penalties

Antitrust & Trade Law > Clayton Act > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > Damages

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > Prioritizing Resources & Organization for Intellectual Property Act

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > ... > Private Actions > Standing > Clayton Act

Antitrust & Trade Law > ... > Private Actions > Standing > Sherman Act

Antitrust & Trade Law > Sherman Act > Remedies > Damages

## **HN10** [down] **Clayton Act, Claims**

To state a claim for monopolization in violation of [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), a plaintiff must allege (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historical accident. The right to maintain a private cause of action for damages arising under [15 U.S.C.S. § 2](#) flows from § 4 of the Clayton Act, [15 U.S.C. § 15\(a\)](#), which provides that any person who shall be injured in his business or property by reason of anything forbidden in the Accordingly, plaintiffs bringing a private cause of action under [15 U.S.C.S. § 2](#) must prove more than injury causally linked to an illegal presence in the market. Plaintiffs must prove antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

## [\*\*HN11\*\*](#) [+] **Private Actions, Remedies**

The existence of antitrust injury is not typically resolved through motions to dismiss. Moreover, there are no special pleading requirements for an antitrust claim. Rather, notice pleading is all that is required for a valid antitrust complaint. Courts, therefore, must accept as true the factual allegations in the complaint and all reasonable inferences that can be drawn from them. Courts are not, however, required to accept as true unsupported conclusions and unwarranted inferences.

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For 3M COMPANY, formerly known as MINNESOTA MINING AND MANUFACTURING COMPANY, Defendant: BRENT N. RUSHFORTH, KATHERINE E. WOOD, KIT A. PIERSON, PAUL ALEXANDER, HELLER EHRLMAN LLP, WASHINGTON, DC; DAVID W. ENGSTROM, ELEANOR ILLOWAY, JOHN G. HARKINS, JR., HARKINS CUNNINGHAM, PHILADELPHIA, PA.

**Judges:** John R. Padova, J.

**Opinion by:** John R. Padova

## **Opinion**

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### **MEMORANDUM**

**Padova, J.**

Plaintiffs, Meijer, Inc. and Meijer Distribution, Inc. (collectively "Meijer"), have brought this antitrust action against Defendant 3M for damages arising out of 3M's anticompetitive conduct during the time period from October 2, 1998,

through the present. Presently before the Court is 3M's Motion to Dismiss the Complaint pursuant to [Federal Rule of Civil Procedure 12\(b\)\(6\)](#). For the reasons that [\*2] follow, this Motion is denied.

## I. BACKGROUND

The conduct of 3M which forms the basis of this class action lawsuit was the subject of a prior lawsuit in this Court, [LePage's, Inc. v. 3M, 1997 U.S. Dist. LEXIS 18501, Civ. A. No. 97-3983 \(E.D. Pa.\)](#). In that suit, LePage's, Inc., a competing supplier of transparent tape, sued 3M alleging, inter alia, unlawful maintenance of monopoly power in violation of Section 2 of the Sherman Act, [15 U.S.C. § 2](#). After a nine-week trial, the jury found in favor of LePage's on its unlawful maintenance of monopoly power claim. The jury awarded damages in the amount of \$ 22,828,899.00, which were subsequently trebled to \$ 68,486,697.00. See [LePage's, Inc. v. 3M, Civ. A. No. 97-3983, 2000 WL 280350 \(E.D. Pa. Mar. 14, 2000\)](#). 3M filed a Motion for Judgment as a Matter of Law, which this Court denied on March 14, 2000. See *id.* 3M thereafter appealed this Court's denial of its Motion for Judgment as a Matter of Law to the United States Court of Appeals for the Third Circuit ("Third Circuit"). A Third Circuit panel initially reversed this Court's Order upholding the jury's verdict and directed the Court to enter judgment for 3M on LePage's [\*3] 'unlawful maintenance of monopoly power claim. [LePage's, Inc. v. 3M, 277 F.3d 365 \(3d Cir. 2002\)](#) ("LePage's I"). Upon rehearing en banc, the Third Circuit vacated the panel decision and reinstated the original jury verdict against 3M. [LePage's, Inc. v. 3M, 324 F.3d 141 \(3d Cir. 2003\)](#) ("LePage's II"), cert. denied 542 U.S. 953, 124 S. Ct. 2932, 159 L. Ed. 2d 835 (2004).

Thereafter, Bradburn Parent/Teacher Store, Inc. brought a class action lawsuit against 3M on the basis of the conduct litigated in *LePage's*. [Bradburn Parent/Teacher Store, Inc. v. 3M, Civ. A. No. 02-7676 \(E.D. Pa.\)](#). Bradburn, who originally had sought to represent a class which included Meijer, was ultimately granted class certification on a modified class that excluded purchasers of private label tape, such as Meijer. [Bradburn Parent/Teacher Store v. 3M, 2004 U.S. Dist. LEXIS 16193, Civ. A. No. 02-7676, 2004 WL 1842987 \(E.D. Pa. Aug. 18, 2004\)](#). Having been excluded from the class in *Bradburn*, Meijer first attempted to intervene in that lawsuit as an additional class representative. In denying Meijer's motion to intervene, the Court noted that "there is nothing which would prevent Meijer [\*4] from filing its own individual or class action lawsuit against [3M] and presenting its claims in that forum." [Bradburn Parent/Teacher Store, Inc. v. 3M, 2004 U.S. Dist. LEXIS 25246, Civ. A. No. 02-7676, 2004 WL 2900810, at \\*6 \(E.D. Pa. Dec. 10, 2004\)](#). On December 16, 2004, Meijer filed the instant Complaint.

Meijer brings this action on behalf of itself and other members of a proposed class, which includes "all persons and entities who purchased invisible or transparent tape directly from 3M . . . at any time during the period from October 2, 1998 to the present . . ." (Compl. P 18.) The Complaint sets forth one count of monopolization in violation of [Section 2 of the Sherman Act](#). The Complaint alleges that 3M unlawfully maintained monopoly power in the transparent tape market through its bundled rebate programs<sup>1</sup> and through exclusive dealing arrangements with various retailers. (*Id.* P 27.) The Complaint further alleges that "3M has used its unlawful monopoly power . . . to harm Plaintiffs and the other Class members in their business or property by increasing, maintaining, or stabilizing the prices they paid for invisible and transparent tape above competitive levels." (*Id.* P 34.) [\*5] The damages period in this case runs from October 2, 1998, to the present. (*Id.* P 18.) In the instant Motion, 3M moves to dismiss the Complaint in its entirety pursuant to [Federal Rule of Civil Procedure 12\(b\)\(6\)](#).

## II. LEGAL STANDARD

**HN1** When determining a motion to dismiss pursuant to [Rule 12\(b\)\(6\)](#), the court may look only to the facts alleged in the complaint and its attachments. [Jordan v. Fox, Rothschild, O'Brien & Frankel, 20 F.3d 1250, 1261 \(3d Cir. 1994\)](#). The court must accept as true all well pleaded allegations in the complaint and view them in the light most favorable to the Plaintiff. [Angelastro v. Prudential-Bache Sec., Inc., 764 F.2d 939, 944 \(3d Cir. 1985\)](#). [\*6] A [Rule 12\(b\)\(6\)](#) motion will be granted when a Plaintiff cannot prove any set of facts, consistent with the complaint,

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<sup>1</sup> As described at length in the *LePage's* litigation, 3M's bundled rebate programs provided purchasers with significant discounts on 3M's products. However, the availability and size of the rebates were dependant upon purchasers buying products from 3M from multiple product lines. See [LePage's II, 324 F.3d at 154-55](#).

which would entitle him or her to relief. [Ransom v. Marrazzo](#), 848 F.2d 398, 401 (3d Cir. 1988). Documents "integral to or explicitly relied upon in the complaint" and related matters of public record may be considered on a motion to dismiss. [In re Burlington Coat Factory Sec. Litig.](#), 114 F.3d 1410, 1426 (3d Cir. 1997).

### III. DISCUSSION

3M argues that the Complaint should be dismissed pursuant to [Rule 12\(b\)\(6\)](#) because (1) Meijer's claim is barred by the applicable statute of limitations; and (2) the Complaint fails to state a valid claim of antitrust injury.

#### A. Statute of Limitations

3M first argues that this case is time-barred under the applicable statute of limitations. [HN2](#)<sup>↑</sup> The statute of limitations is an affirmative defense, and the burden of establishing its applicability to a particular claim rests with the defendant. [Buskirk v. Carey Canadian Mines, Ltd.](#), 760 F.2d 481, 487 (3d Cir. 1985). [HN3](#)<sup>↑</sup> When considering a motion to dismiss pursuant to [Rule 12\(b\)\(6\)](#) on statute of limitations grounds, "[courts] must [\*7] determine whether the time alleged in the statement of a claim shows that the cause of action has not been brought within the statute of limitations." [Davis v. Grusemeyer](#), 996 F.2d 617, 623 (3d Cir. 1993) (quoting [Cito v. Bridgewater Twp. Police Dept.](#), 892 F.2d 23, 25 (3d Cir. 1989)). The defendant bears a heavy burden in seeking to establish that the challenged claims are barred as a matter of law. [Davis](#), 996 F.2d at 623, n.10 (citing [Buskirk](#), 760 F.2d at 498).

[HN4](#)<sup>↑</sup> The Clayton Act, [15 U.S.C. § 15b](#), which governs private antitrust actions, provides that "any action to enforce any cause of action under [section 15](#), [15a](#), or [15c](#) of this title shall be forever barred unless commenced within four years after the cause of action accrued." [15 U.S.C. § 15b](#). "Generally, a cause of action accrues, and the statute begins to run, when a defendant commits an act that injures a plaintiff's business." [Zenith Radio Corp. v. Hazeltine Research, Inc.](#), 401 U.S. 321, 338, 28 L. Ed. 2d 77, 91 S. Ct. 795 (1971). Meijer, which seeks damages for the period from October 2, 1998 through the present [\*8] based on conduct by 3M which began as early as 1993, does not dispute the applicability of the Clayton Act's four year statute of limitations. Meijer argues, however, that the instant action is timely under the continuing violation and speculative damages exceptions to the four-year accrual rule.

##### 1. Continuing violation exception

Meijer argues that the instant action is timely because 3M's conduct constitutes a continuing violation of the Sherman Act. "The Supreme Court has considered and rejected the argument that, in the context of a defendant's continuing violation of the Sherman Act, the statute of limitations runs from the violation's earliest impact on a plaintiff." [In re Lower Lake Erie Iron Ore Antitrust Litig.](#), 998 F.2d 1144, 1171 (3d Cir. 1993). [HN5](#)<sup>↑</sup> The four year statute of limitations does not bar recovery for later private antitrust actions if the defendant's conduct "constituted a continuing violation of the Sherman Act and . . . inflicted continuing and accumulating harm." [Hanover Shoe, Inc. v. United Shoe Mach. Corp.](#), 392 U.S. 481, 502, n.15, 20 L. Ed. 2d 1231, 88 S. Ct. 2224 (1968). In such situations, even if the overt act which demonstrates [\*9] the antitrust violation occurs outside the statute of limitations period, an injurious act within the limitations period may serve as the basis for a timely antitrust suit. [Lower Lake Erie Iron Ore](#), 998 F.2d at 1172.

Here, Meijer argues that the continuous violation exception should be applied because the predatory and exclusionary practices 3M engaged in outside the limitations period have resulted in continuing and accumulating harm to Meijer within the limitations period by allowing 3M to continue to charge supracompetitive prices for its invisible and transparent tape. Generally, a subsequent act will only preserve an antitrust claim if that act is an "injurious act actually occurring during the limitations period, not merely the abatable but unabated inertial consequence[] of some pre-limitations action." [Al George, Inc. v. Envirotech Corp.](#), 939 F.2d 1271, 1275 (5th Cir. 1991) (quoting [Pace Indus., Inc. v. Three Phoenix Co.](#), 813 F.2d 234, 238 (9th Cir. 1987)) (emphasis deleted); see also [Varner v. Peterson Farms](#), 371 F.3d 1011, 1019 (8th Cir. 2004); [Grand Rapids Plastics, Inc. v. Lakian](#), 188 F.3d 401, 406 (6th Cir. 1999); [\*10] see generally Phillip E. Areeda et al., [Antitrust Law](#), P 320 at 208-211 (2d ed. 2000). [HN6](#)<sup>↑</sup> While a leading commentator has noted that "it should seem that high prices following . . . the

creation of a monopoly are mere inertial consequences one naturally expects to flow from such acts," Areeda P 320 at 210, it has long been held that "a purchaser suing a monopolist for overcharges paid to recovery by pointing to anticompetitive actions taken before the limitations period." [Berkey Photo, Inc. v. Eastman Kodak Co., 603 F.2d 263, 296 \(2d Cir. 1979\)](#). This principle is based on the recognition that

although the business of a monopolist may be injured at the time the anticompetitive conduct occurs, a purchaser, by contrast, is not harmed until the monopolist actually exercises its illicit power to extract an excessive price. The case of predatory pricing illustrates the point clearly. As soon as the dominant firm commences such a policy, other producers, who may be driven out of the market, are injured. But, clearly, purchasers are not, for they receive the temporary boon of artificially low prices. It is only when the monopolist, having devoured its smaller [\*11] rivals, enjoys the spoils of its conquest by boosting its price to excessive levels that a purchaser feels the adverse impact of the violation. And if the monopolist never consummates its scheme by taking this final step, the purchaser has no cause of action.

[Id. at 295](#) (quoting [Zenith, 401 U.S. at 339](#)).

The United States Court of Appeals for the Third Circuit ("Third Circuit") has similarly differentiated between "on the one hand, an 'overt act' necessary to show the existence of a [continuing violation], and, on the other hand, an injurious act causing damages within the limitations period." [Lower Lake Erie Iron Ore, 998 F.2d at 1172](#). Accordingly, courts have held that, [HNT](#) in purchaser antitrust actions, the requisite injurious act within the limitations period can include being overcharged as the result of an unlawful act which took place outside the limitations period but continues to allow the defendant to maintain market control. See [In re K-Dur Antitrust Litig., 338 F. Supp. 2d 517, 551 \(D.N.J. 2004\)](#) (purchasers' antitrust claims "are not barred by the statute of limitations to the extent that they bought [\*12] and overpaid for [defendant's] products within the applicable time limitations"); see also [In re Buspirone Patent & Antitrust Litig., 185 F. Supp. 2d 363 at 365, 378 \(S.D.N.Y. 2002\)](#) ("if a party commits an initial unlawful act that allows it to maintain market control and overcharge customers for a period longer than four years, purchasers maintain a right of action for any overcharges paid within the four years prior to their filings.").

Here, the Complaint alleges that "as found in LePage's or otherwise, 3M's unlawful maintenance of its tape monopoly has suppressed competition and has maintained prices paid by direct purchasers to 3M above competitive levels, even after any 3M rebates attributable to tape purchases." (Compl. P 32.) The Complaint further alleges that "the issues regarding 3M's violation of [Section 2 of the Sherman Act](#) in LePage's v. 3M are identical to those in the case at bar," (*id.* P 37), and that "3M has used its unlawful monopoly power . . . to harm Plaintiffs and other Class members in their business or property by increasing maintaining, or stabilizing the prices they paid for invisible and transparent tape above competitive levels." (*Id.* [\*13] P 34.) The Complaint, therefore, alleges a cause of action on the basis of an initial overt act of unlawful maintenance of monopoly power that occurred more than four years ago, but which continues to allow 3M to commit the injurious act of overcharging Meijer and other purchasers. See [Lower Lake Erie Iron Ore, 998 F.2d at 1172](#); see also [In re K-Dur, 338 F. Supp. 2d at 551](#); [In re Buspirone, 185 F. Supp. 2d at 378](#). Accordingly, the Court concludes that Meijer's claims are not barred by the statute of limitations to the extent that Meijer seeks to recover for any overcharges paid within the four years prior to the filing of the instant Complaint, plus any additional time period during which the statute of limitations may be tolled.<sup>2</sup>

[\*14]

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<sup>2</sup> Although the parties have made some arguments with respect to the possible tolling of the statute of limitations in this case, which would extend the damages time period in this case. The Court notes, however, that it need not decide what the applicable period for the calculation of damages may ultimately be in ruling on the instant Motion. [In re K-Dur, 338 F. Supp. 2d at 551](#). Moreover, Meijer has advised the Court that "there are additional arguments for further tolling," which it did not develop in the submission currently before the Court. (04/04/2005 Tr. at 40.) Accordingly, the Court will defer ruling on the propriety of tolling the statute of limitations at this time.

## 2. Speculative damages exception

Meijer also argues that the statute of limitations does not bar the instant action because Meijer's damages were speculative prior to the filing of the instant lawsuit. [HN8](#)[<sup>15</sup>] The general rule of accrual in antitrust actions provides that "if a plaintiff feels the adverse impact of an antitrust [violation] on a particular date, a cause of action immediately accrues to him to recover all damages incurred by that date and all provable damages that will flow in the future." [Zenith, 401 U.S. at 339](#). The mere fact that damages may continue to accrue "in the future, as opposed to at the from accruing." [Astoria Entm't, Inc. v. Edwards, 159 F. Supp. 2d 303, 316 \(E.D. La. 2001\)](#) (quoting 8 Julian O. van Kalinowski et al., *Antitrust Laws and Trade Regulation* § 162.02[1] at 162-5). However,

it is hornbook law, [HN9](#)[<sup>16</sup>] in antitrust actions as in others, that even if injury and a cause of action have accrued as of a certain date, future damages that might arise from the conduct sued on are unrecoverable if the fact of their accrual is speculative or their amount and nature unprovable. [\*15]

[Zenith, 401 U.S. at 339](#). In these instances, antitrust causes of action for future damages "will accrue only on the date [the damages] are suffered; thereafter the plaintiff may sue to recover them at any time within four years from the date they were inflicted." *Id.*

In purchaser antitrust actions, damages from future overcharges necessarily fall into the speculative damages exception to the four year statute of limitations. See [Berkey Photo, 603 F.2d at 295-96](#). The United States Court of Appeals for the Second Circuit has explained that

plainly, at the time a monopolist commits anticompetitive conduct it is entirely speculative how much damage that action will cause its purchasers in the future. Indeed, some of the buyers who will later feel the brunt of the violation may not even be in existence at the time. Not until the monopolist actually sets an inflated price and its customers determine the amount of their purchases can a reasonable estimate be made. The purchaser's cause of action, therefore, accrues only on the date damages are 'suffered.'

[Berkey Photo, 603 F.2d at 295-96](#) (internal quotations [\*16] omitted.) To hold otherwise would require a purchaser to predict and prove, within four years of the time it was first injured by anticompetitive conduct, the amount of future overcharges, the quantity of future product purchases, the level of future competition in the relevant market, and the availability of substitutes and new suppliers over time. Resolution of these issues depends on overall changes in consumer demand for tape, developments in the purchaser's overall business, variations in the cost of producing the product over time, and the future prices which the supplier ultimately decides to charge. These considerations are too speculative and remote to properly predict a purchaser's future damages. The Court, therefore, finds that Meijer's antitrust claim against 3M could not accrue until it actually payed the overcharge. See [Berkey Photo, 603 F.2d at 295](#).

3M argues that the Court should nonetheless find that Meijer's claims are barred by the statute of limitations, because

repose is especially valuable in antitrust, where tests of legality are often rather vague, where many business practices can be simultaneously efficient and beneficial to consumers [\*17] but also challengeable as antitrust violations, where liability doctrines change and expand, where damages are punitively trebled, and where duplicate treble damages for the same offense may be threatened.

Areeda, P 320a at 205. The Court notes, however, that "there can be no unfairness in preventing a monopolist that has established its dominant position by unlawful conduct from exercising that power in later years to extract an excessive price," because "the . ." [Berkey Photo, 603 F.2d at 296](#). The Court, therefore, concludes that because Meijer's future damages were speculative in 1993, when Meijer was first injured, a new cause of action accrued to Meijer each time it payed an overcharge. See [Berkey Photo, 603 F.2d at 295](#). Accordingly, this action is not barred by the statute of limitations to the extent that Meijer seeks to recover for overcharges during the four years prior to the filing of the instant Complaint, plus any additional time period during which the statute of limitations may be tolled.

### B. Failure to State a Valid Claim of Antitrust Injury

3M also argues that the Complaint should be dismissed pursuant to [Rule 12\(b\)\(6\)](#) [\*18] because it fails to state a valid claim of antitrust injury.

[HN10](#) [↑] To state a claim for monopolization [in violation of [Section 2](#)], a plaintiff must allege "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historical accident."

[Schuylkill Energy Res., Inc. v. Pa. Power & Light Co.](#), 113 F.3d 405, 412-13 (3d Cir. 1997) (quoting [Fineman v. Armstrong World Indus.](#), 980 F.2d 171, 197 (3d Cir. 1992)). The right to maintain a private cause of action for damages arising under [Section 2](#) flows from Section 4 of the Clayton Act, [15 U.S.C. § 15\(a\)](#), which provides that "any person who shall be injured in his business or property by reason of anything forbidden in the Accordingly, plaintiffs bringing a private cause of action under [Section 2](#)

must prove more than injury causally linked to an illegal presence in the market. Plaintiffs must prove antitrust injury, which is to say injury of the type the antitrust laws were intended to prevent and [\*19] that flows from that which makes defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation.

[Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.](#), 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977). The Court notes that [HN11](#) [↑] "the existence of antitrust injury is not typically resolved through motions to dismiss." [Schuylkill Energy](#), 113 F.3d at 417 (citing [Brader v. Allegheny Gen. Hosp.](#), 64 F.3d 869, 876 (3d Cir. 1995)). Moreover, "there are no special pleading requirements for an antitrust claim. Rather, 'notice pleading is all that is required for a valid antitrust complaint.' [Bradburn Parent/Teacher Store, Inc. v. 3M](#), 2003 U.S. Dist. LEXIS 13273, Civ. A. No. 02-7676, 2000 WL 34003597, at \*2 (E.D. Pa. July 25, 2003) (quoting [Mun. Utils. Bd. of Albertville v. Ala. Power Co.](#), 934 F.2d 1493, 1501 (11th Cir. 1991)). Courts, therefore, "must accept as true the factual allegations in the complaint and all reasonable inferences that can be drawn from them." [Schuylkill Energy](#), 113 F.3d at 417. Courts "are not, however, required to accept [\*20] as true unsupported conclusions and unwarranted inferences." *Id.*

Here, 3M argues that the Complaint fails to state a valid claim for antitrust injury because, although the Complaint alleges rebate programs and exclusive dealing arrangements with retailers, "it does not necessarily follow . . . that Meijer or the class it seeks to represent suffered any injury at all because such retailers benefitted directly and significantly from those rebates." (Def. at 18.) The Complaint alleges as follows:

As found in [LePage's](#) or otherwise, 3M's unlawful maintenance of its tape monopoly has suppressed competition and has maintained tape prices paid by direct purchasers to 3M above competitive levels, even after any 3M rebates attributable to tape purchases. . . . 3M has used its unlawful monopoly power described herein to harm [Meijer] and other Class members in their business or property by increasing, maintaining, or stabilizing the prices they paid for invisible and transparent tape above competitive levels.

(Compl. PP 32, 34.) (emphasis added). Moreover, the Complaint alleges that 3M "intended to use, did use, and continues to use" its "anitcompetitive and monopolistic [\*21] practices in the conduct of trade or commerce." (Compl. P 1.) The Court has previously held that these allegations, "if proven, could establish that, were it not for [3M's] anti-competitive conduct, [Meijer] would have paid less for transparent tape than it actually paid during the damages period, even when any bundled rebates or other discounts are taken into account." [Bradburn](#), 2003 U.S. Dist. LEXIS 13273, 2000 WL 34003597, at \*4. The Court, therefore, concludes that Meijer has properly alleged injury of the type the antitrust laws were designed to prevent.<sup>3</sup> Accordingly, 3M's Motion is denied in this respect.

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<sup>3</sup>The Court notes that it is "not in a position to predict whether [Meijer] will ultimately be able to sustain [its] burden of proof on this issue since [Meijer] has not yet had an opportunity to obtain evidence." [Brader](#), 64 F.3d at 876. Accordingly, the sufficiency

[\*22] **ORDER**

**AND NOW**, this 13th day of July, 2005, upon consideration of Defendant 3M's Motion to Dismiss (Doc. No. 9), all documents submitted in response thereto, and the Argument held on April 25, 2005, **IT IS HEREBY ORDERED** that said Motion is **DENIED**.

BY THE COURT:

John R. Padova, J.

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## Olstad v. Microsoft Corp.

Supreme Court of Wisconsin

September 22, 2004, Submitted on Briefs ; July 13, 2005, Opinion Filed

2003AP1086

**Reporter**

2005 WI 121 \*; 284 Wis. 2d 224 \*\*; 700 N.W.2d 139 \*\*\*; 2005 Wisc. LEXIS 393 \*\*\*\*; 2005-2 Trade Cas. (CCH) P74,918

Gene L. Olstad, Individually and on Behalf of All Others Similarly Situated, Plaintiff-Appellant, v. Microsoft Corporation, a foreign corporation, and Does 1 through 100, inclusive, Defendants-Respondents.

**Subsequent History:** Costs and fees proceeding at, Remanded by [Bettendorf v. Microsoft Corp., 2009 Wisc. App. LEXIS 986 \(Wis. Ct. App., Dec. 22, 2009\)](#)

**Prior History:** [\*\*\*\*1] APPEAL from an order of the Circuit Court for Milwaukee County, Jeffrey Kremers, Judge. (L.C. No. 00 CV 3042).

*Olstad v. Microsoft Corp., 2004 WI 50, 271 Wis. 2d 113, 679 N.W.2d 548, 2004 Wisc. LEXIS 404 (2004)*

**Disposition:** Reversed and cause remanded.

## **Core Terms**

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interstate commerce, antitrust, commerce, monopolize, conspiracy, anti trust law, revision, cases, state law, Sherman Act, regulation, attorney general, intrastate, federal statute, circuit court, preempt, courts, intrastate commerce, legislative intent, commerce clause, circumstances, effects, antitrust statute, interstate, preemption, files, restraint of trade, manufacturers, practices, recreated

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Supporting Materials > Discovery Materials

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

**HN1[ Supporting Materials, Discovery Materials**

An appellate court reviews the circuit court's grant of summary judgment independently, applying the same methodology as the circuit court. Summary judgment shall be rendered if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. [Wis. Stat. § 802.08\(2\)](#). The appellate court evaluates the facts in the light most favorable to the nonmoving party and draws all reasonable inferences from the facts in his favor. If the salient facts are undisputed, its task is simply to apply the law to the undisputed facts.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers

## [HN2](#) Public Enforcement, State Civil Actions

A state may regulate interstate commerce in some circumstances. The most important point is that when a practice has sufficient effects within the state, that state has the power to apply its **antitrust law**. A state **antitrust law** of general application can virtually always be applied to a practice having sufficient effects within the state. State law is precluded from regulating interstate commerce only if it "unduly burdens" interstate commerce.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Penalties

## [HN3](#) Public Enforcement, State Civil Actions

See [Wis. Stat. § 133.03](#) (2001-02).

Civil Procedure > Appeals > Standards of Review > De Novo Review

Governments > Legislation > Interpretation

## [HN4](#) Standards of Review, De Novo Review

An appellate court reviews de novo the circuit court's construction of a statute.

Governments > Legislation > Interpretation

**HN5** Legislation, Interpretation

Statutory interpretation begins with the language of the statute. If the meaning of the statute is plain, the court ordinarily stops the inquiry. It assigns the words in the statute their common, ordinary, and accepted meaning. It also considers the context and structure of the statute. It interprets statutes to avoid absurd or unreasonable results and to give effect to every word in the text.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Governments > Legislation > Interpretation

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN6** Monopolies & Monopolization, Actual Monopolization

See [Wis. Stat. § 133.01](#) (2001-02).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Governments > Legislation > Interpretation

**HN7** Public Enforcement, State Civil Actions

[Wis. Stat. § 133.03](#) (2001-02) is ambiguous, in that reasonably well-informed observers have interpreted it in two different senses. The language itself provides no express limit to the statute's scope.

Governments > Legislation > Interpretation

**HN8** Legislation, Interpretation

To resolve an ambiguity in a statute, a court turns to both intrinsic and extrinsic sources, including legislative history, to determine the intent of the legislature.

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers

Constitutional Law > Supremacy Clause > Federal Preemption

Constitutional Law > Supremacy Clause > General Overview

Constitutional Law > Supremacy Clause > Supreme Law of the Land

Transportation Law > Interstate Commerce > Federal Preemption

**HN9** Interstate Commerce, State Powers

The federal constitution is clearly the supreme law of the land. [U.S. Const. art. VI, cl. 2](#). Therefore, a federal law regulating interstate commerce may preempt a state law on the same topic. Federal preemption may occur through express preemption or implied preemption. Congress may expressly preempt contradictory--or even coterminous--

state laws in the text of the laws it passes. In that event, the state laws must yield to the federal law. Congress may also impliedly preempt state laws by completely occupying a given regulatory field. However, if the preemption is only implied, courts typically require clear evidence of legislative intent to preempt. The United States Supreme Court has stated that there is a "strong presumption" against a finding of preemption.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Constitutional Law > Supremacy Clause > General Overview](#)

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

#### **HN10[] Antitrust & Trade Law, Sherman Act**

Congress has neither expressly (in the language of the Sherman Act) nor impliedly attempted to preempt state antitrust laws. Each state can and does prevent and control combinations within the limit of the state. This Congress has not proposed to interfere with. Congress has never expressed the least willingness to limit state antitrust by making federal antitrust occupy the field, thus preempting state law. The result is that federal and state policy often overlap and address precisely the same practices, often with inconsistent results.

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

[Constitutional Law > Supremacy Clause > General Overview](#)

[Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers](#)

[Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview](#)

#### **HN11[] Public Enforcement, State Civil Actions**

The U.S. Supreme Court has acknowledged that state legislation, designed to serve legitimate state interests and applied without discrimination against interstate commerce, does not violate the Commerce Clause even though it affects commerce.

[Antitrust & Trade Law > Public Enforcement > State Civil Actions](#)

[Constitutional Law > Supremacy Clause > General Overview](#)

[Transportation Law > Interstate Commerce > Balancing Tests](#)

[Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview](#)

#### **HN12[] Public Enforcement, State Civil Actions**

States may burden interstate commerce unless the burden is "clearly excessive" in relation to the local benefits.

[Governments > Legislation > Interpretation](#)

#### **HN13[] Legislation, Interpretation**

The Wisconsin Supreme Court has often used legislative declarations as a valuable aid to its analysis of statutes.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **HN14** [+] **Public Enforcement, State Civil Actions**

The Wisconsin Supreme Court concludes that Wis. Stat. ch. 133, particularly [Wis. Stat. § 133.03](#), applies to interstate commerce, at least in some circumstances. Consistent with this holding, it withdraws the language from [Conley Publ'g Group v. Journal Communications, 2003 WI 119, 265 Wis. 2d 128, 665 N.W.2d 879](#), that the scope of Wis. Stat. ch. 133 is limited to intrastate transactions.

Antitrust & Trade Law > Regulated Practices > Monopolies & Monopolization > General Overview

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Double Jeopardy

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Constitutional Law > Bill of Rights > Fundamental Rights > General Overview

#### **HN15** [+] **Regulated Practices, Monopolies & Monopolization**

In some circumstances, a monopolist's conduct is actionable under either federal law, Wisconsin law, or both. This concern is not unique to [antitrust law](#). Concerns about "double jeopardy" prosecutions date back to the adoption of the Bill of Rights.

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Double Jeopardy

#### **HN16** [+] **Procedural Due Process, Double Jeopardy**

See [U.S. Const. amend. V.](#)

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Double Jeopardy

Criminal Law & Procedure > Commencement of Criminal Proceedings > Double Jeopardy > Dual Sovereignty Doctrine

#### **HN17** [+] **Procedural Due Process, Double Jeopardy**

As a general rule, a person is not unconstitutionally subject to double jeopardy when he is tried successively by different sovereigns for the same crime. This rule derives from the more general concept that the states and the federal government are separate sovereigns, each entitled to enforce its own laws. Duplicative prosecution is one thing; duplicative recovery is another. It goes without saying that the courts can and should preclude double recovery by an individual.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN18** [blue checkmark] **Public Enforcement, State Civil Actions**

A civil plaintiff filing an action under Wisconsin's antitrust act must allege that (1) actionable conduct, such as the formation of a combination or conspiracy, occurred within Wisconsin, even if its effects are felt primarily outside Wisconsin; or (2) the conduct complained of "substantially affects" the people of Wisconsin and has impacts in Wisconsin, even if the illegal activity resulting in those impacts occurred predominantly or exclusively outside Wisconsin. Questions of provincialism, favoritism, and undue burden on interstate commerce should be determined by resort to contemporary federal commerce clause jurisprudence.

**Counsel:** For the plaintiff-appellant there were briefs by John F. Maloney and McNally, Maloney & Peterson, S.C., Milwaukee and Ben Barnow and Barnow and Associates, P.C., Chicago, IL, and oral argument by John F. Maloney.

For the defendant-respondent there were briefs by W. Stuart Parsons, Jeffrey Morris, Brian D. Winters, Kelly H. Twigger, and Quarles & Brady LLP, Milwaukee; David B. Tulchin, Jeremy T. Kamras, Ryan C. Williams and Sullivan & Cromwell, LLP, New York, NY; Charles B. Casper and Montgomery, McCracken, Walker & Rhoads LLP, (of counsel), Philadelphia, PA; and Thomas W. Burt, Richard J. Wallis, Steven J. Aeschbacher (of counsel) and Microsoft Corporation, Redmond, WA, and oral argument by David B. Tulchin.

An amicus curiae brief was filed by Stephen E. Meili, Peter C. Carstensen and Susan LaCava and Susan LaCava S.C., Madison, on behalf of the University of Wisconsin Law School Consumer Law [\*\*\*\*2] Litigation Clinic, Professor Peter C. Carstensen of the University of Wisconsin Law School, and Susan LaCava, Esq.

An amicus curiae brief was filed by John J. Prentice, Andrew T. Phillips and Prentice & Phillips, LLP, Milwaukee; Richard M. Hagstrom and Zelle, Hofmann, Voelbel, Mason & Gette LLP, Minneapolis, MN, on behalf of Wisconsin Counties Association.

An amicus curiae brief was filed by H. Dale Peterson and Stroud, Willink & Howard, LLC, Madison; William L. Oemichen, Madison; Gary Bakke and Bakke Norman SC, New Richmond; on behalf of Wisconsin Farm Bureau Federation, Cooperative, Wisconsin Federation of Cooperatives and Wisconsin Agri-Service Association.

An amicus curiae brief was filed by Gerald Thain, University of Wisconsin Law School, Madison, and James May, Washington College of Law/American University of Law School, Washington, D.C., on behalf of the American Antitrust Institute.

An amicus curiae brief was filed by Peggy A. Lautenschlager, attorney general and Eric J. Wilson, assistant attorney general, on behalf of the Wisconsin Department of Justice, and oral argument by Eric J. Wilson.

**Judges:** DAVID T. PROSSER, J. SHIRLEY S. ABRAHAMSON, C.J., and ANN [\*\*\*\*3] WALSH BRADLEY, J., did not participate.

**Opinion by:** DAVID T. PROSSER

## Opinion

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### [\*\*229] ON CERTIFICATION FROM THE COURT OF APPEALS

[\*P1] [\*\*\*141] DAVID T. PROSSER, J. Gene L. Olstad (Olstad), suing individually and as class representative of all others similarly situated, appeals from a final order of the Circuit Court for Milwaukee County granting Microsoft Corporation's (Microsoft) motion for summary judgment and dismissing Olstad's action alleging that Microsoft employs monopolistic practices prohibited by [Wis. Stat. § 133.03](#) (2001-02).<sup>1</sup> The circuit court dismissed Olstad's complaint because it found that [Chapter 133 of the Wisconsin Statutes](#) applies only to intrastate commerce. We reverse the circuit court's order because we conclude that Wisconsin's antitrust statutes may reach interstate

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<sup>1</sup> All subsequent references to the Wisconsin Statutes are to the 2001-02 edition unless otherwise indicated.

commerce if (1) actionable conduct, such as the formation of a combination or conspiracy, occurred within this state, even if its effects are felt primarily outside Wisconsin; or (2) the conduct complained of "substantially affects" the people of Wisconsin and has impacts in this state, even if the illegal activity resulting in those impacts occurred predominantly or exclusively outside this [\*\*\*\*4] state.

## I. FACTS AND PROCEDURAL POSTURE

[\*P2] Olstad, <sup>2</sup> [\*\*\*\*5] seeking to represent a class of Wisconsin consumers,<sup>3</sup> alleges that Microsoft controls a [\*\*230] "dominant and persistent share" of the market for Intel-compatible<sup>4</sup> personal computer operating systems. In 1985 Microsoft introduced its "Windows" operating system. In the following years, Microsoft released newer--and increasingly dominant--versions of Windows. Olstad alleges that Microsoft's Windows market share has "at times exceeded ninety-five percent."

[\*P3] Olstad claims that Microsoft's dominant market share acts as a barrier to entry for would-be competitors. He alleges that Microsoft has created a continuously increasing feedback loop: that is, because "everyone" uses Windows, all new [\*\*\*142] consumers must also buy Windows. In Olstad's view, this feedback loop has become a vicious cycle for consumers. He claims that Microsoft has engaged in various forms of anticompetitive conduct to maintain its monopoly, including actively discouraging competitors from "encroaching upon its operating system monopoly."

[\*P4] In 2000 a United States District Court in the District of Columbia accepted most of these arguments. *United States v. Microsoft Corp.*, 97 F. Supp. 2d 59 (D.D.C. 2000) [\*\*\*\*6] (final judgment); *United States v. Microsoft Corp.*, 87 F. Supp. 2d 30 (D.D.C. 2000) (conclusions of law); *United States v. Microsoft Corp.*, 84 F. Supp. 2d 9 (D.D.C. 1999) (findings of fact). Olstad directs our attention to the District Court's findings for "the details of Microsoft's and its co-conspirators' conduct."

[\*P5] In its "conclusions of law," the District Court found that Microsoft's conduct violated the federal *Sherman Act* "sufficient to meet analogous elements of [\*\*231] causes of action arising under the laws of each plaintiff state," one of which was Wisconsin. *Microsoft*, 87 F. Supp. 2d at 54. Microsoft argued that "a plaintiff cannot succeed in an antitrust claim under the laws of . . . Wisconsin without proving an element that is not required under the Sherman Act, namely, intrastate impact." *Id. at 55*. The court rejected Microsoft's argument, concluding that even if a state like Wisconsin had such a requirement, "that element is manifestly proven by the facts presented here." *Id.* The court was "compelled" to the conclusion that "Microsoft's anticompetitive conduct has substantially hampered competition" [\*\*\*\*7] in Wisconsin. *Id.* Accordingly, the court found that Microsoft violated *Wis. Stat. § 133.03*. *Id. at 56.*

[\*P6] Microsoft appealed, and the United States Court of Appeals for the D.C. Circuit affirmed that part of the District Court's decision holding that Microsoft committed monopoly violations. *United States v. Microsoft Corp.*, 346 U.S. App. D.C. 330, 253 F.3d 34, 51 (D.C. Cir. 2001). The court of appeals remanded the case for further findings on other issues. See *id. at 95.*

[\*P7] Olstad alleges that as a result of Microsoft's anticompetitive conduct, Wisconsin consumers have paid artificially high prices for Microsoft products over the past six years. He argued to the circuit court that Microsoft's

<sup>2</sup>There is a question whether Olstad is a proper class representative. At oral argument, Olstad's counsel asserted that if this court reversed the circuit court's order, he would substitute a new class representative. Because the circuit court ultimately dismissed Olstad's complaint, it never addressed the issue of whether to certify the class. We need not reach the issue for the purposes of determining this appeal.

<sup>3</sup>Olstad asserts that the class consists of "all persons or entities in the State of Wisconsin who purchased for purposes other than re-sale or distribution during the last six years, Microsoft licensed Intel compatible PC operating systems." The class does not include government entities. *Id.*

<sup>4</sup>"Intel" is a brand of microprocessor commonly used in personal computers.

conduct violated [Wis. Stat. § 100.18](#) (prohibiting unfair trade practices) and [Wis. Stat. § 133.03](#) (prohibiting unlawful contracts and conspiracies).

[\*P8] Microsoft denied these allegations and moved for summary judgment. Microsoft noted that it is a foreign corporation, not organized under the laws of Wisconsin, and its principal place of business is [\*\*\*\*8] not in Wisconsin. It is undisputed that most of the conduct complained of occurred outside Wisconsin and affected interstate commerce. Microsoft argued that Wisconsin [\\*\\*232](#) courts have consistently held that Wisconsin's [antitrust law](#), [Chapter 133](#), does not apply to conduct that primarily affects interstate commerce. Microsoft also argued that Olstad failed to state a claim actionable under [Wis. Stat. § 100.18](#).

[\*P9] The Milwaukee County Circuit Court, Jeffrey Kremers, Judge, granted Microsoft's motion and dismissed Olstad's complaint. In an oral ruling, Judge Kremers held that plaintiffs like Olstad could not recover under [Chapter 133](#) because it does not extend to interstate commerce. Judge Kremers relied on a line of cases beginning with [Pulp Wood Co. v. Green Bay Paper & Fiber Co., 157 Wis. 604, 147 N.W. 1058 \(1914\)](#).

[\*P10] Olstad appealed,<sup>5</sup> and the court of appeals certified the following issue to this [\\*\\*\\*\\*143](#) court: "Does Wisconsin's antitrust act, [Wis. Stat. § 133.03](#), apply to interstate commerce affecting Wisconsin commerce?" We accepted the certification.

[\*P11] [\*\*\*\*9] In this appeal we are not concerned with the truth or merit of Olstad's allegations. The circuit court did not address the substance of the claim that Microsoft violated [Chapter 133](#). The circuit court concluded that controlling precedent did not allow it to consider whether [Chapter 133](#) had been violated because, as a threshold matter, the statute could not apply to the interstate conduct at issue. Accordingly, we must decide whether the Wisconsin statute reaches interstate commerce.

[\*P12] [HN1](#) We review the circuit court's grant of summary judgment independently, applying the same methodology [\\*\\*233](#) as the circuit court. [Smaxwell v. Bayard, 2004 WI 101, P12, 274 Wis. 2d 278, 682 N.W.2d 923](#). Summary judgment "shall be rendered if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." [Wis. Stat. § 802.08\(2\)](#). We evaluate the facts in the light most favorable to the nonmoving party, Olstad, and draw all reasonable inferences from the facts in [\\*\\*\\*\\*10](#) his favor. [Garcia v. Mazda Motor of America, 2004 WI 93, P4 n.3, 273 Wis. 2d 612, 682 N.W.2d 365](#). If, as here, the salient facts are undisputed, our task is simply to apply the law to the undisputed facts.

## II. DISCUSSION

[\*P13] We note at the outset that Microsoft concedes that [HN2](#) a state may regulate interstate commerce in some circumstances. This point is well settled. See, e.g., [California v. ARC America Corp., 490 U.S. 93, 101-02, 104 L. Ed. 2d 86, 109 S. Ct. 1661 \(1989\)](#) (state laws may reach interstate commerce in indirect purchaser action); David Lamb, [Avoiding Impotence: Rethinking the Standards for Applying State Antitrust Laws to Interstate Commerce, 54 Vand. L. Rev. 1705, 1721 \(2001\)](#) ("Most recent decisions have upheld state antitrust regulations despite their incidental impact on interstate commerce"); Herbert Hovenkamp, [State Antitrust in the Federal Scheme, 58 Ind. L.J. 375, 386-87 \(1983\)](#) ("applications of state antitrust laws to situations 'in or affecting' interstate commerce have rarely been condemned and nearly all cases that did condemn such applications were decided before 1935, [\\*\\*234](#) when judges had a much more [\\*\\*\\*\\*11](#) restrictive view of the power of the states to regulate in interstate commerce").

[\*P14] "The most important point is that when a practice has sufficient effects within the state, that state has the power to apply its [antitrust law](#) . . . a state [antitrust law](#) of general application can virtually always be applied to a practice having sufficient effects within the state." Hovenkamp, [Antitrust Law](#), P2403a (2d ed. 2000). State law is

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<sup>5</sup> Olstad decided not to pursue the circuit court's dismissal of his claim under [Wis. Stat. § 100.18](#), because he did not brief that issue to this court. Accordingly, we address only the issue certified by the court of appeals.

precluded from regulating interstate commerce only if it "unduly burdens" interstate commerce. Von Kalinowski, Antitrust Laws & Trade Regulation § 100.03 (2d ed. 2004).

[\*P15] While conceding that Wisconsin may enact a statute reaching interstate commerce, Microsoft contends that our legislature has not done so. We turn to Wisconsin's antitrust act, [Wis. Stat. § 133.03](#), to determine whether Microsoft is correct.

#### [\*\*\*144] A. Statutory Analysis

[\*P16] At issue is [Wis. Stat. § 133.03](#), which provides:

133.03 Unlawful contracts; conspiracies. (1) [HN3](#)<sup>6</sup> Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce [\*\*\*\*12] is illegal. Every person who makes any contract or engages in any combination or conspiracy in restraint of trade or [\*\*235] commerce may be fined not more than \$ 100,000 if a corporation, or, if any other person, may be fined not more than \$ 50,000 or imprisoned for not more than 7 years and 6 months or both.

(2) Every person who monopolizes, or attempts to monopolize, or combines or conspires with any other person or persons to monopolize any part of trade or commerce may be fined not more than \$ 100,000 if a corporation, or, if any other person, may be fined not more than \$ 50,000 or imprisoned for not more than 7 years and 6 months or both.

[Wis. Stat. § 133.03](#).<sup>6</sup>

[\*P17] [HN4](#)<sup>7</sup> This court reviews de novo the circuit court's construction of the statute. [State v. Lombard, 2004 WI 95, P17, 273 Wis. 2d 538, 684 N.W.2d 103](#). [\*\*\*\*13]

[\*P18] [HN5](#)<sup>8</sup> Statutory interpretation begins with the language of the statute. If the meaning of the statute is plain, we ordinarily stop the inquiry. [Kalal v. Circuit Court for Dane County, 2004 WI 58, P45, 271 Wis. 2d 633, 681 N.W.2d 110](#). We assign the words in the statute their common, ordinary, and accepted meaning. *Id.* We also consider the context and structure of the statute. *Id.*, [P46](#). We interpret statutes to avoid absurd or unreasonable results and to give effect to every word in the text. *Id.*

[\*P19] Olstad argues that the plain language of the statute shows that it applies to interstate commerce because of the absence of any language expressly limiting the scope of the statute. On its face, the statute refers to "every contract," "any contract," and "every person" without restricting its purview to Wisconsin contracts or persons in Wisconsin. [Wis. Stat. § 133.03](#).

[\*P20] Olstad also directs our attention to the context of the statute, namely, the expression of legislative intent in [Wis. Stat. § 133.01](#):

[HN6](#)<sup>9</sup> [\[\\*\\*236\]](#) The intent of this chapter is to safeguard the public against the creation or [\*\*\*\*14] perpetuation of monopolies and to foster and encourage competition by prohibiting unfair and discriminatory business practices which destroy or hamper competition. It is the intent of the legislature that this chapter be interpreted in a manner which gives the most liberal construction to achieve the aim of competition. It is the intent of the legislature to make competition the fundamental economic policy of this state and, to that end, state regulatory agencies shall regard the public interest as requiring the preservation and promotion of the maximum level of competition in any regulated industry consistent with the other public interest goals established by the legislature.

[Wis. Stat. § 133.01](#).

<sup>6</sup>The legislature revised this statute effective February 1, 2003, to alter its penalty provisions. The revision is not material to this appeal and we will not address it further. See 2001 Wis. Act 109.

[\*P21] Microsoft does not address the broad language of [Wis. Stat. § 133.03](#). Instead it relies on several cases that, it claims, interpret the statute's plain language to apply only to purely intrastate conduct. Microsoft then quotes [Zimmerman v. Wisconsin Electric Power Co., 38 Wis. 2d 626, 633-34, \\*\\*\\*145L-157 N.W.2d 648 \(1968\)](#), to the effect that:

It has often been said that once a construction has been [\*\*\*\*15] given to a statute, the construction becomes part of the statute; and it is within the province of the legislature alone to change the law.

. . . Where a law passed by the legislature has been construed by the courts, legislative acquiescence in or refusal to pass a measure that would defeat the courts' construction is not an equivocal act. The legislature is presumed to know that in absence of its changing the law, the construction put upon it by the courts will remain unchanged.

Microsoft asserts that the judicial gloss this court has placed on the language of [Wis. Stat. § 133.03](#) unambiguously [\*\*237] shows that the statute can be applied only to purely intrastate commerce.

[\*P22] The evidence to support Microsoft's argument begins with [Pulp Wood](#). This was also the case principally relied upon by the circuit court. In [Pulp Wood](#), the court evaluated an allegedly illegal contract made in Wisconsin involving a wood supply from Wisconsin, Minnesota, Michigan, and Canada. [Pulp Wood, 157 Wis. at 615](#). The court stated: "The contract we think involved interstate commerce, and if so the federal statute is applicable and the case will [\*\*\*\*16] be treated on that basis." [Id. at 615](#). However, the court noted that it observed "little difference" whether the state or federal statute or both applied. [Id. at 616](#). It added that the state statute "is a copy of the federal statute, except that it applies to attempts to monopolize trade and commerce within the state . . ." [Id. at 625](#).<sup>7</sup>

[\*P23] Most of our cases since [Pulp Wood](#) have followed its bright line division between interstate [\*\*\*\*17] commerce (governed by the federal statute) and intrastate commerce (governed by [Chapter 133](#)) without further analysis. See, e.g., [Pulp Wood Co. v. Green Bay Paper & Fiber Co., 168 Wis. 400, 404-05, 170 N.W. 230 \(1919\)](#) ([Pulp Wood II](#)) ("The contract in question involved interstate commerce, and hence the federal statute is the statute to be applied to the case, although little, if any, difference is to be observed in the result in [\*\*238] the present case whether the state or the federal statutes, or both, apply"); [State v. Lewis & Leidersdorf Co., 201 Wis. 543, 549, 230 N.W. 692 \(1930\)](#) ("sec. [133.01](#) [has] application to intrastate as distinguished from interstate transactions"); [Reese v. Assoc. Hosp. Serv., Inc., 45 Wis. 2d 526, 532, 173 N.W.2d 661 \(1970\)](#) ("Sec. [133.01](#) . . . has been held by this court to be a reenactment of the first two sections of the federal Sherman Antitrust Act, with application to intrastate as distinguished from interstate transactions"); [John Mohr & Sons, Inc. v. Jahnke, 55 Wis. 2d 402, 410, 198 N.W.2d 363 \(1972\)](#) (same); [Grams v. Boss, 97 Wis. 2d 332, 346, 294 N.W.2d 473 \(1980\)](#) [\*\*\*\*18] (same); [Conley Publ'g Group v. Journal Communications, 2003 WI 119, P16, 265 Wis. 2d 128, 665 N.W.2d 879](#) ("the scope of [Chapter 133](#) is limited to intrastate transactions"). Microsoft emphasizes the importance of [Grams](#) and [Conley Publishing](#) because both were decided after a 1980 revision of [Chapter 133](#).

[\*P24] There are two notable exceptions to this line of cases. In [State v. Allied Chemical & Dye Corp., 9 Wis. 2d 290, 101 N.W.2d 133 \(1960\)](#), the court evaluated the circuit court's grant of summary judgment to three defendant corporations. The court reversed, concluding that even though the acts at issue involved interstate commerce and none of the defendants owned, operated, or maintained "any manufacturing plant, sales or other office, warehouse, or stock of calcium chloride in the state of Wisconsin," [Chapter 133](#) could apply. [Id. at 292, 296](#). Without elaboration, the court held:

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<sup>7</sup> In its decision, the court did not declare the contract void. It remanded the case to the circuit court for Brown County. [Pulp Wood Co. v. Green Bay Paper & Fiber Co., 157 Wis. 604, 625, 147 N.W. 1058 \(1914\)](#). The case was tried to the court, which dismissed the complaint on the ground that the contract was void "because [the contract was] contrary to both the federal and state anti-trust statutes." [Pulp Wood Co. v. Green Bay Paper & Fiber Co., 168 Wis. 400, 402, 170 N.W. 230 \(1919\)](#).

1. There is no language in the federal enactments that pre-empts the field of regulation and enforcement in the federal government or that precludes the states from enacting effective legislation dealing with such unlawful practices. [\*\*\*\*19]

[\*\*239] 2. There is no conflict between the federal and state statutes.

3. The Wisconsin statutes make no attempt to regulate or burden interstate commerce.

*Id. at 295.*

[\*P25] The Allied Chemical court also concluded that "The public interest and welfare of the people of Wisconsin are substantially affected if prices of a product are fixed or supplies thereof are restricted as the result of an illegal combination or conspiracy. The people of Wisconsin are entitled to the advantages that flow from free competition . . ." *Id.* The briefs in Allied Chemical permit no doubt that our court was challenged by the Department of Justice to apply Wisconsin's antitrust statute to interstate commerce, and it did.<sup>8</sup>

[\*P26] [\*\*\*20] [\*\*240] In State v. Milwaukee Braves, Inc., 31 Wis. 2d 699, 144 N.W.2d 1 (1966), the court addressed the departure from Wisconsin of the Milwaukee Braves baseball club. The State charged that major league baseball unlawfully practiced monopolistic conduct in violation of Chapter 133. *Id. at 702*. Despite the interstate nature of major league baseball, the court appeared willing to apply Wisconsin's antitrust statute, noting:

[Major League Baseball] terminated very substantial business activity in Wisconsin . . . On their face, these facts support a conclusion that there is a combination or conspiracy in restraint of trade and commerce, declared illegal by the first sentence of sec. 133.01, Stats., as well as a combination to monopolize trade, under the third sentence of the section.

....

[\*\*\*147] The state may, ordinarily, protect the interests of its people by enforcing its antitrust act against persons doing business in interstate commerce . . . (citing Allied Chemical, 9 Wis. 2d at 295.

*Id. at 713-14, 721.*<sup>9</sup>

<sup>8</sup> In its brief, the State argued that even though the respondent corporations were "undoubtedly engaged in interstate commerce, they are subject to prosecution for violating the applicable Wisconsin Statutes by conspiring to fix and control the prices at which other defendants" in Milwaukee sold calcium chloride to Milwaukee County. The State quoted Leader Theatre Corp. v. Randforce Amusement Corp., 186 Misc. 280, 58 N.Y.S.2d 304, 307 (1945): "It is now well established that states, under their police powers, can enact and implement legislation which affects interstate commerce, when such commerce has significant local consequences." The State summed up: "While there is no denying that the respondents are engaged in interstate commerce and that all of the calcium chloride sold in Wisconsin is shipped in interstate commerce, significant and necessary parts of this conspiracy are alleged to have been carried out in [Wisconsin], concern this state and are within the jurisdiction of our courts."

The three chemical companies answered: "After the calcium chloride leaves the producing point no employee or agent of the respondent handles or has any contact with it." The corporations continued: "A corporation engaged in interstate commerce may, of course, be subject to state antitrust laws for violations which occur in connection with transactions which are wholly intrastate." (Emphasis added.)

The focused argument by the parties in State v. Allied Chemical & Dye Corp., 9 Wis. 2d 290, 101 N.W.2d 133 (1960), put the court's decision in context.

<sup>9</sup> In his dissenting opinion, Justice Nathan Heffernan wrote:

It is well settled that a state may exercise its police powers through such devices as the antitrust laws even though an incidental benefit may be to local commerce, providing that the law or its operation do not discriminate against interstate commerce or disrupt its required uniformity. There is no intimation . . . that the Wisconsin antitrust laws are applied in a

[\*P27] [\*\*\*\*21] [\*\*241] The Milwaukee Braves court declined to enforce Chapter 133 in part because of major league baseball's well-settled exception from the antitrust laws. *Id.* at 725. But all seven members of the court asserted that Chapter 133 could be applied to interstate commerce.

[\*P28] Taking this authority into account, we conclude that Chapter 133 has been interpreted inconsistently. Wisconsin Stat. § 133.03 is HNT<sup>1</sup> ambiguous, in that reasonably well-informed observers have interpreted it in two different senses. The language itself provides no express limit to the statute's scope, but this court ascribed a limit to the statute as recently as 2003. Conley Publ'g, 2003 WI 119, 265 Wis. 2d 128, P16, 665 N.W.2d 879. HN8<sup>2</sup> To resolve this ambiguity, we turn to both intrinsic and extrinsic sources, including legislative history, to determine the intent of the legislature. Kalal, 2004 WI 58, 271 Wis. 2d 633, PP43, 50.

## B. Legislative History

[\*P29] The late nineteenth century saw the birth and growth of the earliest antitrust laws, a genesis that took place against a backdrop dominated by principles of dual federalism [\*\*\*\*22] dating back to the Founding Era. Cf. [\*\*242] James May, Antitrust Practice and Procedure in the Formative Era: The Constitutional and Conceptual Reach of State Antitrust Law, 1880-1918, 135 U. Pa. L. Rev. 495, 497-99, 518 (1987). The Wisconsin Legislature enacted Wisconsin's antitrust act in 1893. See ch. 219, Laws of 1893. It did not act in a vacuum. It was influenced by the constraining boundaries of federal commerce clause jurisprudence.

[\*P30] Article I, Section 8, clause 3 of the federal constitution gives Congress the power "to regulate commerce with foreign nations, and among the several states, and with the Indian tribes." U.S. Const., art. I § 8 cl.3. The Supreme Court's early cases made clear that this "commerce clause" also has a negative or "dormant" form restricting the states' ability to regulate interstate commerce. Quill Corp. v. North Dakota, 504 U.S. 298, 309, 119 L. Ed. 2d 91, 112 S. Ct. 1904 (1992) (citing Gibbons v. Ogden, 22 U.S. 1, 231-232, 239, 6 L. Ed. 2d 23 (1824) (Johnson, J., concurring) ("It would be in vain to deny the possibility of a clashing and collision between the measures of the two governments. . . . When [a \*\*\*\*23] collision] does arise, the question must be decided how far the powers of Congress are adequate to put it down.")).

[\*P31] Chief Justice Marshall shaped early conceptions of the role of the national government. "If any one proposition could command the universal assent of mankind we might expect it would be this--that the government of the Union, though limited [\*\*\*\*148] in its powers, is supreme within its sphere of action." McCulloch v. Maryland, 17 U.S. 316, 405, 4 L. Ed. 579 (1819). Marshall believed that the federal government could employ any means not expressly prohibited to it as long as it acted within the "sphere of its specified powers." *Id.* at 384. In so holding, the Court implied that the states, too, are sovereign within their spheres of influence.

[\*P32] [\*\*243] Marshall's concept of mutually exclusive spheres of influence dominated judicial analysis throughout most of the nineteenth century. "It is unquestionably no easy task to . . . fix the precise point, in relation to every important article, where the paramount power of Congress terminates, and that of the State begins." Thurlow v. Massachusetts, 46 U.S. 504, 514, 12 L. Ed. 256 (1847) [\*\*\*\*241] (Opinion of Taney, C.J. <sup>10</sup>).

[\*P33] During the latter half of the nineteenth century, the concept of "spheres of influence" attained nearly impregnable status as black letter law. "The general government, and the States, although both exist within the same territorial limits, are separate and distinct sovereignties, acting separately and independently of each other, within their respective spheres." The Collector v. Day, 78 U.S. 113, 124, 20 L. Ed. 122 (1870).

discriminatory manner. It is equally clear that state antitrust laws can be enforced concurrently with, or in the absence of, federal regulation.

State v. Milwaukee Braves, Inc., 31 Wis. 2d 699, 739, 144 N.W.2d 1 (1966) (Heffernan, Hallows, and Beifuss, JJ., dissenting) (internal citations omitted).

<sup>10</sup> In Thurlow v. Massachusetts, 46 U.S. 504, 12 L. Ed. 256 (1847), popularly known as "The License Cases," the Court did not file a majority opinion; each Justice concurred separately.

[\*P34] Shortly before the passage of the federal Sherman Act, the Court pronounced that "no state has the right to lay a tax on interstate commerce in any form." [Leloup v. Port of Mobile](#), 127 U.S. 640, 648, 32 L. Ed. 311, 8 S. Ct. 1380 (1888). The court believed that such a tax would be a "burden" on interstate commerce, [\*\*\*\*25] regulation of which "belongs solely to congress." *Id.* To put it in Marshall's terms, the Court believed that interstate commerce fell within the "sphere" of federal power, to the total exclusion of state power. [McCulloch, 17 U.S. at 384](#).

[\*P35] **Antitrust law** was born in this era of mutually exclusive sovereignties. At least 13, and possibly as many as 21, states acted before Congress passed the Sherman Act. Compare [ARC America, 490 U.S. at 101 n.4](#), with [May, supra at 499](#). Wisconsin was not one of these states.

[\*P36] [\*\*244] In 1890 Congress passed the Sherman Act. It provided:

- (1) Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. . . .
- (2) Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, [\*\*\*\*26] or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.
- ....
- (8) That the word "person," or "persons," wherever used in this act shall be deemed to include corporations and associations existing under or authorized by the laws of either the United States, the laws of any of the Territories, the laws of any State, or the laws of any foreign country.

[\*\*\*149] Sherman Antitrust Act, ch. 647 §§ 1-8, 26 Stat. 209 (1890) (codified as amended at [15 U.S.C. §§ 1-7 \(2000\)](#)).

[\*P37] Although the passage of a federal statute so similar to then existing state laws--and so similar to the state laws passed shortly thereafter--raises the specter of federal preemption, the legislative history reveals that Congress did not intend to preempt state laws. See Hovenkamp, **Antitrust Law** § 2401a, at 290 (2d ed. 2000). Rather, in accord with the dominating theory of the era, Congress intended the federal law to apply only to interstate cases while the state laws continued to apply to intrastate cases. [See id.](#)

[\*P38] [\*\*245] **HN9** The federal constitution is clearly "the supreme law of the land." [U.S. Const. art. VI, cl. 2](#). Therefore, [\*\*\*\*27] a federal law regulating interstate commerce may preempt a state law on the same topic. Federal preemption may occur through express preemption or implied preemption. [Gorton v. Am. Cyanamid Co.](#), 194 Wis. 2d 203, 215-16, 533 N.W.2d 746 (1995). Congress may expressly preempt contradictory--or even coterminous--state laws in the text of the laws it passes. In that event, the state laws must yield to the federal law. Congress may also impliedly preempt state laws by completely occupying a given regulatory field. *Id.* However, if the preemption is only implied, courts typically require clear evidence of legislative intent to preempt. [Id. at 216](#). In a similar vein, the United States Supreme Court has stated that there is a "strong presumption" against a finding of preemption. [Id. at 219](#) (citing [Cipollone v. Liggett Group, 505 U.S. 504, 523, 120 L. Ed. 2d 407, 112 S. Ct. 2608 \(1992\)](#)).

[\*P39] But **HN10** Congress has neither expressly (in the language of the Sherman Act) nor impliedly attempted to preempt state antitrust laws. See [ARC America, 490 U.S. at 102](#) (citing [Watson v. Buck, 313 U.S. 387, 403, 85 L. Ed. 1416, 61 S. Ct. 962 \(1941\)](#)); [\*\*\*\*28] [Puerto Rico v. Shell Co., 302 U.S. 253, 259-60, 82 L. Ed. 235, 58 S. Ct. 167 \(1937\)](#)). Before the passage of the Sherman Act, its sponsor, Senator John Sherman of Ohio, stated: "Each state can and does prevent and control combinations within the limit of the state. This we do not propose to interfere with." 21 Cong. Rec. 2456, 2460. In fact, "Congress has never expressed the least willingness to limit state antitrust by making federal antitrust 'occupy the field,' thus preempting state law. The result is that federal and state policy often overlap and address [\*\*246] precisely the same practices, often with inconsistent results." Hovenkamp, **Antitrust Law**, P216 (2d ed. 2000).

[\*P40] We discuss preemption only for the sake of completeness, as Microsoft has not argued that the Sherman Act preempts Wisconsin's antitrust laws.

[\*P41] Three years after the passage of the Sherman Act, the Wisconsin Legislature enacted its own antitrust act. See ch. 219, Laws of 1893. The 1893 law provided:

(1) Every contract or combination in the nature of a trust or conspiracy in restraint of trade or commerce, is hereby declared illegal.

(2) Every person who shall monopolize, or attempt [\*\*\*\*29] to monopolize, or combine, or conspire with any other person or persons to monopolize any part of the trade or commerce in this state, shall be deemed guilty of violating the provisions of this act, and upon conviction thereof shall forfeit for each such violation not less than fifty dollars, nor more than three thousand dollars . . .

. . .

(8) The word "person" or "persons," wherever used in this act, shall be deemed to include corporations, partnerships, [\*\*\*150] individuals and associations existing under or authorized by the laws of the United States, the laws of any of the territories, the laws of this or any other state, or the laws of any foreign country.

Ch. 219, Laws of 1893 (codified at Wis. Stat. § 1747e (1898)) (emphasis added).

[\*P42] Comparison of the language and structure of the Sherman Act and Wisconsin's antitrust act reveals many similarities. The pivotal language in the first two sections is nearly identical. This has led courts [\*\*247] and commentators to refer to that first incarnation of Wisconsin's antitrust act as the "Little Sherman Act." See, e.g., Conley Publ'g, 2003 WI 119, 265 Wis. 2d 128, P18, 665 N.W.2d 879.

[\*P43] The dawn of the twentieth century [\*\*\*\*30] coincided with the heyday of the federal "trust-busters" led by President Theodore Roosevelt. See Marc Winerman, The Origins of the FTC: Concentration, Cooperation, Control and Competition, 71 Antitrust L.J. 1, 16 (2003);<sup>11</sup> see generally Edwin J. Hughes, The Left Side of Antitrust: What Fairness Means and Why It Matters, 77 Marq. L. Rev. 265, 292 (1994). The early twentieth century presidents implemented policies favoring broad application of the Sherman Act--and furthered the stratification of the state and federal antitrust laws. See generally Hughes, 77 Marq. L. Rev. at 292 (noting that in 1912, Woodrow Wilson made attacks on trusts one of the centerpieces of his successful presidential campaign).

[\*P44] [\*\*\*\*31] By 1914 antitrust regulation was "most prominent as a political issue." Id. This court's 1914 holding in Pulp Wood is best understood in light of the dominant conception of the time, fathered by Chief Justice Marshall, that the federal government and the various state governments existed in mutually exclusive spheres, with no overlap. See McCulloch, 17 U.S. at 405. As the Pulp Wood court expressed it: "The contract we think involved interstate commerce, and if so the federal statute is applicable and the case will be treated on that basis." Pulp Wood, 157 Wis. at 615. That determination reflected the outlook of the era, even [\*\*248] though the disputed contract was made in Wisconsin and its effects were felt in Wisconsin.

[\*P45] In 1921 the Wisconsin Legislature undertook the first significant revision to the 1893 act. Ch. 458, Laws of 1921. The legislature chose to "amend and renumber" the first section of the statute. Id. The new section stated:

Every contract or combination in the nature of a trust or conspiracy in restraint of trade or commerce is hereby declared illegal. Every combination, conspiracy, trust, [\*\*\*\*32] pool, agreement or contract intended to restrain or prevent competition in the supply or price of any article or commodity in general use in this state, to be produced or sold therein or constituting a subject of trade or commerce therein, or . . . in any manner control the price of any such article or commodity . . . manufactured, mined, produced or sold in this state, or fix any standard or figure in which its price to the public shall be in any manner controlled or established, is hereby

<sup>11</sup> Roosevelt's predecessor, William McKinley, had initiated only three antitrust cases in four years of his presidency; Roosevelt initiated 45 cases during his eight years in office. Marc Winerman, The Origins of the FTC: Concentration, Cooperation, Control and Competition, 71 Antitrust L.J. 1, 16 (2003).

declared an illegal restraint of trade. Every person, corporation, copartnership, trustee or association who shall . . . monopolize or attempt to monopolize any part of the trade or commerce in this state shall forfeit for each offense not less than one hundred dollars nor more than five thousand [\*\*\*151] dollars. Any such person . . . shall also be liable to any person transacting or doing business in this state for all damages he may sustain by reason of the doing of anything forbidden by this section.

Id. (emphasis added). The amendment is notable not because it made major substantive changes to the law, but because of its repeated use of the phrase "in this state." <sup>12</sup> [\*\*\*33] The phrase had appeared once in the 1893 legislation that copied the Sherman Act. The sentence [\*\*249] from the Sherman Act, "Every person who shall . . . conspire . . . to monopolize any part of the trade or commerce among the several States," was changed in the Wisconsin legislation to read, "Every person who shall . . . conspire . . . to monopolize any part of the trade or commerce in this state." Although, in hindsight, the language could have been interpreted to focus on the place where the effects of a conspiracy were felt as opposed to the place where the conspiracy was hatched, this does not appear to have been the initial interpretation. Consequently, the addition of three more "in this state" phrases to the section was not inconsequential. It must be noted, however, that the phrase "in this state" is linked to the word "sold," meaning that it could distinguish the manufacture or production of an article from its sale.

[\*P46] [\*\*\*34] As the twentieth century unfolded, this court formally adhered to Pulp Wood. See, e.g., Pulp Wood II, 168 Wis. at 404-05; Lewis & Leidersdorf Co., 201 Wis. at 549. But the face of federalism was changing. The line between Chief Justice Marshall's mutually exclusive spheres of influence began to blur, as noted by the United States Supreme Court's decision in H.P. Hood & Sons, Inc. v. DuMond, 336 U.S. 525, 93 L. Ed. 865, 69 S. Ct. 657 (1949), in which the Court recognized "broad power in the State to protect its inhabitants against perils to health or safety, fraudulent traders and highway hazards even by use of measures which bear adversely on interstate commerce." Id. at 531-32 (citations omitted).

[\*P47] By 1978 the erosion of Marshall's "spheres of influence" concept was complete. In Raymond Motor Transportation, Inc. v. Rice, 434 U.S. 429, 54 L. Ed. 2d 664, 98 S. Ct. 787 (1978), HN11[] the Court acknowledged that "state legislation, designed to serve legitimate state interests and applied without [\*\*250] discrimination against interstate commerce, does not violate the Commerce Clause even though it affects commerce. [\*\*\*35] " Id. at 440.

[\*P48] The Rice Court characterized the process of evaluating a state law under the dormant commerce clause as one of "delicate adjustment" and announced a balancing test, believing that "no single conceptual approach identifies all of the factors that may bear upon a particular case." Id. at 440-41. The Court framed the inquiry as a balance between the state regulatory concern and the burden imposed on interstate commerce.

[\*P49] The Court elaborated on the test courts should use to determine whether a state law unduly burdens interstate commerce:

The general rule that emerges can be phrased as follows: Where the statute regulates evenhandedly to effectuate a legitimate local public interest, and its effects on interstate commerce are only incidental, it will be upheld unless the burden imposed on such commerce is [\*\*\*152] clearly excessive in relation to the putative local benefits. If a legitimate local purpose is found, then the question becomes one of degree. And the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as [\*\*\*36] well with a lesser impact on interstate activities.

Id. at 441-42 (quoting Pike v. Bruce Church, Inc., 397 U.S. 137, 142, 25 L. Ed. 2d 174, 90 S. Ct. 844 (1970) (internal citations omitted)).

[\*P50] This "delicate" balancing test, expressing the Court's view of the commerce clause in 1978, is dramatically different from the rigid interpretation of the same clause in the late nineteenth century.

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<sup>12</sup> The Legislature also made minor changes to what is now Wis. Stat. § 133.03 in 1923, 1945, 1947, 1957, 1969, and 1975.

[\*P51] In 1980 the Wisconsin Legislature repealed and recreated Chapter 133 of the statutes. Ch. 209, [\*\*251] Laws of 1979. As in 1893, it did not act in a vacuum. When it recreated this chapter, the legislature acted in an entirely different era of commerce clause jurisprudence than at the time of the law's original passage.

[\*P52] By 1980 the United States Supreme Court had clearly abandoned the notion that there might be a "precise point, in relation to every important article, where the paramount power of Congress terminates, and that of the State begins." [Thurlow, 46 U.S. at 514](#). That view had been replaced by the Court's new perception that [HN12↑](#) states could burden interstate commerce unless the burden was "clearly excessive" in relation [\*\*\*37] to the local benefits. See [Rice, 434 U.S. at 441-42](#).

[\*P53] Conversely, the Supreme Court had approved federal legislation under the commerce clause that might, in an earlier era, have been considered regulation of intrastate commerce. In [Heart of Atlanta Motel, Inc. v. United States, 379 U.S. 241, 13 L. Ed. 2d 258, 85 S. Ct. 348 \(1964\)](#), the Court's analysis was revealing:

It is said that the operation of the motel here is of a purely local character. But, assuming this to be true, "if it is interstate commerce that feels the pinch, it does not matter how local the operation which applies the squeeze." [United States v. Women's Sportswear Mfrs. Ass'n, 336 U.S. 460, 464, 93 L. Ed. 805, 69 S. Ct. 714 \(1949\)](#). As Chief Justice Stone put it in [United States v. Darby \[312 U.S. 100, 118, 85 L. Ed. 609, 61 S. Ct. 451 \(1941\)\]](#):

The power of Congress over interstate commerce is not confined to the regulation of commerce among the states. It extends to those activities intrastate which so affect interstate commerce or the exercise of the power of Congress over it as to make regulation of them appropriate means to the attainment of a legitimate end, the [\*\*\*38] exercise of the granted power of Congress to regulate [\*\*252] interstate commerce. See [[McCulloch v. Maryland, 17 U.S. 316, 4 Wheat. 316, 421, 4 L. Ed. 579](#)].  
....

Thus the power of Congress to promote interstate commerce also includes the power to regulate the local incidents thereof, including local activities in both the States of origin and destination, which might have a substantial and harmful effect upon that commerce. ....

[Id. at 258](#) (internal citation omitted).

[\*P54] If a state were to confine itself to the regulation of what remained as purely intrastate commerce after [Heart of Atlanta Motel](#), it would not be regulating much.

[\*P55] Against this new backdrop, the legislature recreated Chapter 133. Microsoft discounts the significance of the 1980 legislation, arguing that the legislature "did not intend to alter the long-standing [\*\*\*153] interpretation of the act." After careful review, however, we think the 1980 action leaves little doubt of the legislature's intent to apply the Wisconsin antitrust statute to interstate commerce.

[\*P56] First, 1979 Assembly Bill 831, which led to 1979 Act 209, was introduced "by request [\*\*\*39] of Attorney General Bronson C. La Follette." Representative Mary Lou Munts, the principal Assembly author, had introduced a bill to repeal and recreate Chapter 133 in 1977. See 1977 A.B. 685. It proved to be very controversial and did not pass. Her legislation was revised for the 1979 session with the help of the Wisconsin Department of Justice, and the new version was given the official imprimatur of the Attorney General. In testimony on the 1979 bill, Representative Munts said: "I am very pleased to have been involved with the Justice Department in the effort to revise Chapter 133, the [\*\*253] Wisconsin Statute on Trusts and Monopolies. We are indebted to the work of the Attorney General's office for the basic revision and to a number of attorneys with anti-trust experience for their suggestions for significant improvements in our current statutes." Testimony of Mary Lou Munts dated October 8, 1979 (located in Legislative Council Files, Madison, Wisconsin).

[\*P57] On October 3, 1979, Attorney General La Follette wrote the chair of the Assembly Commerce and Consumer Affairs Committee, Representative Marjorie (Midge) Miller. He indicated that Assembly Bill 831 was a "comprehensive [\*\*\*\*40] revision of Chapter 133, Wisconsin's antitrust law." He wrote that the "revision is the result of many hours of work by University of Wisconsin Law School faculty, members of the private bar, legislators, and members of the Department of Justice." Letter to Representative Marjorie Miller from Attorney General Bronson C. La Follette dated October 3, 1979 (located in Legislative Council files, Madison, Wisconsin).

[\*P58] Nineteen years before Assembly Bill 831 was introduced, the State argued its authority to regulate interstate commerce in the Allied Chemical case and won. Three years before Assembly Bill 831 was introduced, the Wall Street Journal published a story on state antitrust enforcement. It cited Wisconsin Assistant Attorney General Michael Zaleski to the effect that in 1975, Wisconsin's antitrust division won 29 convictions against businesses, filed 32 consent decrees, and recovered almost \$ 1 million. Timothy D. Schellhardt, Antitrust Enforcement Stepped Up by States: Budgets, Staffs Grow, Wall St. J., Oct. 4, 1976. Legislative files show that Zaleski played a key role in developing Assembly Bill 831. One year before Assembly Bill 831 was introduced, the Wisconsin [\*\*\*\*41] Department of Justice argued Raymond Motor Transportation, Inc. v. [\*\*254] Rice, in the United States Supreme Court. The case was argued by Albert Harriman, an assistant attorney general who helped write the State's brief in Allied Chemical. As noted above, Rice is one of the key cases revitalizing state power to regulate interstate commerce.

[\*P59] A few months before introduction of Assembly Bill 831, Attorney General La Follette spoke at the Antitrust Seminar of the National Association of Attorneys General and stated: "It is now more likely that the wrath of state antitrust enforcement will be felt by violators than that of the federal government." Press Release, State of Wisconsin Department of Justice (May 18, 1979) (on file at Wisconsin Legislative Reference Bureau).

[\*P60] Because Assembly Bill 831 was so closely linked to the Wisconsin Department of Justice, it must have reflected the thinking of the Wisconsin Department of Justice that Chapter 133 reached interstate [\*\*\*154] commerce, for that was the interpretation the Department consistently gave to the statute after the Allied Chemical decision.

[\*P61] Second, one of the major objectives of the 1980 legislation [\*\*\*\*42] was to "reverse" the holding in Illinois Brick Co. v. State of Illinois, 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977). In Illinois Brick, the Supreme Court concluded that indirect purchasers harmed by antitrust violations could not recover under federal antitrust law. Assembly Bill 831 addressed this deficiency in Wis. Stat. § 133.18, which provides in part: "Any person injured, directly or indirectly, by reason of anything prohibited by this chapter may sue therefor and shall recover threefold the damages sustained by the person . . ." (Emphasis added.)

[\*P62] [\*\*255] In his letter to Representative Marjorie Miller of October 3, 1979, Attorney General La Follette wrote:

An important new change would reverse the effect of the U.S. Supreme Court's ruling in the Illinois Brick case on Wisconsin law. The Court, in that case, ruled that only direct purchasers may recover damages for illegally price-fixed goods. Thus, indirect purchasers -- such as state and local governments which purchase most of their supplies through wholesalers, retailers or other middlemen -- are left out in the cold when it comes to recovering for the illegally [\*\*\*\*43] inflated prices they and their constituents must pay. As only one example of how this adversely affects Wisconsin and its taxpayers, my office recently returned nearly a half million dollars to numerous Wisconsin schools, hospitals, municipalities, and counties from a settlement of an antitrust case against manufacturers of contract hardware. Had the Illinois Brick decision been in effect in 1973, when this case was brought, we would not have been able to recover this money for Wisconsin taxpayers.

Letter to Representative Marjorie Miller from Attorney General Bronson C. La Follette dated October 3, 1979 (located in Legislative Council files, Madison, Wisconsin).

[\*P63] When the legislature permitted indirect purchasers to seek recovery for antitrust violations it certainly intended the statute to reach interstate commerce. This result was discussed and upheld in ARC America.<sup>13</sup> The Court's holding in ARC America reveals that at least under some circumstances, state antitrust [\*\*256] statutes are expected to reach interstate commerce.<sup>14</sup> It would be completely unrealistic [\*\*\*155] to interpret Wis. Stat. § 133.18 as being limited to intrastate commerce. [\*\*\*\*44]

[\*P64] [\*\*\*45] Third, turning directly to the text of the legislation, there is ample evidence of changes in prior law requiring a new interpretation of the statute. This evidence supports four significant principles.

[\*P65] a. Chapter 133 was repealed and recreated, not simply amended. In her testimony, Representative Munts stated:

Wisconsin's current anti-trust laws rest on a foundation begun over eighty years ago and are overdue for a comprehensive revision. . . .

[\*\*257] Because the laws concerning anti-trust have been enacted in [] piecemeal fashion, conflicts have arisen in the interpretation and wording of the various sections. . . .

AB 831 not only clarifies the scope and intent of Wisconsin's anti-trust laws, but also insures that the state's statutes are brought into line with federal statutes. . . .

....

AB 831 . . . broadens critical sections of the statutes [citing sections including section 133.03].

In conclusion, AB 831 will eliminate many ambiguities in the present statutes. More importantly, it will improve compatibility with federal anti-trust law, enhance state enforcement and insist on the preservation of a competitive climate in Wisconsin. [\*\*\*46] . . .

Testimony of Mary Lou Munts dated October 8, 1979 (located in Legislative Council files, Madison, Wisconsin) (emphasis added).

[\*P66] In an October 5, 1979, memorandum to Representative Miller, a senior staff attorney for the Legislative Council, Russ Whitesel, wrote: "This Bill is a complete revision of the state anti-trust and monopoly law, Ch. 133 . . ." Wisconsin Legislative Council Staff Memorandum to Representative Midge Miller from Russ Whitesel, Senior Staff Attorney dated October 5, 1979 (located in Wisconsin Legislative Council files, Madison, Wisconsin). In testimony on October 8, 1979, a representative of Wisconsin Manufacturers and Commerce, Fred W. Shaffer, said "AB 831 does far more than revise existing Wisconsin law. It changes it significantly." Testimony of Fred W. Shaffer dated October 8, 1979 (located in Legislative Council files, Madison, Wisconsin).

<sup>13</sup> In California v. ARC America Corp., 490 U.S. 93, 104 L. Ed. 2d 86, 109 S. Ct. 1661 (1989), several states alleged violations of both federal and state antitrust law by an interstate monopoly of concrete block producers. Id. at 97. The parties settled the case, but the federal judge administering the settlement refused to allow indirect purchasers to have access to the settlement fund because he believed that federal law preempted the state antitrust statutes. Id. at 99. The Supreme Court held that the state "repeater" statutes were not preempted. Id. at 101.

<sup>14</sup> Wisconsin's Department of Justice has certainly interpreted the law as enabling it to reach activities in interstate--and even international--commerce. See Press Release, Wisconsin Department of Justice, Doyle Announces Historic Settlements With Vitamin Companies; Six Manufacturers Agree to Pay More Than \$ 335 Million (Oct. 10, 2000), available at [www.doj.state.wi.us](http://www.doj.state.wi.us). In the "vitamin cases," Wisconsin led 23 states alleging that the six companies met in secret in locations "around the world" to fix vitamin prices, harming indirect purchasers. Id. The states alleged violations of "state and federal law." Id. The six companies involved are giants in international commerce, including BASF of Germany and Eisai Company of Japan. Id. Three of the companies were European and three were Japanese. Id. None was based in the United States, let alone Wisconsin.

We recognize that the Department's conduct cannot, *sua sponte*, legitimize the underlying statute. However, it is persuasive evidence that in practice, commercial parties tacitly agree that Wisconsin's law may apply to interstate--even international--commerce.

[\*P67] [\*\*258] These statements contradict Microsoft's interpretation of the 1980 action and document a comprehensive revision of the law.

[\*P68] b. The legislature created a very broad statement of legislative intent in a new [section 133.01](#). This declaration said in part: "It is the intent [\*\*\*\*47] of the legislature that this chapter be interpreted in a manner which gives the most liberal construction to achieve the aim of competition."

[\*P69] Wisconsin's Little Sherman Act did not have a declaration of intent in 1914 when this court decided the Pulp Wood case. Moreover, section 133.01 [now [§ 133.03](#)] was not covered by any legislative declaration of intent until revision of the whole chapter in 1980. A previous statement of intent applied to only "ss. 133.17 [through] 133.185." Thus, the 1980 legislation not only added the phrase "most liberal construction," but also applied [\*\*\*156] the legislative declaration to [§ 133.03](#) for the first time.

[\*P70] [HN13](#)[] This court has often used legislative declarations as a valuable aid to our analysis. See, e.g., [LeMere v. LeMere, 2003 WI 67, P15, 262 Wis. 2d 426, 663 N.W.2d 789](#); [Wood v. City of Madison, 2003 WI 24, P18, 260 Wis. 2d 71, 659 N.W.2d 31](#); [Ocasio v. Froedtert Mem'l Lutheran Hosp., 2002 WI 89, P14, 254 Wis. 2d 367, 646 N.W.2d 381](#).

[\*P71] c. The Legislature deleted references to "in this state" in the Little Sherman Act portion of the chapter. Considering that [\*\*\*\*48] Assembly Bill 831 came out of the Department of Justice and the elimination of the phrase "in this state" furthered the Department's views, a reasonable inference may be drawn that the elimination has significance. Microsoft directs our attention to [Emergency One, Inc. v. Waterous Co., 23 F. Supp. 2d 959, 963-64 \(1998\)](#), in which a federal district court faced [\*\*259] with the same question dismissed the repeated deletion of "in this state" as insignificant. We disagree. It is true enough that we have no document addressing the issue directly. Nonetheless, in interpreting the statute in context, we believe the deletion carries some weight.

[\*P72] d. If we discount the prevailing atmosphere of 1893 in an interpretation of [Wis. Stat. § 133.03](#), we are left with an exceptionally broad statute that uses such phrases as "Every contract . . . or conspiracy," "Every person," "any contract," "any combination," and "Every person who . . . attempts to monopolize." The text itself does not permit a limiting construction.

[\*P73] Finally, we address the principle of statutory interpretation stated in Zimmerman that "once a [\*\*\*\*49] construction has been given to a statute, the construction becomes part of the statute; and it is within the province of the legislature alone to change the law." [Zimmerman, 38 Wis. 2d at 633](#). In the Allied Chemical and Milwaukee Braves cases, this court gave a focused construction to the statute. We think it is far more likely that in 1980 the legislature acquiesced in or strengthened the interpretation of Allied Chemical than that it revised the statute with the intent of undoing that decision.

[\*P74] In short, [HN14](#)[] we conclude that Chapter 133, particularly [§ 133.03](#), applies to interstate commerce, at least in some circumstances. Consistent with this holding, we withdraw the language from Conley Publishing that "the scope of Chapter 133 is limited to intrastate transactions." See [Conley Publ'g, 2003 WI 119, 265 Wis. 2d 128, P16, 665 N.W.2d 879](#).

[\*P75] The United States District Court in Milwaukee reached the same conclusion in the Emergency One case. The court extensively analyzed the history and [\*\*260] purpose of Chapter 133, and determined that it applies to interstate commerce under some circumstances. [23 F. Supp. 2d at 966-67](#). [\*\*\*\*50] Like this court, the Emergency One court was persuaded by the legislative history of the 1980 revision, particularly the portion legislatively repealing Illinois Brick, as well as our holdings in Allied Chemical and Milwaukee Braves. [Emergency One, 23 F. Supp. 2d at 966-67](#).

[\*P76] In 1997 the Seventh Circuit considered an antitrust case involving an Alabama statute in which the defendants, manufacturers and wholesalers of prescription drugs, made similar arguments to those Microsoft makes in this case. [In re Brand Name Prescription Drugs Antitrust Litigation, 123 F.3d 599, 612 \(7th Cir. 1997\)](#). The defendants cited several cases seemingly showing that "Alabama's antitrust statute is indeed limited to

2005 WI 121, \*1211-284 Wis. 2d 224, \*\*260L-700 N.W.2d 139, \*\*\*156L-2005 Wisc. LEXIS 393, \*\*\*\*50

intrastate commerce." *Id.* (citing *Georgia Fruit Exchange v. Turnipseed*, 9 Ala. App. 123, [\*\*\*157] 62 So. 542, 546 (Ala. 1913) ("There being thus both a state and national law prohibiting unlawful combinations in restraint of trade--the one law relating to intrastate, the other to interstate, commerce . . . ")).<sup>15</sup>

[\*P77] [\*\*\*\*51] The Seventh Circuit rejected the defendant's argument. It stated:

The cases on which the defendants rely . . . date from a period in which, interstate commerce being narrowly defined, and federal power to regulate such commerce being deemed exclusive, a state statute limited to intrastate commerce would have some, albeit a strictly limited, scope and could not have a greater scope no matter how much the state wanted it to. The [\*\*261] cases thus were not interpreting the statute; they were interpreting the Constitution as placing upper and lower bounds on the reach of the statute, and the Constitution has since been reinterpreted.

*Id. at 612-13.*

[\*P78] The Seventh Circuit added: "If the statute is limited today as it once was to commerce that is not within the regulatory power of Congress under the commerce clause, it is a dead letter because there are virtually no sales, in Alabama or anywhere else in the United States, that are intrastate in that sense." *Id. at 613*. We agree.

[\*P79] The Seventh Circuit thus interpreted the Alabama statute to have evolved in response to changing interpretations of the federal constitution. [\*\*\*\*52]<sup>16</sup> In Wisconsin, the interpretation of our statute has changed not only because of evolution in constitutional theory, but also because the legislature acted to repeal and recreate Chapter 133 in 1980, with altered language.

[\*P80] [\*\*\*\*53] [\*\*262] A number of state courts have construed statutes similar to Wisconsin's to reach interstate commerce. See, e.g., *C. Bennett Building Supplies, Inc. v. Jenn Air Corp.*, 759 S.W.2d 883, 888 (Mo. Ct. App. 1988); *State v. Sterling Theatres Co.*, 64 Wn.2d 761, 394 P.2d 226, 227 (Wash. 1964).

[\*P81] **HN15**↑ We recognize that our holding implies that in some circumstances, a monopolist's conduct is actionable under either federal law, Wisconsin law, or both. This concern is not unique to antitrust law. Concerns about "double jeopardy" prosecutions date back to the adoption of the *Bill of Rights*. U.S. Const. Amend. V (**HN16**↑) "nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb". **HN17**↑ As a general rule, a person is not unconstitutionally subject to double jeopardy when he is tried successively by different sovereigns for the same crime. See *United States v. Wheeler*, 435 U.S. 313, 317, [\*\*\*158] 55 L. Ed. 2d 303, 98 S. Ct. 1079 (1978). This rule derives from the more general concept that the states and the federal government are separate sovereigns, each entitled to enforce its own laws. *Id. at 320*. [\*\*\*\*54]

[\*P82] Duplicative prosecution is one thing; duplicative recovery is another. "It goes without saying that the courts can and should preclude double recovery by an individual." *E.E.O.C. v. Waffle House, Inc.*, 534 U.S. 279, 297, 151 L. Ed. 2d 755, 122 S. Ct. 754 (2002).

<sup>15</sup> The Alabama court's statement is remarkably similar to the language in *Pulp Wood*: "The contract we think involved interstate commerce, and if so the federal statute is applicable and the case will be treated on that basis." *Pulp Wood*, 157 Wis. at 615.

<sup>16</sup> We acknowledge that the Alabama Supreme Court subsequently interpreted the same statute differently. *Abbott Laboratories v. Durrett*, 746 So. 2d 316, 337 n.5 (Ala. 1999). The Alabama court conducted an extensive review of the Supreme Court's commerce clause jurisprudence, as we have. *Id. at 330-32*. It reached the same conclusion we have: that during the late nineteenth century, the theory of "dual sovereignty" or, as we have termed it, "mutually exclusive spheres" of power, was predominant. *Id.* However, the Alabama court adopted an originalist construction of the statute, giving great weight to the Alabama Legislature's intent at the time it enacted the Alabama statute. *Id. at 337 n.5*. Specifically, the Alabama court relied on the presence of the phrase "within this state" in the original act. *Id.* The case here is different because, as we have discussed, our legislature repealed and recreated our antitrust act, expressly deleting all references to "in this state," after our decision in *Allied Chemical*.

[\*P83] In summary, we conclude that Chapter 133 may reach interstate commerce under some circumstances.

C. When May Chapter 133 Reach Interstate Commerce?

[\*P84] Having determined that Wisconsin's antitrust law may apply to interstate commerce under some [\*\*263] circumstances, we are confronted with the question of what those circumstances are.

[\*P85] HN18↑ A civil plaintiff filing an action under Wisconsin's antitrust act must allege that (1) actionable conduct, such as the formation of a combination or conspiracy, occurred within this state, even if its effects are felt primarily outside Wisconsin; or (2) the conduct complained of "substantially affects" the people of Wisconsin and has impacts in this state, even if the illegal activity resulting in those impacts occurred predominantly or exclusively outside this state. Allied Chemical, 9 Wis. 2d at 295. Operating with lesser standards [\*\*\*\*55] would jeopardize the action, undermine the validity of our antitrust statute, and create the spectacle of Lilliputian harassment in Wisconsin courts. Questions of provincialism, favoritism, and undue burden on interstate commerce should be determined by resort to contemporary federal commerce clause jurisprudence. To say more is beyond the scope of this opinion.

*By the Court.*-The order of the circuit court is reversed and the cause is remanded.

[\*P86] SHIRLEY S. ABRAHAMSON, C.J., and ANN WALSH BRADLEY, J., did not participate.

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## In re GlaxoSmithKline PLC

Supreme Court of Minnesota

July 14, 2005, Filed

A04-2150, A04-2151

**Reporter**

699 N.W.2d 749 \*; 2005 Minn. LEXIS 403 \*\*; 2005-2 Trade Cas. (CCH) P74,892

In the Matter of GlaxoSmithKline plc

**Subsequent History:** On remand at, Remanded by [In re GlaxoSmithKline PLC, 713 N.W.2d 48, 2006 Minn. App. LEXIS 51 \(Minn. Ct. App., Apr. 18, 2006\)](#)

**Prior History:** [\*\*1] Court of Appeals. H. Peter Albrecht.

[In re GlaxoSmithKline plc, 2005 Minn. LEXIS 61 \(2005\)](#)

**Disposition:** Reversed and remanded (No. A04-2150); dismissed as moot (No. A04-2151).

## Core Terms

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confidential, documents, special proceeding, substantial rights, court of appeals, district court, discovery, merits, protective order, final order, antitrust, discretionary, notice

## LexisNexis® Headnotes

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Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Governments > State & Territorial Governments > Claims By & Against

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

Civil Procedure > Discovery & Disclosure > General Overview

Civil Procedure > Discovery & Disclosure > Discovery > Relevance of Discoverable Information

### [HN1\[ Discovery, Privileged Communications](#)

A civil investigative demand (CID) is a discovery tool provided by statute to aid the state in the investigation of suspected violations of Minnesota laws. [Minn. Stat. § 8.31, subd. 2](#) (2004), authorizes the attorney general to obtain discovery from any person regarding any matter, fact or circumstance, not privileged, which is relevant to the subject matter involved in the pending investigation, in accordance with the provisions of this subdivision. The discovery may be obtained without commencement of a civil action and without leave of court.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Governments > Courts > Rule Application & Interpretation

## **HN2** **Standards of Review, De Novo Review**

The Supreme Court of Minnesota applies de novo review to the court of appeals' interpretations of the rules of civil appellate procedure.

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

## **HN3** **US Department of Justice Actions, Investigations**

The Supreme Court of Minnesota has defined a final order as one that ends the proceeding as far as the court is concerned or that finally determines some positive legal right of the appellant relating to the action. A confidential agreement and protective order (CID order) may be considered final if it determines all issues presented to the court in the CID proceeding. This conclusion parallels federal law, which generally recognizes that orders from proceedings related to CIDs and administrative subpoenas are appealable as "final decisions" of the district courts under [28 U.S.C.S. § 1291](#).

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

Civil Procedure > Discovery & Disclosure > Discovery > Subpoenas

## **HN4** **US Department of Justice Actions, Investigations**

Federal law generally recognizes that orders from proceedings related to a civil investigative demand (CID) and administrative subpoenas are appealable as "final decisions" of the district courts under [28 U.S.C.S. § 1291](#).

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

Civil Procedure > Discovery & Disclosure > Discovery > Subpoenas

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

## **HN5** **Public Enforcement, State Civil Actions**

At least three federal statutes specify that orders enforcing federal confidential agreements and protective orders (CID order) are appealable under [28 U.S.C.S. § 1291](#). Federal courts of appeals have held administrative subpoenas to be appealable as final decisions under [§ 1291](#).

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Estate, Gift & Trust Law > Trusts > General Overview

#### **[HN6](#) [↓] Appellate Jurisdiction, Final Judgment Rule**

Minn. R. Civ. P. 103.03(g), regarding appealable orders, does not define substantial right. "Substantial right" is defined as an essential right that potentially affects the outcome of a lawsuit and is capable of legal enforcement and protection, as distinguished from a mere technical or procedural right.

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

Governments > Courts > Court Records

#### **[HN7](#) [↓] Discovery, Protective Orders**

Court proceedings and documents enjoy a "presumption of openness" that generally may be overcome only by showing that a party's constitutional rights would be at risk if the proceeding or document is made public.

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Trade Secrets Law > Civil Actions > Discovery

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

Governments > Courts > Court Records

Trade Secrets Law > Civil Actions > Protection Orders

#### **[HN8](#) [↓] Bill of Rights, Fundamental Freedoms**

Documents produced as discovery are not presumed to be public and district courts have broad discretion to issue protective orders, such as to protect trade secrets and similar commercial information. [Minn. R. Civ. P. 26.03\(g\)](#). Still, district courts presiding over civil actions are directed to weigh policies in favor of openness against the interests of the litigant in sealing the record.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Governments > Courts > Court Records

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

#### **HN9** Consumer Protection, Deceptive & Unfair Trade Practices

The attorney general has a statutory duty to enforce state antitrust laws. [Minn. Stat. § 8.31, subd. 1](#) (2004) requires the attorney general to investigate suspected antitrust violations under [Minn. Stat. § 325D.49-66](#) (2004). Finally, the state has the right under the Minnesota Government Data Practices Act (MGDPA), Minn. Stat. ch. 13 (2004), to bring an action in the district court in the county where the data is maintained to obtain disclosure of data classified as confidential or protected nonpublic. [Minn. Stat. § 13.39, subd. 2a](#) (2004).

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Governments > Courts > Court Records

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

#### **HN10** Discovery, Protective Orders

The classification of inactive investigation data is relevant when a civil action is not brought. [Minn. Stat. § 13.39, subd. 3](#) (2004). The pertinent question under the Minnesota Government Data Practices Act (MGDPA), Minn. Stat. ch. 13 (2004), may be whether commencement of a county action makes the investigative data public. [Minn. Stat. § 13.39, subd. 2a](#) (2004). And the conclusion that there is a First Amendment privilege for "petitioning documents" is not clearly recognized in case law.

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

Civil Procedure > Judgments > Relief From Judgments > Independent Actions

#### **HN11** Appellate Jurisdiction, Final Judgment Rule

Minn. R. Civ. P. 103.03(g), regarding appealable orders, does not define the words "special proceeding." The Supreme Court of Minnesota has preferred an interpretation that preserves the parties' rights to appeal where appropriate. A special proceeding is defined as usually meaning such a proceeding as may be commenced independently of a pending action by petition or motion, upon notice, in order to obtain special relief. Its existence is not dependent upon the existence of any other action and it therefore is not an integral part of the original action but is separate and apart. It adjudicates by final order a substantial right distinct from any judgment entered upon the merits of the original action.

Civil Procedure > Pleading & Practice > Motion Practice > Content & Form

#### **HN12** Motion Practice, Content & Form

A special proceeding is a generic term for a remedy that is not part of the underlying action and that is brought by motion or petition, upon notice, for action by the court independent of the merits of the underlying action.

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

Civil Procedure > Pretrial Matters > Conferences > Pretrial Orders

Civil Procedure > Discovery & Disclosure > General Overview

Civil Procedure > Discovery & Disclosure > Discovery > Protective Orders

Civil Procedure > Pretrial Matters > General Overview

### **HN13** [blue icon] US Department of Justice Actions, Investigations

The attorney general is authorized to serve a civil investigative demand (CID) without commencement of a civil action, and the district court is authorized to order compliance with CID procedures. [Minn. Stat. § 8.31, subds. 2, 2a](#) (2004). In a CID proceeding, the ultimate remedy to be provided by the court is the ordering of the production of discovery, which includes any determination of the public or confidential nature of discovery documents. The CID proceeding is not merged into any subsequent litigation, and discovery produced pursuant to a CID may or may not lead to a separate action. Thus, a CID order should not be characterized as a "pretrial discovery tool."

Antitrust & Trade Law > Public Enforcement > US Department of Justice Actions > Investigations

### **HN14** [blue icon] US Department of Justice Actions, Investigations

A civil investigative demand (CID) enforcement proceeding that finally determines the confidentiality of documents produced in response to a CID meets the prior definitions of a "special proceeding." It is not dependent upon the existence of any other action. It is commenced and enforced independent of the merits of the underlying action.

Civil Procedure > Appeals > Reviewability of Lower Court Decisions > Preservation for Review

### **HN15** [blue icon] Reviewability of Lower Court Decisions, Preservation for Review

Generally, an appellate court does not address issues that were not raised in a petition for review. But the Supreme Court of Minnesota may deviate from its usual procedure in the interest of justice. [Minn. R. Civ. App. P. 103.04](#).

## **Syllabus**

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- When the district court issues an order finally determining the confidentiality status of documents produced pursuant to a Civil Investigative Demand, the order may be appealed of right under [Minn. R. Civ. App. P. 103.03\(g\)](#) as a final order affecting a substantial right in a special proceeding.

- The interests of justice do not warrant the consideration of the merits of confidentiality issues that were not raised in the petition for further review.

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For Amicus Minnesota Newspaper Association: MARK R. ANFINSON, Minneapolis, MN.

**Judges:** Hanson, J.

**Opinion by:** Hanson

## Opinion

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[\*752] Heard, considered, and decided by the court en banc.

HANSON, Justice.

We review orders of the court of appeals [\*\*2] dismissing two appeals by appellant State of Minnesota from an order of the Hennepin County District Court determining that certain discovery documents produced pursuant to a Civil Investigative Demand were confidential and could not be made public. The court of appeals denied discretionary review under [Minn. R. Civ. App. P. 105.01](#) and a separate panel then dismissed the appeal of right under [Minn. R. Civ. App. P. 103.03](#). We granted the state's petitions for review of both orders and consolidated the matters. We reverse the dismissal of the appeal of right and remand to the court of appeals for consideration of the merits.

**HN1** A Civil Investigative Demand (CID) is a discovery tool provided by statute to aid the state in the investigation of suspected violations of Minnesota laws. [Minnesota Statutes § 8.31, subd. 2](#) (2004), authorizes the attorney general to

obtain discovery from any person regarding any matter, fact or circumstance, not privileged, which is relevant to the subject matter involved in the pending investigation, in accordance with the provisions of this subdivision. The discovery may be obtained without commencement of a civil action and without [\*\*3] leave of court \* \* \*.

The state served a CID on respondent GlaxoSmithKline plc (GSK), a pharmaceutical company that the state suspected of committing antitrust violations by preventing Canadian pharmacies from supplying prescription drugs to United States consumers. The CID requested the production of documents concerning, among other things, GSK's sales of drugs in Canada and its communications with Canadian pharmacies that sold drugs in the United States.

Before any documents were produced, GSK and the state entered a Confidentiality Agreement that (1) permitted GSK to mark documents as "confidential" if they contained trade secret information or if GSK could assert "another legal basis for treating the documents as confidential, including \* \* \* commercial information that could be subject to a protective order pursuant to [Minnesota Rule of Civil Procedure 26.03](#)"; (2) required the state to use confidential documents solely for the "investigation and any litigation arising from the investigation"; and (3) stated that if the state objected to a confidentiality designation or received a third-party request for access to a document, the state would give 10-day notice to GSK and [\*\*4] GSK then could move the district court to resolve the issue. The Confidentiality Agreement specified that if the state were to commence litigation, the agreement "shall continue to govern \* \* \* until such time as the Court should modify, terminate, or supersede it."

After GSK produced some documents, the state brought a motion in the Hennepin County District Court to compel production of further documents, and GSK countered with a motion for a protective order. The court granted a Protective Order that largely mirrored the Confidentiality Agreement, but also contained a provision stating that confidential documents filed with the court in any resulting litigation must be filed under seal, "pending further Order of the presiding judge in such proceedings." GSK then produced additional documents--the vast majority of which were marked as "confidential." The state filed a second motion in Hennepin County District Court for an order declaring that about 45 of those documents were [\*753] not confidential under the Confidentiality Agreement, the Protective Order, the [Minnesota Government Data Practices Act](#) (MGDPA), [Minn. Stat. ch. 13](#) (2004), or [Minn. R. Civ. P. 26.03](#) (which governs protective [\*\*5] orders).

Five days after a hearing on its motion, the state commenced a civil antitrust action against GSK in Ramsey County District Court and provided a copy of the complaint to the judge presiding over the CID proceeding in Hennepin County. On October 13, 2004, the Hennepin County District Court denied the state's motion, ruling that the documents were to remain confidential because (1) civil investigative data do not become "inactive" under the MGDPA when a suit is commenced; (2) the documents were "petitioning documents subject to [First Amendment](#) privilege," thus disclosure was not required under [Minn. R. Civ. P. 26.03](#); and (3) public disclosure was not permitted by terms of the Confidential Agreement and the Protective Order (the CID order).

The state appealed the CID order by simultaneously filing a Notice of Appeal and a Petition for Discretionary Review. A three-judge special-term panel of the court of appeals denied discretionary review under [Minn. R. Civ. App. P. 105.01](#), holding that the petition "does not establish that the district court's enforcement of the state's agreement to maintain confidentiality (even if litigation resulted) warrants discretionary review." [\[\\*\\*6\] In the Matter of GlaxoSmithKline plc](#), No. A04-2151 (Minn. App. Dec. 8, 2004).

A separate special-term panel of the court of appeals subsequently granted GSK's motion to dismiss the state's appeal of right on grounds that the appeal was taken from a nonappealable order. [In the Matter of GlaxoSmithKline plc](#), No. A04-2150 (Minn. App. Dec. 22, 2004). The court rejected the state's first argument that the CID order was a final order affecting a substantial right made in a special proceeding under [Minn. R. Civ. App. P. 103.03\(g\)](#). The court held that "[a] motion to compel compliance with a CID under [Minn. Stat. § 8.31, subd. 2a](#), is not a special proceeding because a CID is a pretrial discovery tool, not a remedy." The court further rejected the state's arguments that the CID order was appealable under other parts of [rule 103.03](#)--as an injunction under part (b), as a collateral order under part (j), or as an order that determines the action and prevents a judgment under part (e).

The state submitted two petitions for review to this court, asking us to reinstate the appeal and remand to the court of appeals. Then, on brief, the state argued that we should [\[\\*\\*7\]](#) decide the merits of the CID order, even though not requested in the petitions for further review. GSK argues that this is not an "exceptional case" warranting departure from our usual procedure to only review issues raised in the petition for further review.

## I.

We begin our analysis with the state's first argument that the CID order was appealable of right as "a final order, decision or judgment affecting a substantial right made in an administrative or other special proceeding." [Minn. R. Civ. App. P. 103.03\(g\)](#).<sup>1</sup> We [HN2](#) apply de novo review to court of appeals' interpretations of the rules of civil appellate procedure. See [Kastner v. Star Trails Ass'n](#), 646 N.W.2d 235, 238 (Minn. 2002).

[\[\\*754\]](#) First, we examine whether the CID [\[\\*\\*8\]](#) order was a "final order" under [rule 103.03\(g\)](#). We [HN3](#) have defined a final order as one that "ends the proceeding as far as the court is concerned or that finally determines some positive legal right of the appellant relating to the action." [In re Estate of Janecek](#), 610 N.W.2d 638, 642 (Minn. 2000) (holding that the order disqualifying an attorney in a probate proceeding was a final order, and citing [Weinzierl v. Lien](#), 296 Minn. 539, 540, 209 N.W.2d 424, 424 (1973)). The CID order may be considered final because it determined all issues presented to the court in the CID proceeding. This conclusion parallels [HN4](#) federal law, which generally recognizes that orders from proceedings related to CIDs and administrative subpoenas are appealable as "final decisions" of the district courts under [28 U.S.C. § 1291 \(2000\)](#).<sup>2</sup> Cf. [Gordon v. Microsoft](#)

<sup>1</sup> We have examined a CID order once before and did so under discretionary review. [Kohn v. State](#), 336 N.W.2d 292, 295-97 (Minn. 1983). But we did not explain why discretionary review was selected or even discuss review as of right. [Id. at 294](#).

<sup>2</sup> [HN5](#) At least three federal statutes specify that orders enforcing federal CIDs are appealable under [28 U.S.C. § 1291](#). See [15 U.S.C. § 57b-1\(h\) \(2000\)](#) (Federal Trade Commission's CID); [15 U.S.C. § 1314\(e\) \(2000\)](#) (federal antitrust CID); [31 U.S.C. § 3733\(j\)\(5\) \(2000\)](#) (False Claims Act CID). We have not previously examined the appealability of attorney general administrative subpoenas issued pursuant to [Minn. Stat. § 8.16](#) (2004) and express no opinion on the question here. But it is helpful for our present analysis to note that federal courts of appeals have held administrative subpoenas to be appealable as final decisions under [28 U.S.C. § 1291](#). See [Univ. of Med. & Dentistry of N.J. v. Corrigan](#), 347 F.3d 57, 63 (3d Cir. 2003); [United States v. Legal Servs. for New York City](#), 346 U.S. App. D.C. 83, 249 F.3d 1077, 1080-81 (D.C. Cir. 2001); [In re Subpoena Duces Tecum](#), 228

Corp., 645 N.W.2d 393, 399-400 (Minn. 2002) (examining federal law to determine standards for appealability of class certification orders in Minnesota courts).

[\*\*9] Next, we examine whether a "substantial right" is at issue. HN6 [↑] Rule 103.03(g) does not define substantial right, and our prior interpretations of the words have been fact specific. See In re Janecek, 610 N.W.2d at 642 (indicating that a person has substantial right to be represented by an attorney of one's choice); In re Trust of Tufford, 275 Minn. 66, 67 n.1, 145 N.W.2d 59, 60 n.1 (1966) (holding that right to terminate a trust is a substantial right); see also Douglas D. McFarland & William J. Keppel, *Minnesota Civil Practice* § 2719 (3d ed. 1999) (observing that "the appellate court will rarely find an order in a special proceeding nonappealable on the ground that it does not affect a *substantial right*"); *Black's Law Dictionary* 1349 (8th ed. 2004) (defining substantial right as "an essential right that potentially affects the outcome of a lawsuit and is capable of legal enforcement and protection, as distinguished from a mere technical or procedural right").

The state suggests that a substantial right is at issue because the order requiring the state to keep the documents confidential will envelop the entire litigation in a "shroud" [\*\*10] of secrecy," requiring the trial and any appeals to take place behind closed doors. GSK counters that no substantial right is at issue because the state is not hindered from prosecuting the merits of the antitrust case, and the CID order may be appealed after the merits ultimately are decided. The court of appeals did [\*755] not examine whether a substantial right was at issue.

Although the state's prediction of a "secret" trial is premature, we cannot ignore that HN7 [↑] court proceedings and documents enjoy a "presumption of openness" that generally may be overcome only by showing that a party's constitutional rights would be at risk if the proceeding or document is made public. See Minneapolis Star & Tribune Co. v. Schumacher, 392 N.W.2d 197, 203-04 (Minn. 1986) (citing Richmond Newspapers, Inc. v. Virginia, 448 U.S. 555, 573, 575-81, 65 L. Ed. 2d 973, 100 S. Ct. 2814 (1980)); see also Gannett Co., Inc., v. DePasquale, 443 U.S. 368, 386 n.15, 61 L. Ed. 2d 608, 99 S. Ct. 2898 (1979) ("For many centuries, both civil and criminal trials have traditionally been open to the public."). In civil actions, "each case involves a weighing of the policies in favor of openness against the" [\*\*11] interests of the litigant in sealing the record. In re Rahr Malting Co., 632 N.W.2d 572, 576 (Minn. 2001) (citing Schumacher, 392 N.W.2d at 202-03).

GSK is correct that HN8 [↑] documents produced as discovery are not presumed to be public and that district courts have broad discretion to issue protective orders, such as to protect trade secrets and similar commercial information. Minn. R. Civ. P. 26.03(g); Seattle Times Co. v. Rhinehart, 467 U.S. 20, 33, 81 L. Ed. 2d 17, 104 S. Ct. 2199 (1984) (holding that "pretrial depositions and interrogatories are not public components of a civil trial"). And GSK has claimed that a constitutional right--a "petitioning privilege" under the First Amendment to the United States Constitution--is implicated. Compare Schumacher, 392 N.W.2d at 204 (holding that there is no First Amendment right for the public to access sealed settlement documents and transcripts). Still, district courts presiding over civil actions are directed to weigh "policies in favor of openness against the interests of the litigant in sealing the record." In re Rahr Malting Co., 632 N.W.2d at 576.

We cannot ignore HN9 [↑] the [\*\*12] attorney general's statutory duty to enforce state antitrust laws. Minn. Stat. § 8.31, subd. 1 (2004) (requiring attorney general to investigate suspected antitrust violations under Minn. Stat. § 325D.49-66 (2004)). To be fully effective, such enforcement usually must be done publicly, for educational purposes and to deter similar conduct by others. See, e.g., Blue Shield of Virginia v. McCready, 457 U.S. 465, 473, 73 L. Ed. 2d 149, 102 S. Ct. 2540 (1982) (referencing "broad remedial and deterrent objectives" of federal antitrust law). In addition, the state is a party to the Confidentiality Agreement and has a right to seek enforcement of its terms, including enforcement of the state's right to object to GSK's confidentiality designations and to seek a judicial determination of confidentiality. Similarly, the state has the right under the Protective Order to object to GSK's

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F.3d 341, 345-46 (4th Cir. 2000); E.E.O.C. v. Citicorp Diners Club, Inc., 985 F.2d 1036, 1038 (10th Cir. 1993); Sheehan v. Doyle, 513 F.2d 895, 898 (1st Cir. 1975). A decision from the Fifth Circuit Court of Appeals is particularly instructive. In In re Kaiser Aluminum & Chemical Co., the panel sua sponte asked the parties to argue whether an order involving an administrative subpoena was appealable under 28 U.S.C. § 1291, as an interlocutory appeal under 28 U.S.C. § 1292 (2000), or under the collateral order doctrine. 214 F.3d 586, 589 (5th Cir. 2000). The panel concluded that appeal of right was most appropriate because "an order enforcing an administrative subpoena is considered a final order." *Id.*

designations and to seek court review of those designations. Finally, the state has the right under the MGDPA to "bring an action in the district court in the county where the data is maintained to obtain disclosure of data classified as confidential or protected [\*\*13] nonpublic." [Minn. Stat. § 13.39, subd. 2a](#) (2004). We conclude that substantial rights of the state are at issue in this appeal.<sup>3</sup>

[\*\*14] [\*756] Finally, we examine whether the CID order resulted from a "special proceeding." [HN11](#)<sup>↑</sup> [Rule 103.03\(g\)](#) does not define the words "special proceeding." We have preferred an interpretation that preserves the parties' rights to appeal where appropriate. As we observed in *Willeck v. Willeck*:

A special proceeding is defined as usually meaning such a proceeding as may be commenced independently of a pending action by petition or motion, upon notice, in order to obtain special relief. Its existence is not dependent upon the existence of any other action and it therefore is not an integral part of the original action but is separate and apart. It adjudicates by final order a substantial right distinct from any judgment entered upon the merits of the original action.

[286 Minn. 553, 554 n.1, 176 N.W.2d 558, 559 n.1 \(1970\)](#).

On occasion, we have referenced the remedial nature of a special proceeding. See [In re Janecek, 610 N.W.2d at 642](#) (stating that [HN12](#)<sup>↑</sup> a special proceeding is a "generic term for a remedy that is not part of the underlying action and that is brought by motion or petition, upon notice, for action by the court independent of the merits of [\*\*15] the underlying action"); [Chapman v. Dorsey, 230 Minn. 279, 283, 41 N.W.2d 438, 440-41 \(1950\)](#) (stating that a special proceeding is a "generic term for any civil remedy in a court of justice which is not of itself an ordinary action"). The court of appeals held that a CID order does not result from a special proceeding "because a CID is a pretrial discovery tool, not a remedy."

We view a CID order differently. [HN13](#)<sup>↑</sup> The attorney general is authorized to serve a CID "without commencement of a civil action," and the district court is authorized to order compliance with CID procedures. [Minn. Stat. § 8.31, subds. 2, 2a](#) (2004). In a CID proceeding, the ultimate remedy to be provided by the court is the ordering of the production of discovery, which includes any determination of the public or confidential nature of discovery documents. The CID proceeding is not merged into any subsequent litigation, and discovery produced pursuant to a CID may or may not lead to a separate action. Thus, a CID order should not be characterized as a "pretrial discovery tool."

[HN14](#)<sup>↑</sup> A CID enforcement proceeding that finally determines the confidentiality of documents produced in [\*\*16] response to a CID meets our prior definitions of a "special proceeding." It "is not dependent upon the existence of any other action." [Willeck, 286 Minn. at 554 n.1, 176 N.W.2d at 559 n.1](#). It is commenced and enforced "independent of the merits of the underlying action." [In re Janecek, 610 N.W.2d at 642](#). In addition, GSK had notice of the proceeding and participated in it. For these reasons, we conclude that the CID order arose from a special proceeding.

We hold that when a district court issues an order in a CID proceeding that finally determines the confidentiality of documents produced, the order may be appealed of right under [Minn. R. Civ. App. P. 103.03\(g\)](#). [\*757] Because

<sup>3</sup> To the extent that our determination of whether the state's rights are substantial involves consideration of the likelihood that the state will prevail on the merits of the appeal, we observe that the district court's analysis underlying the CID order may not have been complete. The district court's conclusion that the state's request was precluded by the Protective Order or the Confidentiality Agreement does not consider that both documents specifically authorized the state to object to GSK's confidentiality designations and to seek district court review. The conclusion that the documents are not "inactive investigative data" under the MGDPA may answer the wrong question. [HN10](#)<sup>↑</sup> The classification of inactive investigation data is relevant when a civil action is not brought. [Minn. Stat. § 13.39, subd. 3](#) (2004). The pertinent question under the MGDPA may be whether commencement of the Ramsey County action makes the investigative data public. *Id.*, [subd. 2a](#). And the conclusion that there is a [First Amendment](#) privilege for "petitioning documents" is not clearly recognized in case law.

this holding resolves the appealability question, we need not consider whether the order may be appealed under other parts of [rule 103.03](#), or whether the court of appeals abused its discretion by denying discretionary review.

## II.

Next, we examine whether it is appropriate for us to consider the merits of the CID order as to whether the documents are confidential. The state's petitions to this court requested remand to the court of appeals and did not request that we examine the merits. [\[\\*\\*17\]](#) Subsequently, the state argued on brief that we should decide the issues on the merits in the "interest of justice" pursuant to [Minn. R. Civ. App. P. 103.04](#).

[HN15](#)  Generally, we do not address issues that were not raised in a petition for review. [Anderly v. City of Minneapolis](#), 552 N.W.2d 236, 239-40 (Minn. 1996); accord [Northwest Racquet Swim & Health Club v. Deloitte & Touche](#), 535 N.W.2d 612, 613 n.1 (Minn. 1995); [Hapka v. Paquin Farms](#), 458 N.W.2d 683, 685-86 (Minn. 1990). But the state is correct that we may deviate from our usual procedure in the interest of justice. [Minn. R. Civ. App. P. 103.04](#); see also [Putz v. Putz](#), 645 N.W.2d 343, 350 (Minn. 2002) (concluding that "justice requires" consideration of child-support issue not previously raised because the court system has a key role in ensuring welfare of children).

It is unclear whether GSK might have argued its position on the merits more extensively had these issues been described in the state's petition for further review and fully developed in the state's brief. For this reason, we apply the general rule that we will consider only issues raised in a petition [\[\\*\\*18\]](#) for review. [Anderly](#), 552 N.W.2d at 239-40. We reverse the order of the court of appeals dismissing the appeal of right in case no. A04-2150 and remand to the court of appeals. See, e.g., [Pulju v. Metro. Prop. & Cas.](#), 535 N.W.2d 608, 609 (Minn. 1995). In light of our ruling in case no. A04-2150, we dismiss case no. A04-2151 as moot.

Reversed and remanded to the court of appeals (No. A04-2150); dismissed as moot (No. A04-2151).

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## **Medtronic Navigation, Inc. v. BrainLAB Medizinische Computersystems GmbH**

United States District Court for the District of Colorado

July 14, 2005, Decided ; July 14, 2005, Filed

Civil Action No. 98-cv-1072-RPM

### **Reporter**

2005 U.S. Dist. LEXIS 21695 \*; 2005 WL 1661081

MEDTRONIC NAVIGATION, INC., MEDTRONIC SOFAMOR DANEK, INC., SOFAMOR DANEK HOLDINGS, INC. and ST. LOUIS UNIVERSITY, Plaintiffs, v. BRAINLAB MEDIZINISCHE COMPUTERSYSTEMS GMBH, BRAINLAB AG, a German corporation, BRAINLAB USA, INC., a Delaware corporation, and BRAINLAB, INC., a Delaware corporation Defendants.

**Subsequent History:** Count dismissed at, Claim dismissed by [Medtronic Navigation v. Brainlab Medizinische Computersystems GmbH, 2005 U.S. Dist. LEXIS 38256 \(D. Colo., Sept. 8, 2005\)](#)

### **Core Terms**

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patents, unfair competition, counterclaim, Unfair, plaintiffs', bundling

### **LexisNexis® Headnotes**

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Antitrust & Trade Law > Sherman Act > Claims

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Antitrust & Trade Law > Regulated Practices > Intellectual Property > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > Fraud

Antitrust & Trade Law > ... > Actual Monopolization > Anticompetitive & Predatory Practices > General Overview

Antitrust & Trade Law > Sherman Act > Defenses

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Enforcement of a patent procured by fraud on the Patent Office may be violative of § 2 of the Sherman Act provided the other elements necessary to a § 2 case are present.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > General Overview

## **HN2** [down arrow] **False Designation of Origin, Elements of False Designation of Origin**

See [15 U.S.C.S. § 1125\(a\)\(1\)](#).

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

## **HN3** [down arrow] **False Designation of Origin, Elements of False Designation of Origin**

Enforcement of a patent alleged to have been obtained through inequitable conduct in the Patent Office does not give rise to a claim under the Lanham Act, [15 U.S.C.S. § 1125\(a\)\(1\)](#).

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Scope

## **HN4** [down arrow] **False Designation of Origin, Elements of False Designation of Origin**

Marketplace communications by a patentee concerning its patent may be actionable under the Lanham Act, [15 U.S.C.S. § 1125\(a\)\(1\)](#), where the marketplace conduct is undertaken in bad faith.

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Criminal Law & Procedure > ... > Crimes Against Persons > Bribery > General Overview

Healthcare Law > ... > Health Insurance > Reimbursement > General Overview

Business & Corporate Compliance > ... > Public Contracts Law > Voiding Contracts > Bribes, Gratuities & Kickbacks

#### **HN5** US Department of Justice Actions, Criminal Actions

[42 U.S.C.S. § 1320a-7b\(b\)\(2\)\(b\)](#) makes it a criminal offense to offer any compensation to induce any person to purchase any good for which payment may be made under a Federal health care program.

Business & Corporate Compliance > ... > Public Contracts Law > Voiding Contracts > Bribes, Gratuities & Kickbacks

Criminal Law & Procedure > ... > Crimes Against Persons > Bribery > General Overview

#### **HN6** Public Contracts, Bribes, Gratuities & Kickbacks

The Anti-Kickback statute, [42 U.S.C.S. § 1320a-7b\(b\)\(2\)\(b\)](#), is a criminal statute and does not provide a private right of action.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > Business Torts > Unfair Business Practices > General Overview

#### **HN7** Regulated Practices, Trade Practices & Unfair Competition

See [Col. Rev. Stat. § 6-2-108](#).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > Business Torts > Unfair Business Practices > General Overview

#### **HN8** Regulated Practices, Trade Practices & Unfair Competition

A private right of action is provided in [Col. Rev. Stat. § 6-2-111\(1\)](#).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > Business Torts > Unfair Business Practices > General Overview

**HN9** [blue download icon] **Regulated Practices, Trade Practices & Unfair Competition**

See [Col. Rev. Stat. § 6-2-111\(1\)](#).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > Business Torts > Unfair Business Practices > General Overview

**HN10** [blue download icon] **Regulated Practices, Trade Practices & Unfair Competition**

An element of a claim under [Col. Rev. Stat. § 6-2-108](#) is injury of a competitor.

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**Judges:** Richard P. Matsch, Senior District Judge.

**Opinion by:** Richard P. Matsch

## Opinion

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### ORDER GRANTING PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT ON DEFENDANTS' UNFAIR COMPETITION COUNTERCLAIM

[\*4] The defendants (collectively, "BrainLAB") allege in their eighth counterclaim:

Plaintiffs have competed unfairly through various improper activities including bringing suit on a patent knowing that it is not infringed by the defendants and that the said patent is invalid and/or unenforceable, using this suit as a marketing ploy, using this suit as a means to settle other conflicts between the parties and improperly characterizing this suit in conversations with customers and potential customers.

(Countercl. P 20; Answer to Fourth Am. Compl). BrainLAB claims that the plaintiffs have engaged in unfair competition "under federal law, under the laws of the State of Colorado and under common law." (*Id.* P 21).

In response to contention interrogatories served by the plaintiffs, BrainLAB identified two categories of allegedly anti-competitive conduct. First, BrainLAB asserted that the plaintiffs had actual knowledge that the Bucholz patents were invalid at the time the lawsuit was commenced, "making the institution and maintenance of this lawsuit an act of unfair competition." Second, BrainLAB asserted that "SNT<sup>1</sup> routinely ties the pricing of StealthStation products [\*5] and related items to the sales of other products made and sold by the Medtronic Family<sup>'</sup> of companies," and that such tying "may be a violation of [42 U.S.C. § 1320a-7b\(b\)](#)...."

The plaintiffs moved for summary judgment, arguing that neither the alleged fraudulent procurement of the Bucholz patents, nor the alleged "bundling" supports a claim for unfair competition under state or federal law. In its opposition brief, BrainLAB identified three bases for its unfair competition counterclaim: (1) [§ 2 of the Sherman Act](#); (2) [§ 43\(a\) of the Lanham Act](#), and (3) the Colorado Unfair Practices Act, specifically [C.R.S. § 6-2-108](#) and [§ 6-2-111](#).

The Sherman Act, § 2. In [Walker Process Equip., Inc. v. Food Mach. & Chem. Corp.](#), 382 U.S. 172, 174, 15 L. Ed. 2d 247, 86 S. Ct. 347 (1965), the United States [\*6] Supreme Court held that [HN1](#) enforcement of a patent procured by fraud on the Patent Office may be violative of [§ 2 of the Sherman Act](#) provided the other elements necessary to a [§ 2](#) case are present." BrainLAB has alleged that during the patent application process Dr. Richard Bucholz of St. Louis University misrepresented his inventorship of the 454 and 183 patents by failing to disclose to the Patent Office that Dr. Waldean Schulz was a co-inventor. BrainLAB's affirmative defense of inequitable conduct is premised on its contention that this omission renders the Bucholz patents unenforceable. (Answer to Fourth Am. Compl. PP 67-68). BrainLAB now asserts that the plaintiffs have violated [§ 2 of the Sherman Act](#) by bringing suit on the Bucholz patents, knowing these patents are unenforceable. BrainLAB's position is that its unfair competition claim encompasses a *Walker Process* antitrust claim.

BrainLAB never pleaded a claim arising under [§ 2 of the Sherman Act](#), and it did not reveal during discovery that it was pursuing a *Walker Process* antitrust claim. BrainLAB's effort to include a claim under [§ 2 of the Sherman Act](#) within its claim for unfair competition is untimely.

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<sup>1</sup> Surgical Navigation Technologies, Inc. ("SNT") is now known as Medtronic Navigation, Inc. Medtronic Navigation, Inc. has been substituted for SNT as a plaintiff in this action.

[\*7] The *Lanham Act*. BrainLAB next argues that the plaintiffs have engaged in unfair competition prohibited under the Lanham Act by bringing suit on the allegedly unenforceable Bucholz patents, and by using the Bucholz patents as a marketing tool.

**HN2** [Section 43\(a\) of the Lanham Act](#) provides:

(1) Any person who, on or in connection with any goods or services, or any container

for goods, uses in commerce any word, term, name, symbol, or device, or any combination thereof, or any false designation of origin, false or misleading description of fact, or false or misleading representation of fact, which --

(A) is likely to cause confusion, or to cause mistake, or to deceive as to the affiliation, connection, or association of such person with another person, or as to the origin, sponsorship, or approval of his or her goods, services, or commercial activities by another person, or

(B) in commercial advertising or promotion, misrepresents the nature, characteristics, qualities, or geographic origin of his or her or another person's goods, services, or commercial activities,

shall be liable in a civil action by any person who believes that he or she is or is [\*8] likely to be damaged by such act.

[15 U.S.C. § 1125\(a\)\(1\)](#). **HN3** Enforcement of a patent alleged to have been obtained through inequitable conduct in the Patent Office does not give rise to a claim under the Lanham Act. [Pro-Mold and Tool Co. v. Great Lakes Plastics, Inc., 75 F.3d 1568, 1575 \(Fed. Cir. 1996\)](#). **HN4** Marketplace communications by a patentee concerning its patent may be actionable under the Lanham Act where the marketplace conduct is undertaken in bad faith. [Zenith Elecs. Corp. v. Exzec, Inc., 182 F.3d 1340, 1353 \(Fed. Cir. 1999\)](#).

BrainLAB has submitted four documents that it contends are evidence of misleading market-directed statements made by SNT. One is an article from the St. Louis Business Journal dated February 12, 2004. (Defs.' opp'n br., Ex. D). This article quotes SNT's counsel as stating that Dr. Bucholz's invention made neurosurgery "much more accurate than it was 10 years ago." The second document is a press release issued by St. Louis University on March 10, 2003. (Ex. E). This press release states that "Bucholz's earlier patented image guided surgical tool, the StealthStation, registers objects that don't [\*9] move in relation to each other -- the skull and the brain -- and gives the physicians control of precise movements during surgery." The third document is an article from the St. Louis Business Journal dated February 15, 2002, describing SNT's StealthStation as the brain mapping device invented and patented by Dr. Bucholz. (Ex. F). The fourth document is a selection from the User Manual for the StealthStation's Spine Software. (Ex. H). The manual refers to the spine application as including the patented Bucholz concept of providing free-hand localization and dynamic referencing. BrainLAB characterizes these documents as showing that SNT has used the Bucholz patents as a marketing tool, knowing that the Bucholz patents were fraudulently procured.

The evidence submitted by BrainLAB is not sufficient to support a Lanham Act claim. In *Zenith*, the alleged wrongful acts of the patentee were statements to customers that a competitor's products infringed its patents and representations that its patents could not be designed around. There is no evidence of conduct of that nature by the patentee in this case. BrainLAB has not submitted any evidence showing that SNT disparaged BrainLAB's products [\*10] through marketplace communications. There is no evidence that SNT represented itself to be the exclusive source of image guided surgery equipment. BrainLAB emphasizes Exhibit E, the press release dated March 10, 2003, in which Dr. Bucholz is quoted as saying, "Almost no one does intracranial surgery without image guidance now." Contrary to BrainLAB's contention, this press release does not imply that SNT is the exclusive source of image guided surgery equipment. Moreover, BrainLAB has not shown that the purportedly misleading statements were likely to cause confusion among consumers or influence purchasing decisions.

The *Colorado Unfair Practices Act*. The other prong of BrainLAB's unfair competition claim involves an alleged bundling scheme by two Medtronic entities, SNT and Medtronic Sofamor Danek. BrainLAB does not assert that these entities engaged in any tying arrangements prohibited by **antitrust law**, but it contends that the alleged

bundling violated the federal Anti-Kickback statute, [42 U.S.C. § 1320a-7b](#). [HN5](#) [↑] Subsection (b)(2)(B) of that statute makes it a criminal offense to offer any compensation to induce any person to purchase any good for which [\*11] payment may be made under a Federal health care program.

[HN6](#) [↑] The Anti-Kickback statute is a criminal statute and does not provide a private right of action. BrainLAB apparently concedes this point, arguing instead that SNT's bundling activities violated the following provision of the Colorado Unfair Practices Act:

[HN7](#) [↑] The secret payment or allowance of rebates, refunds, commissions, or unearned discounts, whether in the form of money or otherwise, or secretly extending to certain purchasers special services or privileges not extended to all purchasers upon like terms and conditions, to the injury of a competitor and where such payment or allowance tends to destroy competition, is an unfair trade practice.

[C.R.S. § 6-2-108](#). [HN8](#) [↑] A private right of action is provided in [C.R.S. § 6-2-111\(1\)](#):

[HN9](#) [↑] Any person, firm, private corporation, municipal corporation, public corporation, or trade association may maintain an action to enjoin a continuance of any act in violation of sections 6-2-103 to 6-2-108 or section 6-2-110 and, if injured thereby, for the recovery of damages. If, in such action, the court finds that the defendant is [\*12] violating or has violated any of the provisions of sections 6-2-103 to 6-2-108 or section 6-2-110, it shall enjoin the defendant from a continuance of the violations. It shall not be necessary that actual damages to the plaintiff be alleged or proved. In addition to such injunctive relief, the plaintiff in said action shall be entitled to recover from the defendant three times the amount of the actual damages, if any, sustained.

BrainLAB argues that its counterclaim for unfair competition encompasses a claim under these Colorado statutes.

BrainLAB's claim under the Colorado Unfair Practices Act is untimely. BrainLAB did not specifically plead this statutory claim. In its response to the plaintiffs' contention interrogatories BrainLAB did not identify these statutes as providing a basis for its unfair competition counterclaim. At this stage, BrainLAB cannot assert a claim under the Colorado Unfair Practice Act under the broad label of unfair competition.

In addition, [HN10](#) [↑] an element of a claim under [C.R.S. § 6-2-108](#) is *injury of a competitor*, and BrainLAB has provided no evidence showing that it was injured as a result of the alleged bundling activities. [\*13] BrainLAB merely asserts that the offering of illegal and secret discounts harms competition generally. BrainLAB's claim under the Colorado Unfair Practices Act fails for this reason as well.

Based on the foregoing, it is

ORDERED that the plaintiffs' motion for summary judgment dismissing defendants' unfair competition counterclaim is granted; it is

FURTHER ORDERED that the plaintiffs' unopposed motion filed February 18, 2005, for permission to file under seal Appendices 3-10 to their memorandum in support of plaintiffs' motion for summary judgment on defendants' counterclaim for unfair competition is granted.

Dated: July 14th, 2005

BY THE COURT:

Richard P. Matsch, Senior District Judge

## In re Enron Corp.

United States Bankruptcy Court for the Southern District of New York

July 18, 2005, Decided

Chapter 11, Case No. 01 B 16034 (AJG) (Confirmed)

**Reporter**

2005 Bankr. LEXIS 3471 \*; 2005 WL 3873895

In re: ENRON CORP., et al., Reorganized Debtors.

**Notice:** NOT FOR PUBLICATION

### **Core Terms**

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filed rate doctrine, electricity, Claimants, tariff, preemption, rates, wholesale, energy, cases, state law claim, anti-trust law, market-based, regulation, preempted, markets, sales, violations, state law, anti-competitive, interstate, manipulation, transactions, antitrust, refunds, Federal Power Act, commerce, entities, reasons

### **LexisNexis® Headnotes**

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Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > Preemption

#### [HN1](#) [down arrow] **Federal Common Law, Preemption**

Federal preemption of state law is rooted in the [Supremacy Clause, U.S. Const. art. VI, cl. 2](#). Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted.

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > Preemption

#### [HN2](#) [down arrow] **Federal Common Law, Preemption**

In the absence of an express preemption by Congress, state law is preempted (1) when Congress intends that federal law occupy a given field (field preemption), and (2) to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN3[ Deceptive & Unfair Trade Practices, State Regulation**

State actions against wholesale electricity suppliers alleging violations of California's unfair business practices law, [Cal. Bus. & Prof. Code § 17200](#), are preempted by Federal Power Act where the conduct the state sought to condemn was expressly governed by tariffs and encroach upon the substantive provisions of the tariff, an area reserved exclusively to the Federal Energy Regulatory Commission, both to enforce and to seek remedy.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN4[ Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) has been granted broad authority by Congress, in addition to the authority to determine the just and reasonable rates for wholesale power. The statute delegates to the FERC exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states. Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states. [16 U.S.C.S. §§ 824-824m](#).

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN5[ Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rule making rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, [16 U.S.C.S. §§ 824d, 824e](#); Department of Energy Organization Act, [42 U.S.C.S. § 7173\(c\)](#).

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

### **HN6[ Filed Rate Doctrine, Public Utilities & Telecommunications Carriers**

"Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include (a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; (b) unexplained or unusual redeclarations of availability; (c) unusual trades or transactions; (d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and (e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

### **HN7[ Electric Power Rates, Filed Rate Doctrine**

The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### [\*\*HN8\*\*](#) **Federal Power Act, Federal Rate Regulation**

Reporting requirements are an integral part of a tariff, with Federal Energy Regulatory Commission's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates.

Energy & Utilities Law > Electric Power Industry > Federal Power Act > Judicial Review

#### [\*\*HN9\*\*](#) **Federal Power Act, Judicial Review**

Implicit in Federal Energy Regulatory Commission (FERC) orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.

Energy & Utilities Law > Electric Power Industry > Federal Power Act > Judicial Review

#### [\*\*HN10\*\*](#) **Federal Power Act, Judicial Review**

The filed rate doctrine applies where marketers had not properly reported to Federal Energy Regulatory Commission (FERC), where such improper reporting affected the reasonableness of the tariff approved by FERC.

Civil Procedure > Pleading & Practice > General Overview

#### [\*\*HN11\*\*](#) **Civil Procedure, Pleading & Practice**

Injury implies violation of a legal right.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### [\*\*HN12\*\*](#) **Electric Power Rates, Filed Rate Doctrine**

Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged.

Energy & Utilities Law > Electric Power Industry > Federal Power Act > Judicial Review

## HN13[] Federal Power Act, Judicial Review

Remedies for breach and non-performance of Federal Energy Regulatory Commission (FERC)-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

## HN14[] Electric Power Rates, Filed Rate Doctrine

The filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate making process would subvert the authority of rate-setting bodies and undermine the regulatory regime.

**Counsel:** [\*1] For Reorganized Debtors, Special Counsel: Edward A. Smith, Esq., Of Counsel, CADWALADER, WICKERSHAM & TAFT LLP, New York, NY; Mark C. Ellenberg, Esq., David F. Williams, Esq., Of Counsel, Washington, DC.

For Fallbrook Public Utility District, Borrego Water District, Ramona Municipal Water District, Vista Irrigation District, and Yuima Municipal Water District: C. Michael Cowett, Esq., Robert J. Hanna, Esq., James B. Gilpin, Esq., Mary E. Coburn, Esq., Of Counsel, BEST BEST & KRIEGER LLP, San Diego, CA.

**Judges:** Arthur J. Gonzalez, UNITED STATES BANKRUPTCY JUDGE.

**Opinion by:** Arthur J. Gonzalez

## Opinion

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OPINION SUSTAINING DEBTORS' OBJECTION TO PROOF OF CLAIM NO. 12233, FILED BY FALLBROOK PUBLIC UTILITY DISTRICT; TO PROOF OF CLAIM NO. 12234, FILED BY BORREGO WATER DISTRICT; TO PROOF OF CLAIM NO. 12235 FILED BY RAMONA MUNICIPAL WATER DISTRICT; TO PROOF OF CLAIM NO. 12236 FILED BY VISTA IRRIGATION DISTRICT; AND TO PROOF OF CLAIM NO. 12237 FILED BY YUIMA MUNICIPAL WATER DISTRICT REGARDING STATE LAW CLAIMS IN ELECTRICITY MARKET

ARTHUR J. GONZALEZ

United States Bankruptcy Judge

On October 11, 2002, claimants' counsel filed separate proofs of claims (the "Claims") in unliquidated amounts on behalf of Vista Irrigation District, [\*2] Borrego Water District, Ramona Municipal Water District, Fallbrook Public Utility District and Yuima Municipal Water District (collectively ,the "Claimants") against Enron Corporation ("Enron") and certain of its affiliated entities (collectively, the "Debtors") in the following cases (Claim Nos. 12233, 12234, 12235, 12236, 12237). The claims are based on actions filed by the Claimants and other plaintiffs against Enron Energy Services, Inc. ("EESI"), Enron Power Marketing, Inc. ("EPMI") and other defendants in the Superior Court of the State of California for San Diego County.

The Claimants allege that the Debtors manipulated energy markets in California and overcharged for energy through unlawful and anti-competitive acts during the western power crisis of 2000 and 2001. They maintain the alleged manipulation in the electricity market constitutes a violation of state antitrust law and unfair competition

law, and seek disgorgement, restitution, actual and treble damages together with interest and injunctive relief<sup>1</sup>. On February 18, 2005, the Debtors filed objections to the Claimants' state law claims and argued that the Federal Power Act (the "FPA") preempts the state laws and the [\*3] filed rate doctrine precludes consideration of these claims.

The issue before the Court is whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine. The Court finds that because the Federal Energy Regulatory Commission ("FERC") has exclusive jurisdiction over interstate sales of wholesale electricity, the state law claims sought to be enforced by Claimants in the prosecution of the Claims are preempted by the FPA. Further, the filed rate doctrine precludes consideration of such Claims.

## I. BACKGROUND

Commencing on December 2, 2001, and from time to time continuing [\*4] thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the "Plan") in these cases. The Plan became effective on November 17, 2004.

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, the California legislature had passed Assembly Bill 1890<sup>2</sup> (the "Bill") to create two non-governmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. [California v. Dynegy, Inc., 375 F.3d 831, 850 \(9th Cir. 2004\)](#). The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. [\*5] Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC found that the Debtors engaged in gaming<sup>3</sup> in the form of inappropriate trading strategies and further engaged in the deliberate submission of false information or the deliberate omission of material information. [Enron Power Mktg., Inc., et al., 106 FERC ¶ 61,024 \(2004\)](#). Both proceedings are ongoing, including the determination of remedies by FERC.

## II. DISCUSSION

### A. Legal Standard of Preemption

<sup>1</sup> Claimants allege that the Debtors' violation of the Cartwright Act, the Unfair Competition Law and the California Commodity Law. The Cartwright Act prohibits agreements "to limit or reduce the production, or increase the price of merchandise or of any commodity." [Cal. Bus. & Prof. Code § 16720\(b\)](#). The Unfair Competition Law prohibits unlawful, unfair, or fraudulent business acts and practices. [Cal. Bus. & Prof. Code § 17200](#). The California Commodity Law prohibits fraudulent acts or conduct in connection with the purchase or sale of a commodity. [Cal. Corp. Code §§ 29536-37](#).

<sup>2</sup> 1996 Cal. Stat. 854

<sup>3</sup> The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule . . . to the detriment of the efficiency of, and of consumers in, the ISO markets." [Am. Electric Power Service Corp., et al., 103 FERC ¶ 61,345, 62,330 \(2003\)](#).

**HN1**[] "Federal preemption of state law is rooted in the [Supremacy Clause, Article VI, clause 2, of the United States Constitution](#)." *Transmission Agency of Cal. v. Sierra Pacific Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests intent to occupy an entire [\*6] regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. [Metro. Life Ins. Co. v. Taylor](#), 481 U.S. at 63-64 (1987). Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction. [Caterpillar, Inc. v. Williams](#), 482 U.S. 386, 107 S. Ct. 2425, 96 L. Ed. 2d 318 (1987).

Here, neither party raises the argument that complete preemption is applicable, nor is there any evidence in the record that would support the conclusion that Congress intended for complete preemption to apply in this case.

**HN2**[] In the absence of an express preemption by Congress, state law is preempted (1) "when Congress intends that federal law occupy a given field." [Silkwood v. Kerr-McGee Corp.](#), 464 U.S. 238, 248, 104 S. Ct. 615, 78 L. Ed. 2d 443 (1984) ("Field Preemption"), and (2) "to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* ("Conflict Preemption").

## B. Field Preemption

The Debtors, in support of their position that the state law claims should be barred by FERC's exclusive jurisdiction, [\*7] cite to [Grays Harbor v. IDACORP Inc.](#), 379 F.3d 641 (9th Cir. 2004), *Dynegy*, and  [Snohomish County v. Dynegy Power Marketing Inc.](#), 384 F.3d 756 (9th Cir. 2004). These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The Debtors argue that state law claims in the instant case, alleging violations of state antitrust and unfair competition law, are nearly identical to those involved in the cited cases, and for the reasons set forth in those cases, field preemption is applicable here.

The *Dynegy* court ruled that **HN3**[] "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." [375 F.3d at 852](#).

The Court finds that the statute's framework under the FPA supports the conclusion in *Dynegy* that **HN4**[] FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale [\*8] power. The statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states . . . . Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states." Federal Power Act, [16 U.S.C. § 824-824m](#).

Claimants do not dispute that the transactions at issue involved wholesale interstate sales. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute should be characterized as either retail sales of electricity or wholesale intrastate sales. The statute provides that upon a determination by FERC that "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, *the Commission shall determine* the just and reasonable rate, charge, [\*9] classification, rule, regulation, *practice, or contract* to be thereafter observed and in force, and shall fix the same by order." Federal Power Act, [16 U.S.C. § 824e](#) (emphasis added).

Moreover, pursuant to the statute, **HN5**[] FERC possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, §§ 205, 206(a), as amended, [16 U.S.C.A. §§ 824d, 824e](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.A. § 7173\(c\)](#).

In addition, after the deregulation of California energy markets, the central transactions, the wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded, "FERC is doing enough regulation to justify federal preemption [\*10] of state laws under the market-based system of setting wholesale electricity rates." *Snohomish, 384 F.3d at 760-61*. For instance,

(1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and the ISO. FERC approved the market-based tariffs only upon a showing that the seller lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under FPA §205(c) [16 U.S.C. §824d\(c\)](#). (3) FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, "[e]ach participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market." *Id.*

The Court also recognizes that "entities that transact through the ISO or [the] PX and engage in improper practices<sup>4</sup> are in violation of filed tariffs . . . . FERC and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement." [103 FERC ¶ 62,334](#). Here, Claimants do [\*11] not dispute the fact that it procured electricity through the market administered by the ISO.

Moreover, the Court finds that *Otter Tail Power Co. v. United States, 410 U.S. 366, 93 S. Ct. 1022, 35 L. Ed. 2d 359 (1973)*, and *California v. Federal Power Commission, 369 U.S. 482, 82 S. Ct. 901, 8 L. Ed. 2d 54 (1962)* are not controlling in the instant case. In both cases, [\*12] the Supreme Court found that Congress does not intend to bar governments from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions. However, two important differences exist. First, both cases discussed issues of the interaction between federal administrative law and federal **antitrust law**; thereby no state law preemption issue was presented in these cases. In *California v. Federal Power Commission*, a gas company filed a motion to dismiss the antitrust suit pursuant to the Clayton Act, § 7 as amended [15 U.S.C.A. §18](#), or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's assets pursuant to the Natural Gas Act (the "NGA"), § 7(c) as amended [15 U.S.C.A. §717f\(c\)](#), before the *Power Energy Commission. 369 U.S. at 483*. In *Otter Tail Power*, the government brought an action against an electric power company to enjoin violations of the Sherman Act, [15 U.S.C.A. §2. 410 U.S. at 368](#). In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws. The Court will not address whether, as a result, Congress has left room for enforcement [\*13] of state antitrust laws.

Second, and more importantly, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC. As the Court discussed above, the statute under [16 U.S.C.A. §§ 824d, 824e\(a\)](#) provides FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." [103 FERC at ¶ 62,331](#). Further, "implicit in Commission orders granting market-based rates to the marketers

<sup>4</sup> Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. [HN6](#) [↑] "Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges." *Am. Elec. Power Serv. Corp., et al., 103 FERC at ¶ 62,332 (2003)*.

is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were [\*14] and are subject to revocation of their market-based rate authority." [106 FERC ¶ 61,024](#).

In contrast, the court in [California v. Federal Power Commission](#) concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the Clayton Act. [369 U.S. at 485](#). "The Commission's standard, set forth in § 7 of the NGA, will serve 'the public convenience and necessity.' If existing natural gas companies violate the antitrust laws, the Commission is directed by [§ 20\(a\)](#) to 'transmit such evidence' to the Attorney General." [Id. at 486](#). Similarly, the Court in *Otter Tails* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the Sherman Act. [410 U.S. at 375](#). Moreover, the Supreme Court in [Carnation Co. v. Pacific Westbound Conference](#), [383 U.S. 213, 383 U.S. 932, 86 S. Ct. 781, 15 L. Ed. 2d 709 \(1966\)](#) declined to grant antitrust immunity to a shipping company because "the provisions of the Shipping Act, 46 U.S.C.A. §801, can not reasonably be construed as an implied repeal of antitrust regulation of the shipping industry's rate-making activities." [Id. at 217](#). The Shipping Act does not give the Federal Maritime Commission (the "FMC") [\*15] any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. [Square D Co. v. Niagara Frontier Tariff Bureau](#), [476 U.S. 409, 422, 106 S. Ct. 1922, 90 L. Ed. 2d 413 \(1986\)](#).

The Court further finds that [Grays Harbor](#) and [Gulf States Util. Co. v. Alabama Power Co.](#), [824 F.2d 1465 \(5th Cir. 1987\)](#) are not applicable in the instant case. The courts in both cases concluded that the state law claims concerning contractual disputes were not within the scope of FERC's jurisdiction. The Court finds that the facts here are distinguishable. First, the state law claims in the cited cases were related to contractual issues, which exclusively fall within a state's jurisdiction. The court in *Grays Harbor* granted the utility leave to amend its complaint to seek declaratory relief only as to issues of contract formation. [379 F.3d. at 652-53](#). Similarly, the court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. [824 F.2d at 1474](#). Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily [\*16] intrude upon the rate-setting jurisdiction of FERC. [Grays Harbor, 379 F.3d. at 653](#). Therefore, field preemption bars the Claimants from pursuing its state law claims before the Court.

### C. Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court concludes that FERC has broad authority concerning anti-competitive activities related to the filed rate, apart from that FERC has authority to determine the "just and reasonable" rates for wholesale power. A conflict between the FPA in which grants FERC jurisdiction over the anti-competitive acts and state antitrust claims exists. Accordingly, conflict preemption also bars the Claimants from pursuing state law claims before the Court.

### D. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. [HN7](#) The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions [\*17] are carried out with reference to a filed tariff. *E.& J. Gallo Winery v. Encana Energy Servs., Inc.*, Case No.CV F 03-5412 AWILJO. at 15. The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority." [Ark. L.A. Gas Co. v. Frank Hall](#), [453 U.S. 571, 577-78, 101 S. Ct. 2925, 69 L. Ed. 2d 856 \(1981\)](#). The Court also acknowledges that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates

of which the agency has been made cognizant." [\*City of Cleveland v. FPC\*, 525 F.2d 845, 854, 174 U.S. App. D.C. 1 \(D.C. Cir. 1976\).](#)

In addition, FERC requires each seller to file quarterly reports pursuant to FPA §205(c) [16 U.S.C. § 824d\(c\)](#) on transaction-specific information about its sales and purchases at market-based rates. The Debtors alleged violations of the filing requirements do not preclude FERC from challenging the rate. [\*California v. FERC\*, 383 F.3d 1006, 1016 \(9th Cir. 2004\).](#)

Further, the Court agrees with the opinion of the [\*California v. FERC\*](#) court which concluded that [HN8](#) "the reporting requirements [\*18] are an integral part of a tariff, with FERC's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [383 F.3d at 1016](#). On August 13, 2002, FERC's Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.<sup>5</sup> Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. [106 FERC ¶ 61,024](#). As noted by FERC,

[HN9](#) implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market shares) that reflect a departure [\*19] from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in [\*California v. FERC\*](#), indirectly recognized the application of [HN10](#) the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. [383 F.3d at 1016](#).

Without the availability of retroactive refunds, "[p]arties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

The Court finds that determining the liability or the legal right of Claimants against the Debtors for violation of the antitrust laws would have to be measured by the tariff. Therefore, the filed rate doctrine would be applicable.

In addressing the right of action that [\*20] a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in [\*Keogh v. Chicago & N.W.R.Y. Co.\*, 260 U.S. 156, 43 S. Ct. 47, 67 L. Ed. 183 \(1922\)](#), stated that [HN11](#) "[i]njury implies violation of a legal right." [Id. at 163](#). The Supreme Court concluded that "the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff." [Id. at 163](#). Justice Brandeis explained "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce. Under Section 8 of the latter act . . . the exaction of any illegal rate makes the carrier liable to the 'person injured thereby for the full amount of damages sustained in consequence of any such violation.'" [Id. at 162](#). Thus, the finding of liability in antitrust laws would be integral to the Court's determination of whether the Debtors are liable due to their violations of state **antitrust law** and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first [\*21] deciding the reasonableness of the filed tariff.

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<sup>5</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, as required under their market-based rate authorization. [106 FERC ¶ 61,024](#).

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. "In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company." [453 U.S. at 579](#). The Supreme Court rejected this argument by reasoning that "the mere fact that respondents brought this suit under state law would not rescue it, for when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce . . . [HN12](#)[] Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged." [Id. at 580-84](#).

Moreover, to award monetary relief, the Court would have to determine a "fair price." Thus, the filed rate doctrine bars the Court from awarding monetary damages sought by Claimants. Nonetheless, the Court finds that injunctive relief would also be unavailable to Claimants. The Court agrees with the [\*22] Ninth Circuit's decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. [384 F.3d at 762](#). [HN13](#)[] "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC." *Dynegy*, [375 F.3d at 836](#).

The decisions from the Second Circuit in *Sun City Taxpayers' Association v. Citizens Utilities Co.*, [45 F.3d 58 \(2d Cir. 1995\)](#) and *Wegoland Ltd. v. NYNEX Corp.*, [27 F.3d 17 \(2d Cir. 1994\)](#), provide an additional basis for dismissal of the Claims sought by Claimants. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. *Sun City Taxpayers' Ass'n v. Citizens Utils. Co.*, [847 F.Supp.281, 291 \(D. Conn. 1994\)](#). The Second Circuit in *Wegoland* recognized that [HN14](#)[] the filed rate doctrine exists for reasons independent of the [\*23] type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. [27 F.3d at 21](#).

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects Claimants' challenge to the application of the filed rate doctrine. Accordingly, the filed rate doctrine bars the relief sought by Claimants.

### III. Conclusion

For the foregoing reasons, the Court concludes that the state law claims sought by Claimants concerning electricity market manipulation are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims filed by claimants.

Counsel [\*24] for the Debtors is directed to settle an order consistent with this Court's Memorandum Opinion.

Dated: New York, New York

July 18, 2005

**/s/ Arthur J. Gonzalez**

UNITED STATES BANKRUPTCY JUDGE

## In re Acacia Media Techs. Corp.

United States District Court for the Northern District of California, San Jose Division

July 19, 2005, Decided ; July 19, 2005, Filed

NO. C 05-01114 JW

**Reporter**

2005 U.S. Dist. LEXIS 37009 \*; 2005 WL 1683660

In re: ACACIA MEDIA TECHNOLOGIES CORPORATION.

**Subsequent History:** Patent interpreted by [Acacia Media Techs. Corp. v. New Destiny Internet Group, 405 F. Supp. 2d 1127, 2005 U.S. Dist. LEXIS 38810 \(N.D. Cal., Dec. 7, 2005\)](#)

**Prior History:** [Acacia Media Techs. Corp. v. New Destiny Internet Group, 2004 U.S. Dist. LEXIS 13415 \(C.D. Cal., July 12, 2004\)](#)

## **Core Terms**

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patents, Counterclaim, lawsuit, abuse of process, motion to dismiss, patent infringement, injunctions, default, unfair, alleges, video, baseless, media, initiated, infringe, knowingly false, entertainment, Technologies, antitrust, practices, threatens, abused

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

### **HN1[ Motions to Dismiss, Failure to State Claim**

A [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss tests the legal sufficiency of the claims stated in a complaint. In ruling on a motion to dismiss, the court must accept as true all allegations of material fact and must construe said allegations in the light most favorable to the non-moving party. Any existing ambiguities must be resolved in favor of the pleading. A [Rule 12\(b\)\(6\)](#) motion to dismiss must not be granted unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief. A [Rule 12\(b\)\(6\)](#) motion to dismiss for failure to state a claim is viewed with disfavor and is rarely granted. A motion to dismiss a counterclaim under [Rule 12\(b\)\(6\)](#) is treated the same as a motion to dismiss a complaint.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

Torts > Business Torts > Unfair Business Practices > General Overview

### **HN2[ Trade Practices & Unfair Competition, State Regulation**

[Cal. Bus. & Prof. Code § 17200](#) prohibits five wrongs: (1) unlawful business acts/practices; (2) unfair business acts/practices; (3) fraudulent business acts/practices; (4) unfair, deceptive, untrue, or misleading advertising; and (5) any act prohibited by [Cal. Bus. & Prof. Code §§ 17500-17577.5](#).

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

Torts > Business Torts > Unfair Business Practices > General Overview

### [HN3](#) Trade Practices & Unfair Competition, State Regulation

Generally speaking, the "unfair" standard under [Cal. Bus. & Prof. Code § 17200](#) is broad by design. The unfair standard is intentionally broad, allowing courts maximum discretion to prohibit new schemes to defraud. However, the California Supreme Court has changed the test of "unfairness" for commercial cases. The California Supreme Court holds that, in cases between business competitors, "unfair" means "conduct that threatens an incipient violation of an antitrust law, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition.

Antitrust & Trade Law > General Overview

Patent Law > Infringement Actions > General Overview

### [HN4](#) Antitrust & Trade Law

Antitrust law covers patent infringement lawsuits initiated in bad faith. Patent infringement actions initiated and conducted in bad faith contribute nothing to the furtherance of the policies of either the patent law or the antitrust law.

Torts > Intentional Torts > Abuse of Process > General Overview

### [HN5](#) Intentional Torts, Abuse of Process

The mere filing of a complaint or maintenance of a lawsuit, even for an improper purpose, does not constitute an abuse of process. It is well settled that the mere filing or maintenance of a lawsuit -- even for an improper purpose -- is not a proper basis for an abuse of process action. The gravamen of abuse of process is not the wrongful initiation of civil proceedings.

Torts > Intentional Torts > Abuse of Process > General Overview

### [HN6](#) Intentional Torts, Abuse of Process

For purposes of the tort of abuse of process, the process that is abused must be judicial process. The essence of the tort lies in the misuse of the power of the court. It is an act done in the name of the court and under its authority for the purpose of perpetrating an injustice. Statements (or misstatements) to the media do not abuse judicial process.

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**Judges:** JAMES WARE, United States District Judge.

**Opinion by:** JAMESWARE

## **Opinion**

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### **ORDER DENYING ACACIA'S MOTION TO DISMISS NEW DESTINY'S EIGHTH COUNTERCLAIM AND GRANTING ACACIA'S MOTION TO DISMISS NEW DESTINY'S NINTH COUNTERCLAIM**

#### **I. INTRODUCTION**

This is a patent infringement lawsuit in which Plaintiff Acacia Media Technologies Corporation ("Acacia") claims that various internet-based adult entertainment providers infringe U.S. Patents Nos. 5,132,992 and 6,144,702, which Acacia owns. In response, Defendant New Destiny Internet Group, LLC ("New Destiny") asserts nine counterclaims against Acacia. Presently before this Court is Acacia's Motion [\*6] to Dismiss New Destiny's Eighth and Ninth Counterclaims for Failure to State a Claim. (See Acacia's Motion to Dismiss Defendants' Eighth and Ninth Counterclaims for Failure to State a Claim, hereinafter "Acacia's Motion," Docket Item No. 43 in Central District of California Case No. SA CV 02-1040.)<sup>1</sup> Based upon the arguments advanced by the parties, and for the reasons set forth below, this Court GRANTS Acacia's Motion in part and DENIES it in part.

#### **II. BACKGROUND**

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<sup>1</sup> Acacia's Motion purports to "move[] to dismiss Defendant Game Link's . . . Eighth . . . and Ninth Counterclaim[s] . . . for failure to state a claim under [Rule 12\(b\)\(6\)](#)." (Acacia's Motion at 1:3-6.) Acacia purports to attach Game Link's Answer and Counter-Claim as Exhibit 1 to its Motion. In fact, Exhibit 1 is Defendant New Destiny's Answer and Counter Claim. (Acacia's Motion Ex. 1.) Accordingly, this Court treats Acacia's Motion as a Motion to Dismiss New Destiny's (not Game Link's) Eighth and Ninth Counterclaims.

New Destiny alleges, [\*7] *inter alia*, that Acacia is and has been "threaten[ing], harass[ing], and intimidat[ing] [New Destiny] and other companies in [New Destiny's] industry into paying [Acacia] for license[s] to patents [that] it and they have not infringed and do not infringe." (New Destiny's Opposition to Acacia's Motion, hereinafter "New Destiny's Opposition," Docket Item No. 188 in Central District of California Case No. SA CV 02-1040, Ex. 1 at 42:12-14.) According to New Destiny, Acacia perceived New Destiny and others in New Destiny's industry as unsophisticated, and so "create[d] an atmosphere of fear so as to force [New Destiny] and other companies in [New Destiny's] industry . . . to pay royalties rather than defend against objectively baseless patent infringement suits." (New Destiny's Opposition Ex. 1 at 42:14-20.) As part of its campaign to "create an atmosphere of fear," Acacia allegedly

mailed documents to [New Destiny] and others in [New Destiny's] industry, falsely stating that Acacia had patent claims covering content delivery methods such as video on demand, audio on demand, and video streaming.' Acacia made no mention in this correspondence that the [\*8] scope of its patent claims was very narrow and covered only very specific systems and methods. Instead Acacia stated, incorrectly and without investigation, that [New Destiny's] systems and methods used Acacia's patented systems and methods.

(New Destiny's Opposition Ex. 1 at 43:2-8.) Furthermore, New Destiny alleges, Acacia repeatedly and publicly overstated the breadth of its patents. (New Destiny's Opposition Ex. 1 at 43:9-13 ("Acacia . . . continued to falsely state that its patents covered all methods and systems for transmitting audio and/or video information in press releases, interviews, and in pleadings to this Court[,] [but] [t]hese public statements all ignored the narrow scope of the claims that were obtained by the named inventors of the patents now allegedly owned by Acacia"); see also New Destiny's Opposition Ex. 1 at 44:8-26, 47:1-15, 47:20-48:7.) "Had Acacia, in fact, conducted . . . analyses [of prior art and other validity issues]," New Destiny alleges, "[Acacia] would have been fully aware of the prosecution histories of its patents and that its patent claims could not be given the broad scope they later urged in their media campaign." (New [\*9] Destiny's Opposition Ex. 1 at 43:24-26.) "As such," New Destiny concludes,

those later claims were knowingly false and intended to intimidate, harass, and instill fear in those companies in [New Destiny's] industry, with the intent of interfering with the business relationships between [New Destiny] and its existing and prospective customers, and to further intimidate companies in [New Destiny's] industry to entering into unnecessary patent royalty agreements.

(New Destiny's Opposition Ex. 1 at 43:26-44:3.) New Destiny claims that Acacia's posturing was part and parcel of its business plan to "secure a revenue stream of some \$ 200 million a year, without writing a single line of code."

(New Destiny's Opposition Ex. 1 at 45:1-2.) To support its claim, New Destiny quotes an article from technologymarketing.com, which allegedly states that:

[Acacia CEO Paul] Ryan and his team of executives decided it would be better for the firm if they could get other companies to pay up without the hassle of forcing them to do so through a lawsuit . . . [.] Acacia also decided that alleged infringers would sign up more quickly if it looked as if everyone else were [\*10] jumping on the bandwagon. Ryan launched a rollout plan that involved convincing a host of smaller firms to sign up, and the subsequent publicizing of those signings in order to create a sense of momentum for Acacia's claims. . . By selecting fragmented markets rather than going after big players like MSN or AOL, Acacia hoped to avoid getting embroiled in a debilitating legal battle. My approach is to get some deals done and get some goodwill,' says Rob Berman, Acacia's senior vp [sic] of business development. I don't want to end up in the bowels of legal hell.' . . . Acacia hoped that the adult entertainment industry would be low-hanging fruit. After all, online adult entertainment is a fragmented and apparently incoherent set of companies, full of business amateurs who, Acacia hoped, would probably rather pay a percentage than get hauled into court.

(New Destiny's Opposition Ex. 1 at 45:3-17.)

On July 14, 2003, in a separate patent infringement lawsuit, Acacia Media Technologies Corporation v. Wild Ventures, LLC, No. SACV 02-1053 AHS (MLGx), which involved the same patents at issue in this lawsuit, Judge Alicemarie Stotler granted Acacia a default judgment and an [\*11] injunction against Defendant Wild Ventures, LLC ("Wild Ventures"). (New Destiny's Opposition Ex. 1 at 45:18-26.) <sup>2</sup> According to New Destiny, "Similar default

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<sup>2</sup> Later, on November 21, 2003, pursuant to stipulation, this Court set aside the default judgment entered against Wild Ventures.

injunctions were entered against Extreme Productions (SACV 02-CV-1062), Go Entertainment (SACV 03-CV-204), Lace Productions (SACV 02-CV-1047), and WebZotic LLC (SACV 02-CV-1065)." (New Destiny's Opposition Ex. 1 at 45:26-46:2.) Thereafter, Acacia allegedly embarked upon a media campaign that misrepresented the nature of the default injunctions. Although the default injunctions were entered because the defendants failed to respond to Acacia's lawsuit, Acacia allegedly told the media that "these rulings vindicated Acacia's claims regarding the allegedly broad scope of its patents." (New Destiny's Opposition Ex. 1 at 46:14-15.) New Destiny cites an article in CNET news.com as an illustration. In it, the author explains that,

The company [Acacia] has won a preliminary injunction against five adult entertainment Web sites, barring them from using on-demand digital video or audio online, or providing advertising links to any other such sites. The ruling was a default decision, after the five companies declined to respond [\*12] to a lawsuit, but does mark the first court validation of sweeping patent claims that could ultimately encompass virtually every site offering online multimedia content. Acacia owns patents on the process of transmitting compressed audio or video, which is one of the most fundamental multimedia technologies used on the Internet. We will not allow for the unauthorized use of our technology,' said Rob Berman, Acacia's general counsel. Although not our preference, we are willing to use the power of the court where necessary to stop unauthorized use.'

(New Destiny's Opposition Ex. 1 at 46:16-27 (first emphasis added).) On July 18, 2003, Rob Berman allegedly told Wired News that "Acacia's patents cover just about every form of digital audio and video distribution . . . [sic] these [sic] kinds of activities violate Acacia's intellectual property rights: pushing MP3s from peer-to-peer groups, streaming newscasts from Internet radio sites and delivering movies through cable networks." (New Destiny's Opposition Ex. 1 at 47:1-5.) Furthermore, on September 12, 2003, and again on September 15, 2003, Acacia allegedly issued press releases, in which it stated "that its DMT [\*13] technology, which is covered by pioneering patents, relates to audio and video transmission and receiving systems, commonly known as audio on-demand, video on-demand, and audio/video streaming, and is used for distributing content via several means including Internet, cable television, direct broadcast satellite, and wireless systems." (New Destiny's Opposition Ex. 1 at 47:20-25.)

New Destiny argues that Acacia's patent infringement and business tort claims against New Destiny are "objectively baseless." (New Destiny's Opposition Ex. 1 at 41:26-42:5, 47:26-27, 48:16-18, 49:4-7.) New Destiny also argues that Acacia's statements to the press are "false, misleading, and intimidating" and "were made . . . with the intent to make others reluctant to engage in . . . business with Defendant, to intimidate others in Defendant's industry into paying Acacia for patent licenses that they did [\*14] not need to enter but entered to avoid further harassment and potential baseless infringement litigation." (New Destiny's Opposition Ex. 1 at 47:26-48:6.) Acacia's conduct, Defendant counterclaims, constitutes Violation of [CAL. BUS. & PROF. CODE § 17200](#) (Eighth Counterclaim) and Abuse of Process (Ninth Counterclaim). (New Destiny's Opposition Ex. 1 at 41:14-49:19.) Acacia here moves to dismiss these counterclaims.

### III. STANDARDS

**HN1** [↑] A [Rule 12\(b\)\(6\)](#) motion to dismiss tests the legal sufficiency of the claims stated in a complaint. In ruling on a motion to dismiss, the court must accept as true all allegations of material fact and must construe said allegations in the light most favorable to the non-moving party. [Western Reserve Oil & Gas Co. v. New](#), [765 F.2d 1428, 1430 \(9th Cir. 1985\)](#). Any existing ambiguities must be resolved in favor of the pleading. [Walling v. Beverly Enterprises](#), [476 F.2d 393, 396 \(9th Cir. 1973\)](#). [Conley v. Gibson](#), [355 U.S. 41, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#), sets forth the strict standard for granting a [Rule 12\(b\)\(6\)](#) motion to dismiss. A [Rule 12\(b\)\(6\)](#) motion to dismiss must not be granted "unless it appears [\*15] beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." [Id. at 45-46](#). As the Ninth Circuit has observed, "The [[Rule 12\(b\)\(6\)](#)] motion to dismiss for failure to state a claim is viewed with disfavor and is rarely granted." [Gilligan v. Jamco Develop. Corp.](#), [108 F.3d 246, 249 \(9th Cir. 1997\)](#). A motion to dismiss a counterclaim under [Rule 12\(b\)\(6\)](#) is treated the same as a motion to dismiss a complaint. [Fabricant v. Sears Roebuck](#), [202 F.R.D. 306, 308 \(S.D. Fla. 2001\)](#) (citing [KRW Sales, Inc. v. Kristel Corp.](#), [154 F.R.D. 186, 187 \(N.D. Ill. 1994\)](#)).

#### IV. DISCUSSION

##### A. New Destiny's Eighth Counterclaim: Violation of CAL. BUS. & PROF. CODE § 17200

New Destiny's Eight Counterclaim against Acacia is for Violation of CAL. BUS. & PROF. CODE § 17200. The purpose of § 17200 is to preserve fair business competition. Cel-Tech Communications, Inc. v. Los Angeles Cellular Tel. Co., 20 Cal. 4th 163, 180, 83 Cal. Rptr. 2d 548, 973 P.2d 527 (1999) (quoting Barquis v. Merchants Collection Ass'n, 7 Cal. 3d 94, 110, 101 Cal. Rptr. 745, 496 P.2d 817 (1972)). [\*16] HN2<sup>↑</sup> Section 17200 prohibits five wrongs: (1) unlawful business acts/practices; (2) unfair business acts/practices; (3) fraudulent business acts/practices; (4) unfair, deceptive, untrue, or misleading advertising; and (5) any act prohibited by CAL. BUS. & PROF. CODE §§ 17500-17577.5. CAL. BUS. & PROF. CODE § 17200; WILLIAM L. STERN, BUS. & PROF. C. § 17200 PRACTICE § 3:13 (2005). Only the first three wrongs are relevant here. (See New Destiny's Opposition at 5:6-6:27 (arguing that New Destiny has alleged that Acacia has engaged in "fraudulent" business acts), 7:1-11:2 (arguing that New Destiny has alleged that Acacia has engaged in "unlawful" business acts), 11:3-13:13 (arguing that New Destiny has alleged that Acacia has engaged in "unfair" business acts).)

At minimum, New Destiny arguably alleges that Acacia engaged in an "unfair" business acts or practices. HN3<sup>↑</sup> Generally speaking, the "unfair" standard under § 17200 is broad by design. STERN, supra, § 3:113 ("The unfair' standard is intentionally broad, allowing courts maximum discretion to prohibit new schemes to defraud") (citing Motors, Inc. v. Times Mirror Co., 102 Cal. App. 3d 735, 740, 162 Cal. Rptr. 543 (1980)). [\*17] However, in Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co., 20 Cal. 4th 163, 83 Cal. Rptr. 2d 548, 973 P.2d 527 (1999), the California Supreme Court changed the test of "unfairness" for commercial cases. Id. § 3:114. In Cel-Tech, the Court held that, in cases between business competitors, "unfair" means "conduct that threatens an incipient violation of an antitrust law, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition." Cel-Tech, 20 Cal. 4th at 187. Acacia and New Destiny dispute whether Cel-Tech's narrower test of "unfairness" applies here. (Acacia's Motion at 4:24 ("Defendant does not come close to pleading an antitrust-related cause of action [as required by Cel-Tech]"); New Destiny's Opposition at 12:23-24 ("Defendant need not satisfy Cel-Tech's test for unfair' to state a claim under section 17200"); Acacia's Reply Brief Re: Acacia's Motion, hereinafter "Acacia's Reply," Docket Item No. 198 in Central District of California Case No. SA CV 02-1040, at 6:5 ("Defendants therefore cannot escape the standard [\*18] set forth in Cel-Tech".)) This Court need not determine whether Cel-Tech's narrower test of "unfairness" applies here as a matter of law because, even if it does, New Destiny states a claim under it.

HN4<sup>↑</sup> Antitrust law covers patent infringement lawsuits initiated in bad faith. As the Ninth Circuit observed in Handgards, Inc. v. Ethicon, Inc., 601 F.2d 986, 993 (9th Cir. 1979),

[Patent] infringement actions initiated and conducted in bad faith contribute nothing to the furtherance of the policies of either the patent law or the antitrust law. The district court was correct in holding, in effect, that such actions may constitute an attempt to monopolize violative of Section 2 of the antitrust law.

New Destiny has alleged that Acacia initiated its patent infringement lawsuit against New Destiny in bad faith. In particular, New Destiny alleges that:

Acacia has (i) made knowingly false and/or misleading statements about the systems and methods covered by its patents; (ii) made knowingly false and misleading statements about the validity of its patents . . . ; (iii) made false statements, without investigations, about alleged infringement of [\*19] its patents by Defendant and others; (iv) filed and is prosecuting objectively baseless patent infringement lawsuits, without pre-suit investigation against Defendant and others in Defendant's industry; (v) filed and prosecuted objectively baseless patent infringement lawsuits, without pre-suit investigation, against companies which Acacia's executives concede to do not even need to license the patents-in-suit; (vi) filed and is prosecuting objectively baseless claims of unfair competition, interference with business advantage, and trade libel against Defendant and others in Defendant's industry; (vii) sought and obtained default injunction orders against certain

companies incorporating knowingly false statement about the scope of its patent claims; and (viii) has touted those default injunction orders in the press to validate its knowingly false statements about the systems and methods covered by its patents.

(New Destiny's Opposition Ex. 1 at 41:21-42:9.) Construing New Destiny's pleading in the light most favorable to it, this Court concludes that New Destiny has alleged conduct that "threatens an incipient violation of an antitrust law, or violates the policy or spirit [\*20] of one of those laws . . . , or otherwise significantly threatens or harms competition." *Cel-Tech, 20 Cal. 4th at 187*; *see also Lynch v. Magnavox Co., 94 F.2d 883 (9th Cir. 1938)* (holding that plaintiff stated an antitrust claim against defendants when it alleged that defendants attempted to monopolize by initiating 55 patent infringement lawsuits and mailing numerous letters threatening to sue for patent infringement); *Kobe, Inc. v. Dempsey Pump Co., 198 F.2d 416 (10th Cir. 1952)* (holding that evidence that patent holders had given wide publicity to the number of patents they held -- many of which had expired -- supported a finding that the patent holders had engaged in monopolistic practices).

Accordingly, this Court DENIES Acacia's Motion to Dismiss New Destiny's Eight Counterclaim for Violation of CAL. BUS. & PROF. CODE § 17200.

## B. New Destiny's Ninth Counterclaim: Abuse of Process

New Destiny's Ninth Counterclaim against Acacia is for Abuse of Process. As far as this Court can tell, New Destiny premises its Abuse of Process counterclaim upon two "abuses" of "process." First, New Destiny [\*21] appears to allege that *this* lawsuit, which New Destiny characterizes as "objectively baseless," is abuse of process. (See New Destiny's Opposition Ex. 1 at 49:5-7 ("Acacia has abused the legal process by instituting and maintaining its objectively baseless patent infringement and business tort claims against Defendant . . . to accomplish a purpose for which the legal system is not designed or intended").) Second, New Destiny appears to allege that Acacia's lawsuits against *others* is abuse of process. (See New Destiny's Opposition Ex. 1 at 45:18-46:27, 47:26-48:7, 48:14-15, 48:21-24 (alleging that Acacia, after obtaining default injunctions against other defendants in other cases, embarked upon a media campaign that misrepresented the nature of the default injunction); *see also* New Destiny's Opposition at 20:19-23 ("Acacia has filed a multitude of dubious lawsuits against defendants it perceived as low-hanging fruit,' then deceptively leveraged publicity generated by those lawsuits to coerce defendants -- and others - - into paying for licenses from Acacia").) Neither of these alleged "abuses" of "process" are a sufficient basis upon which to premise an abuse of [\*22] process claim.

First, HN5 [↑] "[t]he mere filing of a complaint or maintenance of a lawsuit, even for an improper purpose, does not constitute an abuse of process." 6A CAL. JUR. 3D *Assault and Other Willful Torts* § 17 (2003); *see also Loomis v. Murphy, 217 Cal. App. 3d 589, 595, 266 Cal. Rptr. 82 (1990)* ("[I]t is well settled that . . . the mere filing or maintenance of a lawsuit -- even for an improper purpose -- is not a proper basis for an abuse of process action") (citing *Oren Royal Oaks Venture v. Greenberg, Bernhard, Weiss & Karma, Inc.*, 42 Cal. 3d 1157, 1169, 232 Cal. Rptr. 567, 728 P.2d 1202 (1986)); *RESTATEMENT (SECOND) OF TORTS* § 682 cmt. a (1977) ("The gravamen of [abuse of process] . . . is not . . . the wrongful initiation of . . . civil proceedings"); 5 B.E. WITKIN, *SUMMARY OF CALIFORNIA LAW* § 460 (9th ed. 1988) ("Obviously, the mere filing of a lawsuit is not an abuse of process"). Thus, Acacia's initiation of this lawsuit cannot form the basis of New Destiny's abuse of process counterclaim. *See Loomis, 217 Cal. App. 3d at 595* (affirming the dismissal of an abuse of process claim because the pleading "contained no allegations of [\*23] misuse of process other than the filing of the complaint"). New Destiny conclusorily argues that its "allegations are extensive and encompass much more than the mere filing or maintenance of a lawsuit." (New Destiny's Opposition at 22:6-7.) Notably, however, New Destiny fails to support this argument with specific citations to its pleading.

Second, Acacia's other lawsuits against other defendants -- and the default injunctions obtained therefrom -- cannot form the basis of New Destiny's abuse of process counterclaim against Acacia. In every case upon which New Destiny relies, the alleged "process" that the defendants/counterdefendants allegedly "abused" is always directed at the plaintiff/counterclaimant. *See Coleman v. Gulf Ins. Group*, 41 Cal. 3d 782, 788, 226 Cal. Rptr. 90, 718 P.2d 77

(1986) (plaintiff alleged that defendant wrongfully appealed a judgment in plaintiffs favor); *Drum v. Bleau, Fox & Assocs.*, 107 Cal. App. 4th 1009, 1014, 132 Cal. Rptr. 2d 602 (2003) (plaintiff alleged that defendant wrongfully levied plaintiffs bank accounts); *Brown v. Kennard*, 94 Cal. App. 4th 40, 43-44, 113 Cal. Rptr. 2d 891 (2001) (plaintiff alleged that defendant wrongfully levied plaintiff's deposit account); *Clark Equip. Co. v. Wheat*, 92 Cal. App. 3d 503, 526, 154 Cal. Rptr. 874 (1979) [\*24] (counterclaimant alleged that counterdefendant wrongfully obtained two contempt orders against counterclaimant). Here, Acacia's other lawsuits against other defendants -- and the default injunctions obtained therefrom -- simply are too remote to form the basis of *New Destiny*'s abuse of process counterclaim against Acacia.

As a final matter, Acacia's alleged misrepresentations to the media regarding the scope of the default injunctions is not the type of "process" protected by the abuse of process claim.[HN6](#) [↑] "For purposes of the tort of abuse of process, the process that is abused must be *judicial* process. The essence of the tort lies in the misuse of the *power of the court*. It is an act done in the name of the court and under its authority for the purpose of perpetrating an injustice." 6A CAL. JUR. 3D *Assault and Other Willful Torts* § 12 (2003) (emphasis added). Statements (or misstatements) to the media, such as those allegedly made by Acacia, do not abuse judicial process.

Accordingly, this Court GRANTS Acacia's Motion to Dismiss *New Destiny*'s Ninth Counterclaim for Abuse of Process.

## V. CONCLUSION

For the reasons set forth above, this Court DENIES Acacia's [\*25] Motion to Dismiss *New Destiny*'s Eighth Counterclaim and GRANTS Acacia's Motion to Dismiss *New Destiny*'s Ninth Counterclaim.

Dated: July 19, 2005

JAMES WARE

United States District Judge

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## **Briggs & Stratton Corp. v. Kohler Co.**

United States District Court for the Western District of Wisconsin

July 20, 2005, Decided

05-C-0025-C

### **Reporter**

2005 U.S. Dist. LEXIS 14808 \*; 2005 WL 1711154

BRIGGS & STRATTON CORP., Plaintiff v. KOHLER CO., Defendant

**Subsequent History:** Patent interpreted by, Summary judgment granted, in part, summary judgment denied, in part by, Partial summary judgment granted by, Motion to strike granted by, in part, Motion to strike denied by, in part [Briggs & Stratton Corp. v. Kohler Co., 2005 U.S. Dist. LEXIS 26913 \(W.D. Wis., Nov. 3, 2005\)](#)

## **Core Terms**

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patent, antitrust, antitrust claim, consumer, sever, counterclaims, allegations, motion to dismiss, engine, unfair competition, infringement, manufacture, notice, lawn tractor

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > General Overview

### **HN1[] Motions to Dismiss, Failure to State Claim**

A motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#) will be granted only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations of the complaint. In deciding a R. 12(b)(6) motion to dismiss, the court takes as true all well-pleaded facts, drawing all inferences and resolving all ambiguities in favor of the non-moving party.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### **HN2[] Motions to Dismiss, Failure to State Claim**

The Federal Rules of Civil Procedure provide for a system of notice pleading pursuant to [Fed. R. Civ. P. 8](#), which requires only that the plaintiff set out a short and plain statement of the claim showing that the pleader is entitled to

relief. [Fed. R. Civ. P. 8\(a\)\(2\)](#). The primary purpose of [Rule 8](#) is rooted in fair notice: under [Rule 8](#), a complaint must be presented with intelligibility sufficient for a court or opposing party to understand whether a valid claim is alleged and if so what it is. In light of this liberal standard, a party can resist a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion to dismiss by setting out facts sufficient to outline the basis of its claim.

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### [HN3](#) **Pleadings, Rule Application & Interpretation**

Federal pleading rules require that a complaint only give notice of the plaintiff's claim and not that it spell out the facts underlying the claim. Plaintiffs don't have to file long complaints, don't have to plead facts, and don't have to plead legal theories.

Civil Procedure > Parties > Joinder of Parties > Misjoinder

Patent Law > Infringement Actions > General Overview

### [HN4](#) **Joinder of Parties, Misjoinder**

[Fed. R. Civ. P. 21](#) allows a court to sever any claim against a party.

Civil Procedure > Trials > Separate Trials

### [HN5](#) **Trials, Separate Trials**

[Fed. R. Civ. P. 42\(b\)](#) allows a court to conduct separate trials on claims in furtherance of convenience or to avoid prejudice.

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > General Overview

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > Appeals

Civil Procedure > ... > Subject Matter Jurisdiction > Federal Questions > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Copyright Law > ... > Civil Infringement Actions > Jurisdiction > General Overview

Copyright Law > ... > Civil Infringement Actions > Jurisdiction > Federal Court Jurisdiction

### [HN6](#) **Intellectual Property, Bad Faith, Fraud & Nonuse**

The jurisdiction of the United States Court of Appeals for the Federal Circuit does not change upon severance of patent infringement claims from antitrust counterclaims in a suit; the Federal Circuit's jurisdiction is based on the allegations in the complaint. Where a complaint alleges patent infringement claims, the Federal Circuit has

jurisdiction. The Federal Circuit has appellate jurisdiction if the district court's original jurisdiction is based in part on [28 U.S.C.S. § 1338](#), as determined by the plaintiff's well-pleaded complaint.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Trials > Separate Trials

Patent Law > ... > Subject Matter Jurisdiction > Supplemental Jurisdiction > Ancillary Jurisdiction

## [HN7](#) [down] Antitrust & Trade Law, Sherman Act

Separating trials of patent and antitrust claims pursuant to [Fed. R. Civ. P. 42\(b\)](#) is typical. As a general rule, separate trials of patent and antitrust claims further the interests of convenience, expediency and economy.

**Counsel:** [\*1] For BRIGGS & STRATTON CORPORATION, Plaintiffs: DAVID L. DEBRUIN, MARK L. KOVNER, THOMAS O. KUHNS

For KOHLER CO., Defendants: DAVID J. HARTH, HELLER EHRLMAN LLP, MADISON, WI

**Judges:** BARBARA B. CRABB, District Judge

**Opinion by:** BARBARA B. CRABB

## Opinion

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### OPINION AND ORDER

In this patent infringement suit, plaintiff Briggs & Stratton Corp. accuses defendant Kohler Co. of manufacturing and selling a single-cylinder internal combustion engine that infringes plaintiff's U.S. Patents Nos. 6,382,166 and 6,460,502. In response to the lawsuit, defendant has filed six counterclaims, alleging noninfringement, patent invalidity, violations of [15 U.S.C. §§ 1](#) and [2](#) of the Sherman Act, Wisconsin antitrust laws, [Wis. Stat. §§ 133.03](#), [133.04](#), [133.04](#), [133.14](#) and [133.18](#), and Wisconsin common law of unfair competition. Now before the court is plaintiff's motion to dismiss defendant's antitrust and unfair competition counterclaims. Jurisdiction is present. [28 U.S.C. §§ 1331](#) and [1338](#).

The crux of plaintiff's motion is whether defendant's counterclaims meet the liberal pleading standards under [Fed. R. Civ. P. 8\(a\)](#). Plaintiff argues that because defendant has alleged no injury [\*2] to the competitive process and because it fails to plead the elements of any recognized federal or state antitrust claim, this court should grant plaintiff's motion to dismiss defendant's antitrust and unfair competition counterclaims under [Fed. R. Civ. P. 12\(b\)\(6\)](#). In the alternative, plaintiff asks the court to sever the patent claims from the antitrust claims pursuant to [Rule 21](#). In response, defendant contends that its counterclaims meet the notice pleading requirements of [Rule 8\(a\)](#) and that the court can meet plaintiff's concerns about delay, increased complexity of trial and juror confusion by bifurcating the patent and antitrust cases under [Rule 42\(b\)](#), rather than severing them under [Rule 21](#). Because defendant's counterclaims meet the minimal pleading requirements of [Rule 8\(a\)](#), I will deny plaintiff's motion to dismiss. In addition, because both parties agree to bifurcation of the patent and antitrust cases, I will deny plaintiff's motion to sever the antitrust claims under [Rule 21](#) and bifurcate the cases pursuant to [Rule 42\(b\)](#).

For the sole purpose of deciding the motion to dismiss, I find that the well-pleaded allegations of plaintiff's complaint and defendant's answer fairly [\*3] allege the following.

### ALLEGATIONS OF FACT

#### A. Factual Allegations of Complaint

Plaintiff Briggs & Stratton Corporation and defendant Kohler Co. are competitors in the market for the manufacture and sale in the United States of engines used in consumer lawn tractors.

On May 7, 2002, the U.S. Patent and Trademark Office issued U.S. Pat. No. 6,382,166 (the '166 patent) to Daniel L. Klika and John H. Thiermann for an invention entitled "Balancing System Using Reciprocating Counterbalance Weight." On October 8, 2002, the United States Patent and Trademark Office issued U.S. Pat. No. 6,460,502 (the '502 patent) to Gary J. Gracyalny for an invention entitled "Engine Cylinder Head Assembly." By virtue of assignment, plaintiff acquired and continues to maintain all rights, title and interest in the '166 and '502 patents.

Without the permission of plaintiff, defendant manufactures, sells and offers for sale deliberately and willfully in the United States a single-cylinder internal combustion engine that infringes the claims of the '166 patent. In addition, defendant manufactures, sells and offers for sale deliberately and willfully in the United States a single-cylinder internal combustion [\*4] engine that infringes the claims of the '502 patent.

#### B. Factual Allegations of Answer and Counterclaim

According to defendant, the '166 and '502 patents are invalid and void for failing to meet one or more of the conditions for patentability specified in [35 U.S.C. §§ 102, 103](#) and [112](#). In addition, plaintiff has monopoly power in the consumer lawn tractor market, as demonstrated by plaintiff's market share as well as by significant barriers to entry, including the investment, technology and business reputation necessary to manufacture and market the products in the consumer lawn tractor market. Plaintiff has willfully maintained its monopoly power in the consumer lawn tractor market by illegal anticompetitive and exclusionary acts and by engaging in unreasonable agreements in restraint of trade affecting a substantial volume of commerce, including, but not limited to the following: 1) bundling rebates that defendant pays to both its direct purchasers (original equipment manufacturers that incorporate engines into a consumer lawn tractor) and to retailers that sell completed consumer lawn tractors directly to consumers; and 2) entering into exclusionary contracts [\*5] that expressly or effectively require direct purchasers or retailers to deal exclusively with plaintiff and not with its competitors, including defendant. Plaintiff has acted for the purpose and with the effect of obtaining and maintaining monopoly power in the market for engines for consumer lawn tractors and it has excluded competition from that market in violation of the [Sherman Act §§ 1 & 2](#), [Wis. Stat. §§ 133.03, 133.04, 133.05, 133.14](#) and [133.18](#) and Wisconsin unfair competition laws. Plaintiff's monopoly power has not resulted from superior products or business acumen or competition on the merits, but rather from unlawful anticompetitive conduct.

As a result of plaintiff's conduct, consumers have been harmed by having to pay higher prices for products in the consumer lawn tractor market and by being denied choice. In addition, plaintiff's conduct has harmed defendant in its business or property through lost sales and profits. Defendant had a reasonable probability of deriving economic benefit from ongoing and prospective business relationships with third parties involving the sale of products to those parties. Plaintiff interfered with defendant's relationships with its customers [\*6] and prospective customers knowingly and without justification or excuse, causing harm to those relationships and economic loss to defendant.

### DISCUSSION

#### A. Motion to Dismiss

**HN1** [↑] A motion to dismiss under [Fed. R. Civ. P. 12\(b\)\(6\)](#) will be granted only if "it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations" of the complaint. [Cook v. Winfrey, 141 F.3d 322, 327 \(7th Cir. 1998\)](#) (citing [Hishon v. King & Spalding, 467 U.S. 69, 73, 81 L. Ed. 2d 59, 104 S. Ct. 2229, \(1984\)](#); [Gossmeier v. McDonald, 128 F.3d 481, 489 \(7th Cir. 1997\)](#)). In deciding a [Rule 12\(b\)\(6\)](#) motion to dismiss, the court takes as true all well-pleaded facts, drawing all inferences and resolving all ambiguities in favor of the non-moving party. [Dawson v. General Motors Corp., 977 F.2d 369, 372 \(7th Cir. 1992\)](#).

**HN2** [↑] The Federal Rules of Civil Procedure provide for a system of notice pleading pursuant to [Rule 8](#), which requires only that the plaintiff set out a "short and plain statement of the claim showing that the pleader is entitled to

relief." *Fed. R. Civ. P. 8(a)(2)*. "The primary purpose of [Rule 8] is rooted in fair notice: [\*7] under *Rule 8*, a complaint must be presented with intelligibility sufficient for a court or opposing party to understand whether a valid claim is alleged and if so what it is." *Vicom, Inc. v. Harbridge Merchant Services, Inc.*, 20 F.3d 771, 775 (7th Cir. 1994) (citations omitted). In light of this liberal standard, a party can resist a 12(b)(6) motion to dismiss by setting out facts sufficient to outline the basis of its claim. *Panaras v. Liquid Carbonic Indus. Corp.*, 74 F.3d 786, 792 (7th Cir. 1996).

Plaintiff raises two related arguments: 1) defendant lacks standing to bring antitrust claims because it failed to allege injury to the competitive process and instead alleged that it lost business, which is not an antitrust injury; and 2) even if defendant had standing, it failed to allege any facts that amount to a violation of **antitrust law**. Specifically, according to plaintiff, defendant failed to allege what market share plaintiff has, what shares its competitors have or what barriers it has erected to expansion by existing firms such as defendant. Defendant points out correctly that *Rule 8(a)* requires notice pleading only and therefore, its allegations [\*8] are sufficient. Defendant's counterclaims identify the laws under which it is suing and the anticompetitive actions in which plaintiff is engaged, namely 1) bundling rebates that defendant pays to both its direct purchasers and to retailers that sell completed consumer lawn tractors directly to consumers; and 2) entering into exclusionary contracts that expressly or effectively require direct purchasers or retailers to deal exclusively with plaintiff and not with its competitors, including defendant. These allegations are sufficient to put plaintiff on notice of the counterclaims and allow it to file an answer. See, e.g., *Beanstalk Group, Inc. v. AM General Corp.*, 283 F.3d 856, 863 (7th Cir. 2002) **HN3**[<sup>1</sup>] (federal pleading rules require that complaint only give notice of plaintiff's claim and not that it spell out facts underlying claim) (citing *Leatherman v. Tarrant County Narcotics Intelligence & Coordination Unit*, 507 U.S. 163, 168, 122 L. Ed. 2d 517, 113 S. Ct. 1160 (1993); *Kirksey v. R.I. Reynolds Tobacco Co.*, 168 F. 3d 1039, 1041 (7th Cir. 1999)) ("The courts keep reminding plaintiffs that they don't have to file long complaints, don't have to plead facts, don't have [\*9] to plead legal theories.") (citing *Johnson v. Hondo, Inc.*, 125 F.3d 408, 417 (7th Cir. 1997)). Whether defendant will be able to prove facts consistent with its allegations that reveal a violation of **antitrust law** is a matter for summary judgment.

#### B. Motion to Sever

As an alternative to its motion to dismiss, plaintiff asks the court to sever the antitrust claims from the patent claims pursuant to *Rule 21* because the antitrust claims raise different issues and will require different proof. **HN4**[<sup>1</sup>] *Rule 21* allows a court to sever any claim against a party. According to plaintiff, without severance, the jury may become confused regarding damages incurred from the patent infringement claims and the antitrust claims. Furthermore, plaintiff contends, without severance and upon appeal, the Court of Appeals for the Federal Circuit will have to apply the antitrust laws of the Court of Appeals for the Seventh Circuit; severance would allow the Seventh Circuit to hear any appeals regarding the antitrust claims.

Defendant points out that plaintiff's concerns can be addressed by separating the patent and antitrust trials pursuant to **HN5**[<sup>1</sup>] *Rule 42(b)*, which allows a court to conduct separate [\*10] trials on claims in furtherance of convenience or to avoid prejudice and which defendant would be willing to accept. Defendant is correct when it contends that **HN6**[<sup>1</sup>] the Federal Circuit's jurisdiction does not change upon severance of claims; the court's jurisdiction is based on the allegations in the complaint. *Apotex, Inc. v. Thompson*, 347 F.3d 1335, 1343 (Fed. Cir. 2003). Because the complaint in this case alleges patent infringement claims, the Federal Circuit has jurisdiction. *Id.* (Federal Circuit has appellate jurisdiction if district court's original jurisdiction was based in part on *28 U.S.C. § 1338*, as determined by plaintiff's well-pleaded complaint). In addition, **HN7**[<sup>1</sup>] separating trials of patent and antitrust claims pursuant to *Rule 42(b)* is typical. See, e.g., *Brandt, Inc. v. Crane*, 97 F.R.D. 707, 708 (N.D. Ill. 1983) ("As a general rule, separate trials of patent and antitrust claims further the interests of convenience, expediency and economy.") In its reply brief, plaintiff appears to concede that it would be satisfied with a separate trial and separate discovery and pre-trial schedules for the antitrust claims. Plt. [\*11]'s Reply Br., dkt. # 31, at 3. Therefore, I will order the clerk of court to set a scheduling conference to arrange a separate trial date and discovery schedule for defendant's antitrust and unfair competition claims and deny plaintiff's motion to sever those claims from the patent claims as unnecessary.

ORDER

IT IS ORDERED that

1. Plaintiff Briggs & Stratton Corporation's motion to dismiss plaintiff Kohler Co.'s antitrust and unfair competition counterclaims pursuant to Fed. R. Civ. P. 12(b)(6) is DENIED;
2. Plaintiff's motion to sever defendant's antitrust counterclaims from the patent claims pursuant to Fed. R. Civ. P. 21 is DENIED as unnecessary;
3. The clerk of court is directed to set a scheduling conference before the magistrate judge to address bifurcation of the antitrust claims from the patent claims.

Entered this 20th day of July, 2005.

BARBARA B. CRABB

District Judge

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## **eMag Solutions LLC v. Toda Kogyo Corp.**

United States District Court for the Northern District of California

July 20, 2005, Decided ; July 20, 2005, Filed

No. C 02-1611 PJH

### **Reporter**

2005 U.S. Dist. LEXIS 44512 \*; 2005 WL 1712084

eMAG SOLUTIONS LLC; et al., Plaintiffs, v. TODA KOGYO CORPORATION, et al., Defendants.

**Notice:** [\*1] NOT FOR CITATION

**Subsequent History:** Motion denied by [\*eMag Solutions, LLC v. Toda Kogyo Corp., 426 F. Supp. 2d 1050, 2006 U.S. Dist. LEXIS 22543 \(N.D. Cal., 2006\)\*](#)

## **Core Terms**

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commerce, domestic, purchases, export, imports, conspiracy, antitrust, defendants', prices, Sherman Act, eMag, foreign commerce, plaintiffs', bought, anti trust law, but-for, effects, reasonably foreseeable, domestic commerce, manufactured, allegations, anticompetitive conduct, injuries, sales, foreign nation, give rise, price-fixing, causation, inflated, abroad

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For Sakai Trading Inc., Defendant: Joseph Froehlich, Richard E. Donovan, LEAD ATTORNEYS, Kelley Drye & Warren LLP, New York, NY.

For Titan Kogyo Kabushiki Kaisha, Defendant: Jeremy D. Blank, LEAD ATTORNEY, Topel & Goodman, San Francisco, CA; William M. Goodman, LEAD ATTORNEY, LIAISON COUNSEL FOR DEFENDANTS, Topel & Goodman, San Francisco, CA.

For Inabata & Company Ltd., Inabata America Corporation, Defendants: Irving P. Seidman, Lawrence H. Silverman, LEAD ATTORNEYS, Seidman Silverman & Seidman P.C., New York, NY.

For Ishihara Sangyo Kaisha, Ltd., Defendant: Bryan Cave, Louis F. Bonacorsi, LEAD ATTORNEYS, St. Louis, MO; Bryan Dunlap, Mark Hellerer, LEAD ATTORNEYS, Pillsbury Winthrop LLP, New York, [\*4] NY; Daveed A. Schwartz, LEAD ATTORNEY, Pillsbury Winthrop LLP, San Francisco, CA; Paul R. Griffin, Pillsbury Winthrop Shaw Pittman LLP, San Francisco, CA; Sutton Keany, Berger & Webb, LLP, New York, NY.

For ISK Americas Incorporated, ISK Magnetics Inc., Ishihara Corporation, USA, Defendants: Leslie W. Jacobs, Matthew E. Liebson, Thomas James Collin, LEAD ATTORNEYS, Thompson Hine LLP, Cleveland, OH; Christopher B. Hockett, Viveka A. Rydell, Bingham McCutchen LLP, San Francisco, CA.

**Judges:** PHYLLIS J. HAMILTON, United States District Judge.

**Opinion by:** PHYLLIS J. HAMILTON

## Opinion

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### ORDER GRANTING MOTION TO DISMISS

Defendants' motion to dismiss the claims of the foreign plaintiffs for failure to state a claim and for lack of subject matter jurisdiction came on for hearing before this court on May 25, 2005. Plaintiffs appeared by their counsel Eric B. Fastiff, Joseph R. Saveri, Kimberly S. Keevers, and Joshua P. Davis. Defendants Toda Kogyo Corporation and Toda America, Inc. appeared by their counsel Thomas P. Hanrahan. William M. Goodman appeared specially for defendant Titan Kogyo Kabushiki Kaisha. Defendant Sakai Trading New York, Inc. appeared by its counsel Richard E. Donovan and Mia [\*5] S. Blackler, who also appeared specially for defendants Sakai Trading Co. Ltd., and Sakai Chemical Co. Ltd.<sup>1</sup>

Having read the parties' papers and considered the relevant legal authority, and good cause appearing, the court hereby GRANTS the motion as follows.

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<sup>1</sup> Defendants Ishihara Sangyo Kaisha, Ltd. ("ISK"); ISK Americas Incorporated ("ISKA"); ISK Magnetics, Inc. ("ISKM"); and Ishihara Corporation (USA) ("ISK USA") -- collectively, "the ISK defendants" -- did not appear. The parties previously advised the court that plaintiffs and the ISK defendants were in the process of settling.

## BACKGROUND

This is an antitrust case, alleging violations of § 1 of the Sherman Antitrust Act, [15 U.S.C. § 1](#), and filed as a proposed class action seeking damages under §§ 4(a) and 16 of the Clayton Act, [15 U.S.C. §§ 15](#) and [26](#). Plaintiffs are eMag Solutions, LLC (a Delaware limited liability company), and four "foreign plaintiffs" -- eMag Solutions Limited ("eMag [\*6] Wales" -- incorporated under the laws of England and Wales); Greencorp Magnetics Pty Ltd. ("Greencorp" -- incorporated under the laws of Australia); Delta Magnetics, S.A. de C.V. ("Delta" -- incorporated under the laws of Mexico); and Cintas VAC, S.A. de C.V. ("Cintas" -- incorporated under the laws of Mexico). Plaintiffs allege that defendants engaged in a worldwide conspiracy to set the prices of magnetic iron oxide ("MIO"), a substance used in magnetic products such as audio and video tapes.

The action is brought as a proposed class action by four of the plaintiffs as "representative plaintiffs," and by the fifth plaintiff individually. The representative plaintiffs claim to represent a class of persons and entities who purchased MIO from defendants in the United States from 1991 to the present, and a class of United States persons or entities who purchased MIO from defendants from 1991 to the present. They allege that defendants fixed the price of MIO throughout the world, including in the United States.

The ten defendants can be divided into four groups. First is the ISK group, which consists of Ishihara Sangyo Kaisha, Ltd. ("ISK" -- a Japanese corporation); ISK Magnetics, Inc. [\*7] ("ISKM" -- a Delaware corporation); ISK's wholly-owned subsidiary ISK Americas, Incorporated ("ISKA" -- a Delaware corporation); and ISKA's wholly-owned subsidiary, Ishihara Corporation USA ("ISK USA" -- a California corporation).

Second is the Sakai group, which consists of Sakai Chemical Industry Co., Ltd. ("Sakai Chemical" -- a Japanese corporation); Sakai Trading Co., Ltd. ("Sakai Trading" -- a Japanese corporation); Sakai Trading's subsidiary, Sakai Trading New York, Inc. ("Sakai NY" -- a New York corporation); and Sakai Chemical Industry Co., Ltd. ("Sakai Chemical" -- place of incorporation not stated), the parent corporation of Sakai Trading (which in turn is the parent corporation of Sakai NY). Plaintiffs claim that Sakai Trading and Sakai NY are so controlled by Sakai Chemical that each is the alter ego of Sakai Chemical.

Third is Titan Kogyo Kabushiki Kaisha ("Titan" -- a Japanese corporation), which is partially owned by Inabata & Co., Ltd. ("Inabata Japan") and Inabata American Corporation ("Inabata America"). Although the Inabata entities are not named as defendants, plaintiffs assert that each is so controlled by Titan that it is the alter ego of Titan.

Fourth is the [\*8] Toda group, which consists of Toda Kogyo Corporation ("Toda Japan" -- a Japanese corporation); and Toda American, Inc. ("Toda America" -- an Illinois corporation).

The Toda defendants, the Sakai defendants, and Titan now seek an order dismissing the claims asserted against them by the foreign plaintiffs in the Third Amended Complaint ("TAC"), for failure to state a claim and for lack of subject matter jurisdiction. Defendants also contend that the foreign plaintiffs lack standing to assert antitrust claims because foreign harm is not actionable under the antitrust laws, and argue that the TAC fails to adequately plead antitrust injury.

## DISCUSSION

### A. Legal Standards

A court should dismiss under [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) for failure to state a claim only where it appears beyond doubt that plaintiff can prove no set of facts in support of the claim which would entitle the plaintiff to relief. See [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#); [Pillsbury, Madison & Sutro v. Lemer, 31 F.3d 924, 928 \(9th Cir. 1994\)](#). Review is limited to the contents of the complaint. [Allarcom Pay Television, Ltd. v. Gen. Instrument Corp., 69 F.3d 381, 385 \(9th Cir. 1995\)](#). [\*9] All allegations of material fact are taken as true and construed in the light most favorable to the nonmoving party. [Smith v. Jackson, 84 F.3d 1213, 1217 \(9th Cir. 1996\)](#).

The plaintiff bears the burden of demonstrating that subject matter jurisdiction exists over this complaint when challenged under [Fed. R. Civ. P. 12\(b\)\(1\)](#). See, e.g., [Tosco Corp. v. Communities for a Better Env't, 236 F.3d 495, 499 \(9th Cir. 2001\)](#). The defendant may either challenge jurisdiction on the face of the complaint or provide extrinsic evidence demonstrating lack of jurisdiction on the facts of the case. [White v. Lee, 227 F.3d 1214, 1242 \(9th Cir. 2000\)](#). Here, since the defendants challenge jurisdiction on the face of the complaint, all allegations of the complaint are taken as true and all disputed issues of fact are resolved in favor of the non-moving party. See [Love v. United States, 915 F.2d 1242, 1245 \(9th Cir. 1990\)](#).

## B. The Sherman Act and the FTAIA

[Section 1](#) of the Sherman Antitrust Act provides, in part, that "[e]very contract, combination in the form of trust or otherwise, or conspiracy, [\*10] in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." [15 U.S.C. § 1](#). The Foreign Trade Antitrust Improvements Act of 1982 ("FTAIA"), which is an amendment to the Sherman Act, excludes from the Sherman Act's reach "much anticompetitive conduct that causes only foreign injury." [F. Hoffman-LaRoche v. Empagran, 542 U.S. 155, 124 S. Ct. 2359, 2363, 159 L. Ed. 2d 226 \(2004\)](#).

The FTAIA sets forth a general rule that the Sherman Act "shall not apply to conduct involving trade or commerce . . . with foreign nations," [15 U.S.C. § 6a](#), but creates exceptions to that general rule for conduct that significantly harms imports, domestic commerce, or American exporters. This "domestic-injury exception" provides that the Sherman Act is applicable to foreign commerce where the conduct has "a direct, substantial, and reasonably foreseeable effect" (a) on trade or commerce which is not trade or commerce with foreign nations, or on import trade or import commerce with foreign nations; or (b) on export trade or export commerce with foreign nations, of a person engaged in such trade or commerce in the United States, where [\*11] that "direct, substantial, and reasonably foreseeable effect" also "gives rise to a claim" under the Sherman Act. [15 U.S.C. § 6a](#); see also [Empagran, 124 S.Ct. at 2366](#) (under limitations imposed by FTAIA, courts have jurisdiction over Sherman Act claim brought by foreign plaintiff only when plaintiff alleges that defendant's conduct affected U.S. commerce *and* that the effect gave rise to the plaintiff's injury). In addition, if the Sherman Act applies to the alleged anticompetitive conduct only because of the effect on "export commerce with foreign nations, of a person engaged in such trade or commerce in the United States," the Sherman Act applies to such conduct "only for injury to export business in the United States." [15 U.S.C. § 6a](#).

In [Empagran](#), the Court held that foreign purchasers who bought product from the sellers for delivery outside of the United States could not bring a Sherman Act claim based on the foreign effect of foreign anti-competitive conduct where the alleged domestic effect was independent of the foreign effect giving rise to the plaintiffs' claims. [Empagran, 124 S.Ct. at 2363](#). [\*12] The Court stated that application of American antitrust laws to foreign anticompetitive conduct is reasonable only where those laws "reflect a legislative effort to redress *domestic* antitrust injury that foreign anticompetitive conduct has caused." [Id. at 2366](#). That is, where the defendant's conduct affects both domestic and foreign commerce, and the plaintiff's injury arises only from the effect on foreign commerce, the plaintiff's injury is independent from the domestic effect and the court has no jurisdiction. In addition, the Court ruled that the language "gives rise to a claim" (the second part of the FTAIA test) means that the foreign conduct's domestic effect must be sufficient to cause a cognizable injury to the plaintiff or plaintiffs. [Id. at 2371-72](#).

## C. Defendants' Motion to Dismiss for Lack of Jurisdiction and Failure to State a Claim

In the TAC, plaintiffs allege that defendants' conspiracy to fix prices resulted in the sale of MIO at artificially high and non-competitive levels in four categories of commerce -- U.S. imports, purely domestic commerce, U.S. exports, and purely foreign commerce. They allege that ISKM sold MIO in [\*13] purely domestic commerce and as U.S. exports, and that ISK, the Sakai defendants, the Toda defendants, and Titan sold MIO in purely foreign commerce and as U.S. imports. Plaintiffs also assert that direct purchasers of MIO throughout the world were deprived of the benefit of free and open competition in the purchase and pricing of MIO in each of these four categories of commerce, and that plaintiffs and the members of the proposed class paid more for MIO than they would have otherwise paid in the absence of defendants' unlawful conduct. Defendants argue that the action should

be dismissed for lack of subject matter jurisdiction and/or for failure to state a claim as to each of these four categories of commerce.

*sales in "purely foreign" commerce*

In the TAC, plaintiffs allege that eMag Wales and Greencorp (not Delta and Cintas) were injured by their purchases of MIO in "purely foreign" commerce. Plaintiffs claim that eMag Wales purchased MIO manufactured and sold in Japan by Sakai companies and Toda Japan, and delivered to eMag Wales in Wales. They allege that Greencorp purchased MIO manufactured and sold in Japan by Sakai companies and Toda Japan, and delivered to Greencorp in [\*14] Australia.

Defendants argue that plaintiffs' claims for recovery based on "purely foreign" commerce are outside the scope of U.S. antitrust law, and must therefore be dismissed for lack of subject matter jurisdiction. Relying on *Empagran*, defendants contend that the FTAIA generally excludes from the Sherman Act's reach all conduct that involves commerce with foreign countries. [Id. at 2364.](#)

Plaintiffs argue, however, that the FTAIA does not bar their claims of sales in "purely foreign" commerce, and that they have adequately alleged that those sales had an effect on U.S. commerce. In the TAC, plaintiffs assert that the effect of defendants' conspiracy on "purely foreign" commerce was dependent on its effect on "American commerce"<sup>2</sup> in three ways: First, they claim that they "bought MIO in American commerce," and so "would have been particularly well-suited to replace purchases of MIO in purely foreign commerce with purchases of MIO in American commerce, if the conspiracy had not affected the prices of MIO in American commerce." TAC P 85(a). Second, they assert that "defendants' conspiracy to fix prices above competitive levels in American commerce was necessary [\*15] for them to support their conspiracy to fix prices in purely foreign commerce because competition from American commerce would have put downward pressure on sales internationally, including through sales diverted to American commerce and through arbitrage by purchasers in American commerce, and thus the defendants' conspiracy to fix prices in American commerce caused . . . [plaintiffs] to pay artificially high prices for MIO they purchased in purely foreign commerce." TAC P 85(b). Third, they allege that they "used the MIO they bought from the defendants in American and purely foreign commerce to manufacture magnetic tape and other products that they in turn sold in substantial volume in American commerce at prices inflated as a result of the defendants' conspiracy." TAC P 85(c).

Defendants contend, however, that the foreign plaintiffs cannot recover based on their foreign purchases for several reasons. [\*16] They argue that the TAC does not adequately plead that the alleged price fixing of MIO purchased by eMag Wales and Greencorp in "purely foreign" commerce had a direct, substantial, and reasonably foreseeable effect on domestic commerce, or that the alleged harm to the foreign plaintiffs arose from the effect in the United States.

Defendants submit that rather than alleging that a foreign conspiracy had a direct, substantial, and foreseeable domestic effect that caused their injury, the foreign plaintiffs assert that they "pa[id] artificially high prices for MIO they purchased in Purely Foreign Commerce" because they could not engage in "arbitrage" purchases in the U.S. market due to inflated domestic prices for MIO. Defendants contend that not only do such circular allegations not meet the "direct, substantial, and reasonably foreseeable" test because they are entirely speculative and conclusory, but also that the claims in the TAC arise only from the foreign plaintiffs' foreign purchases of MIO, and not from any effect on the foreign plaintiffs in the United States, as required by the FTAIA.

Defendants also contend that policy considerations underlying the Sherman Act and the [\*17] government's deterrence of international cartels will be undermined by permitting plaintiffs' foreign commerce claims to proceed. Defendants point to arguments made in an amicus brief filed in the remanded *Empagran* case (in the D.C. Circuit) by the United States Department of Justice ("DOJ") and the Federal Trade Commission ("FTC"), in which those agencies argued that the FTAIA does not grant jurisdiction over claims of worldwide price-fixing conspiracies in worldwide markets based on theories of arbitrage and "but-for" causation without any specific domestic harm.

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<sup>2</sup> Plaintiffs define "American commerce" as meaning U.S. imports, "purely domestic" commerce, and U.S. exports.

Just as in the present case, the foreign plaintiffs in *Empagran* had argued that defendants' "cartel" would have been unsustainable if the United States had been excluded from it, because plaintiffs would have either purchased in the U.S. at lower prices or from arbitrageurs selling product imported from the U.S. The *Empagran* plaintiffs thus asserted that their injuries would not have occurred "but for" the fact that the cartel included the United States, and that the U.S. effect of the cartel "gave rise to" their claim as required by the FTAIA. The DOJ and the FTC noted that the Supreme Court had rejected plaintiffs' [\*18] argument that their construction of the FTAIA would help deter cartels, in light of "important experience-backed arguments (based on amnesty-seeking incentives)" raised by defendants, the United States, and foreign governments. The DOJ and the FTC argued that permitting cases such as the plaintiffs to proceed would undermine the government's deterrence of cartels, because cartel members who do not qualify for amnesty but might otherwise want to cooperate with the government -- i.e., through plea agreement -- would be discouraged from doing so.

Plaintiffs contend, however, that *Empagran* does not bar all foreign buyers from bringing claims under U.S. **antitrust law** for purchases in "purely foreign" commerce, arguing that the Court ruled that purchasers in foreign commerce may bring claims under U.S. **antitrust law** if their injuries would not have occurred "but for" the domestic effects of anticompetitive conduct (citing [\*Empagran\*, 124 S.Ct. at 2372](#)). They claim in addition that case law allows "purely foreign" commerce claims if the effects in the U.S. are the "but-for" cause of the plaintiff's foreign injuries (citing [\*Sniado v. Bank Austria AG\*, 378 F.3d 210, 213 \(2d Cir. 2004\)](#); [\*19] [\*MM Global Servs., Inc. v. Dow Chem. Co.\*, 329 F.Supp. 2d 337, 342-43 \(D.Conn. 2004\)](#)).

Thus, with regard to the present case, plaintiffs argue that the foreign defendants' international conspiracy had an adverse effect in the United States, and that this effect was a "but-for" cause of plaintiffs' injuries; and they also assert that the domestic effects of defendants' conspiracy were the "but-for" cause of their injuries abroad. They contend that if defendants' conspiracy had not inflated U.S. prices, the foreign plaintiffs would not have been injured because lower American prices would have driven down international prices overall, including through arbitrage; and the domestic effects of the conspiracy caused their injuries because they had already bought some MIO in American commerce and could have purchased the rest of their MIO from the U.S. market had it remained competitive.

The provision in the FTAIA that limits the Sherman Act's application to conduct with a "direct, substantial, and reasonably foreseeable effect" on domestic commerce addresses the court's subject matter jurisdiction over antitrust claims and is not merely an element of the claims. [\*U.S. v. LSL Biotechnologies\*, 379 F.3d 672, 679-80 \(9th Cir. 2004\)](#). [\*20] Accordingly, the court must consider whether plaintiffs have met their burden of showing that the court has jurisdiction over their claims of anticompetitive conduct in "purely foreign" commerce. The court finds that plaintiffs' theory of "but-for" causation - that plaintiffs would have paid lower foreign prices "but for" inflated domestic prices - is not sufficient to support a claim under the Sherman Act and is inconsistent with the "gives rise to a claim" language of the FTAIA.<sup>3</sup>

The court disagrees with plaintiffs' characterization of *Empagran* [\*21] as setting forth a "but-for" standard of causation for claims alleging antitrust conduct in purely foreign commerce. In *Empagran*, which involved an alleged scheme to fix the price of vitamins, the respondents (foreign plaintiffs) argued that because vitamins are fungible and readily transportable, the sellers could not have maintained their international price-fixing arrangement and respondents would not have suffered their foreign injury if there had not been an adverse domestic effect (i.e., higher prices in the United States), and that this "but-for" condition was sufficient to bring the price-fixing conduct within the scope of the FTAIA's exception. [\*Empagran\*, 124 S.Ct. at 2372](#).

However, the Supreme Court specifically declined to address this argument, stating, "We have assumed that the anticompetitive conduct here independently caused foreign injury," and noting that the question of the standard to

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<sup>3</sup> In addition, the TAC does not seek class-wide damages arising from "purely foreign" commerce, as the definition of the proposed class includes only (a) "all persons" or other "entities" who purchased MIO in American commerce, and (b) "all United States persons" or other "entities" who purchased MIO in American or in purely foreign commerce. TAC P 72. In other words, plaintiffs do not seek to represent foreign plaintiffs who bought in purely foreign commerce.

be applied where the alleged foreign injury was *not* independent had not been addressed by the court of appeals below. The Court added that the respondents remained "free to ask the Court of Appeals to consider the claim." *Id. at 2372*. The Court [\*22] did not set forth a standard for such claims - it merely commented that the respondents had raised the argument.

Thus, plaintiffs in the present case are advocating a skewed reading of *Empagran*. Contrary to plaintiffs' argument, the Supreme Court did not conclude that foreign purchasers could pursue claims in the United States if their injuries abroad would not have occurred "but for" the domestic effect of the alleged conduct. Moreover, apart from what is stated above, the Court did not make any ruling about what was required for foreign purchasers in foreign commerce to bring a claim under the Sherman Act.

In addition, the D.C. Circuit noted on remand that the Supreme Court had "declined to decide whether this 'but for' condition is sufficient to bring the contested price-fixing conduct within the scope of the FTAIA's exception," and had remanded the case for further proceedings on the issue. *Empagran S.A. v. F. Hoffman-LaRoche, LTD, 363 U.S. App. D.C. 333, 388 F.3d 337, 339 (D.C. Cir. 2004)*. The D.C. Circuit indicated that it would order full merits briefing on the question whether the nature of the alleged link between foreign injury and domestic effects was legally sufficient to [\*23] trigger application of the FTAIA's domestic-injury exception. *Id. at 339, 342-46*.

Subsequently, the D.C. Circuit ruled that the court lacked jurisdiction under the FTAIA. Among other things, the court held that "but-for" causation between the domestic effects and the claim of foreign injury was not sufficient to bring the anti-competitive conduct at issue within the FTAIA exception. *Empagran v. F. Hoffman-Laroche, 368 U.S. App. D.C. 18, 417 F.3d 1267, 2005 WL 1512951 at \*3 (D.C. Cir., June 28, 2005)*. The court emphasized that the language of the FTAIA exception - "gives rise to" - indicates "a direct causal relationship, that is, proximate causation, and is not satisfied by the mere but-for 'nexus'" advanced by the plaintiffs-appellants. *Id.*

This court also disagrees that plaintiffs' position in the present case is supported by *Sniado* and *MM Global Services*. It is true that the court in *Sniado* noted that the plaintiff's complaint had not even alleged that "but for the European conspiracy's effect on United States commerce, he would not have been injured in Europe." Nevertheless, the Second Circuit nowhere adopted "but-for" causation as the [\*24] appropriate standard for antitrust claims involving "purely foreign" commerce. Indeed, the Second Circuit refused to "infer from the general allegations in [plaintiff's] amended complaint that the 'domestic component' of the alleged worldwide conspiracy was 'necessary . . . for the conspiracy's overall success.'" *Sniado, 378 F.3d at 213*.

Nor does *MM Global Services* support plaintiffs' position. In that case, an Indian corporation, Mega Visa, was the distributor for products manufactured by American corporations Union Carbide and Dow Chemical. Mega Visa and its affiliates purchased these products in the United States and resold them in India. The plaintiffs -- Mega Visa and its affiliates -- alleged that Dow and Union Carbide and their affiliates had compelled plaintiffs to agree to a price maintenance conspiracy. The defendants moved to dismiss, arguing that the court was without jurisdiction to hear the claim under the FTAIA, because the complaint failed to allege antitrust conduct having a direct, substantial, and reasonably foreseeable effect on U.S. commerce. The court found that the complaint *did* allege that the defendants' misconduct gave rise to antitrust [\*25] effects in the U.S. that injured the plaintiffs -- quoting the allegation in the complaint that as a result of defendants' price-fixing,

competition in the sale and resale of [p]roducts in and from the United States was improperly diminished and restrained, and as a result of such effect on competition, [the] [p]laintiffs were injured by being precluded from effectively and fully competing and maximizing their sales of [p]roducts.

*M.M Global, 329 F.Supp. 2d at 342*.

The district court in *MM Global* court never discussed whether "but-for" causation is the appropriate standard for foreign claims under the FTAIA. Moreover, the case did not concern "purely foreign" commerce -- the plaintiffs had purchased product in the U.S., which led the court to conclude that the complaint properly alleged that defendants' conduct had an effect on competition in and from the United States, and that plaintiffs were injured as a result of that effect.

Here, plaintiffs seek relief for overcharges in "purely foreign" commerce, but this claim does not arise from a "direct, substantial, and foreseeable effect" on United States commerce (as required by the FTAIA). [\*26] The FTAIA does leave room for the possibility that foreign anticompetitive conduct can be subject to the jurisdiction of the U.S. courts. However, the FTAIA contemplates that occurring only subject to two conditions - the foreign conduct must have a "direct, substantial, and reasonably foreseeable effect" on U.S. commerce, and the plaintiff's claim must arise from the effect on U.S. commerce.

Indeed, as defendants argue, plaintiffs' proposed theory - pleading a global marketplace where inflated prices in the United States facilitated inflated prices abroad - would effectively nullify the Supreme Court's ruling in *Empagan*, because it would allow any foreign plaintiff who suffered harm abroad as a result of a foreign conspiracy to gain access to the U.S. courts and treble damages by making unsupported allegations of a global marketplace with the possibility of arbitrage pricing, even where there are no allegations of a direct impact on U.S. commerce. This result would run counter to the *Empagan* principle that U.S. courts should avoid unreasonable interference with the sovereign authority of other nations, see [\*Empagan\*, 124 S.Ct. at 2366](#), and would require [\*27] district courts to engage in complex, fact-determinations of alleged linkages between foreign and domestic injuries despite the Court's admonition that FTAIA's jurisdictional test should be capable of being applied "simply and expeditiously," see [\*id. at 2369\*](#).

In short, the foreign plaintiffs' claims of antitrust injury in "purely foreign" commerce must be dismissed because plaintiffs are unable to allege that their injury was directly linked to acts that caused injury to U.S. commerce.

#### *U.S. imports, U.S. exports, and sales in "purely domestic" commerce*

In addition to alleging the sales in "purely foreign" commerce, plaintiffs claim that the alleged price-fixing conspiracy resulted in the sale of MIO at artificially high levels in three other categories of commerce - U.S. imports, "purely domestic" commerce, and U.S. exports. Defendants contend that the TAC fails to state a claim under the Sherman Act in any of these categories of commerce.

#### *U.S. imports*

With regard to U.S. imports, eMag USA (a U.S. plaintiff - not a subject of this motion to dismiss the foreign plaintiffs' claims) alleges that it bought MIO manufactured in Japan, from Toda Kogyo and Sakai [\*28] Trading in the United States; and Delta and Cintas allege that they bought MIO manufactured in Japan, from ISKM in the United States. By its terms, the FTAIA does not apply to cases alleging antitrust conduct in foreign import commerce. See [15 U.S.C. § 6a](#). Thus, the rule articulated by the U.S. Supreme Court in [\*Hartford Fire Ins. Co. v. California\*, 509 U.S. 764, 113 S. Ct. 2891, 125 L. Ed. 2d 612 \(1993\)](#) applies - that is, "the Sherman Act applies to foreign conduct that was meant to produce and did in fact produce some substantial effect" in the United States." [\*Id. at 796\*](#).

Here, defendants argue that the purchases by Delta and Cintas do not constitute U.S. imports because these foreign plaintiffs are not themselves importers into the U.S. <sup>4</sup> Plaintiffs contend, however, that the MIO that defendants delivered to the foreign plaintiffs in the U.S. does qualify as U.S. import commerce. Defendants respond that plaintiffs have confused a claim premised on injury to the import trade between the United States and foreign nations with injury to persons who bought goods after they were imported into the U.S. Defendants also argue that the purchases by Delta and Cintas [\*29] cannot be considered U.S. imports because the MIO simply passed through the United States en route to final destinations outside the borders of the United States.

The court finds that the motion must be GRANTED as to the claims of antitrust injury in American import commerce, because plaintiffs have not alleged that Delta and Cintas engaged in "import commerce" that produced some

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<sup>4</sup> The MIO was imported from Japan into the United States by ISKM. Delta took possession of the shipment in Texas, and Cintas took possession in California. In both cases, Mexico was the ultimate destination of the MIO.

substantial effect in the United States. Moreover, as defendants note, the flow of commerce is not interrupted simply by an intermediate drop in the United States before shipping continues to a foreign destination.

#### *"purely domestic" commerce*

With regard to "purely domestic" commerce, plaintiffs allege that eMag U.S., eMag Wales, Delta, and Cintas all bought MIO manufactured in the United States from ISKM, in the [\*30] United States and abroad.

Defendants argue that the purchases by eMag Wales, Delta, and Cintas do not constitute "purely domestic" commerce because the "ultimate" destination of the MIO sold to each of these plaintiffs was outside the United States. Defendants note that each of the foreign plaintiffs is incorporated and has its principal place of business outside the United States. Defendants claim that the act of taking control of the MIO within the United States for ultimate delivery and use outside the United States does not give rise to a claim for violation of the Sherman Act, because the flow of commerce ends when goods reach their ultimate destination.

As with the argument regarding "import commerce," plaintiffs respond that the MIO that defendants delivered to the foreign plaintiffs in the United States qualifies as U.S. "purely domestic" commerce. Plaintiffs contrast the facts in the present case with the facts in *Empagran*, where the Court observed that the foreign purchasers had bought vitamins for delivery outside of the United States, and there was no claim that the plaintiffs had bought any vitamins in the United States or in transactions in U.S. commerce. [\*Empagran\*, 124 S.Ct. at 2363-64.](#) [\*31] Plaintiffs contend that the Court's reasoning reflects that it is possible for foreign purchasers to buy a product in the United States or in transactions in U.S. commerce.

Plaintiffs also argue that the Court never suggested that the final destination of a product, rather than the location of delivery, dictates the kind of commerce at issue. They cite the legislative history, noting that the House Report stated that the FTAIA "preserves antitrust protections in the domestic marketplace for all purchasers, regardless of nationality or the situs of the business." H.R. Rep. No. 97-686, at 10 (1982) ("House Report"). They argue that a foreign purchaser who buys in the United States is participating in the domestic marketplace, even if the foreign purchaser then transports those goods abroad.

The court finds that the motion must be GRANTED as to the claims of antitrust injury in "purely domestic" commerce because plaintiffs have not alleged facts showing that the purchases by eMag Wales, Delta, and Cintas constituted "purely domestic" commerce. The court agrees with defendants that the flow of commerce is not interrupted simply by an intermediate drop in the U.S. before shipping continues [\*32] to a foreign destination. The portion of the House Report cited by plaintiffs says nothing more than that foreign entities are not excluded from the protection of the U.S. law simply because they operate overseas -- it does not purport to define what is or is not within the flow of domestic commerce. *Empagran* did not address this issue, as the Court merely stated that the case involved foreign companies' purchases that were delivered outside of the U.S. It never addressed -- because it was not at issue -- whether transient receipt of product in the U.S. for ultimate delivery and use outside the U.S. constitutes "purely domestic" commerce.

#### *U.S. export commerce*

With regard to U.S. exports, plaintiffs allege that eMag Wales and Greencorp bought MIO manufactured in the United States, from ISKM, in the United States and abroad.

Defendants argue that eMag Wales and Greencorp, as purchasers of U.S. exports, cannot recover because they are not export competitors of an American exporter. Plaintiffs allege violations of the Sherman Act in connection with MIO that was manufactured and sold in the United States by ISKM, and was exported to eMag Wales in Wales and Greencorp in Australia. [\*33] Defendants assert that the FTAIA expressly protects from the reach of the Sherman Act any anticompetitive activities of U.S. exporters, except if the plaintiff is "an American export competitor" injured by such activity. See [15 U.S.C. § 6a](#) (requirement that the anticompetitive conduct have "a

direct, substantial, and reasonably foreseeable effect" on "export trade . . . of a person engaged in such trade . . . in the United States").

Plaintiffs argue, however, that the FTAIA codified the longstanding "effects" test, under which it is the location of the effect of conduct, not the location of the conduct itself, which determines the applicability of U.S. **antitrust law** (citing House Report at 5-6). They claim that one of the primary aims of the FTAIA was to provide U.S. exporters a special exemption from the "effects" test -- in other words, to exempt U.S. exporters from claims by foreign purchasers except in the limited circumstance where the U.S. exporter's conduct adversely affects U.S. imports or purely domestic commerce. They assert, conversely, where the U.S. exporter's conduct does affect U.S. imports or "purely domestic" commerce, then the foreign [\*34] purchaser can sue for conduct that is not solely export-related.

Plaintiffs contend that the TAC supports their claims for purchases of U.S. exports, because it alleges sufficient effects on American commerce (citing TAC PP 15-17, 19, 29, 30, 34, 35, 51, 59, 63, 68, and 84).<sup>5</sup> Plaintiffs also assert that the TAC alleges that ISKM manufactured millions of dollars' worth of MIO in the U.S., which it sold in purely domestic commerce; that ISK Japan pleaded guilty to price-fixing; that defendants' conspiracy had the requisite direct, substantial, and reasonably foreseeable effects on U.S. exports, U.S. imports, and purely domestic commerce; that defendants' conspiracy had a "spillover effect," inflating the price of U.S. imports and purely domestic commerce; and that eMag USA bought over \$ 500,000 worth of MIO as U.S. imports subject to defendants' conspiracy (citing TAC PP 52, 98, 84, 86, and 15-17).

[\*35] The court finds that the motion must be GRANTED as to the claims of antitrust injury in export commerce, as plaintiffs have not adequately alleged a direct, substantial, and reasonably foreseeable effect on U.S. commerce caused by these export sales, because they do not allege that the foreign plaintiffs are American export competitors.

#### D. Motion to Dismiss for Lack of Antitrust Standing

Defendants argue that the foreign plaintiffs lack standing to assert antitrust claims. Antitrust standing is an issue separate from the jurisdictional question discussed above. Unlike Article III standing, antitrust standing is not jurisdictional. *Datagate, Inc. v. Hewlett-Packard Co.*, 60 F.3d 1421, 1425, n. 1 (9th Cir.1995). In *Assoc. Gen'l Contractors v. Cal. State Council of Carpenters*, 459 U.S. 519, 103 S. Ct. 897, 74 L. Ed. 2d 723 (1983), the Supreme Court set forth the factors a court must consider in determining whether a plaintiff has standing to bring a claim for violation of the antitrust laws. These are (1) whether there is a causal connection between the alleged antitrust violation and the harm plaintiff allegedly suffered, and whether defendants intended to cause that harm; (2) [\*36] whether the nature of plaintiff's injury is the type the antitrust laws were intended to forestall; (3) the directness of the injury; (4) the existence of more direct victims; (5) the risk of duplicative recovery; and (6) the complexity of apportioning damages. *Id. at 538-47*.

Defendants focus on one of the these five factors, arguing that the allegations in the TAC fail to establish that the foreign plaintiffs have suffered "antitrust injury" -- i.e., the type of injury that "the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful." *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977). Because "antitrust laws were enacted for "the protection of competition, not competitors,'" a private antitrust claim must allege an injury that results from the

<sup>5</sup> Those paragraphs of the TAC do not appear to support plaintiffs' argument with regard to U.S. export commerce. TAC PP 15 and 16 allege that eMag USA purchased MIO as U.S. imports. TAC P 17 alleges that eMag USA purchased MIO in purely domestic commerce. TAC P 19 alleges that eMag Wales purchased MIO in purely domestic commerce. TAC P29 alleges that Delta purchased MIO directly as U.S imports. TAC P 30 alleges that Delta purchased MIO in purely domestic commerce. TAC P 34 alleges that Cintas purchased MIO directly as U.S. imports. TAC P 35 alleges that Cintas purchased MIO directly in purely domestic commerce. TAC P 51 alleges that ISK sold MIO as U.S. imports. TAC P 59 alleges that Sakai sold MIO as U.S. imports. TAC P 63 alleges that Titan sold MIO as U.S. imports. TAC P68 alleges that Toda sold MIO as U.S. imports. TAC P 84 alleges that all the activities of the defendants alleged in the TAC had a direct, substantial, and foreseeable effect on all four categories of commerce.

anticompetitive aspect of the defendants' conduct. *Legal Econ. Evaluations, Inc. v. Metropolitan Life Ins. Co., 39 F.3d 951, 954 (9th Cir.1994)* (citation and quotation omitted).

Defendants contend that even if U.S. courts have jurisdiction to hear the claims of the foreign plaintiffs, the U.S. antitrust laws intended to protect [\*37] such foreign plaintiffs, and the foreign plaintiffs do not have antitrust standing under the FTAIA. Defendants argue that foreign consumers who have not participated in the U.S. market as consumers or competitors have no right to bring a Sherman Act claim. Defendants also contend that each plaintiff has failed to adequately allege an antitrust injury -- that is, an injury that reflects the anticompetitive effect either of the alleged violation or of anticompetitive acts made possible by the violation.

Plaintiffs contend that antitrust standing doctrine does not apply to parties, like the foreign plaintiffs here, who are consumers in the relevant market, who bought the goods at issue directly from the defendants, whose injuries are clear, and who are entitled to recover the full amount they were overcharged. They claim that it applies only to parties who are not consumers or competitors or consumers in the market at issue, who suffer only an indirect injury, whose injury is speculative, or whose claims might give rise to duplicative recoveries or difficulties in apportioning damages.

The court finds that in view of the disposition of the Sherman Act claim, above, there is no need [\*38] for consideration of defendants' alternative claim that plaintiffs lack antitrust standing. See *Verizon Communications, Inc. v. Law Offices of Curtis v. Trinko LLP, 540 U.S. 398, 416 n.5, 124 S. Ct. 872, 157 L. Ed. 2d 823 (2004)*.

## **CONCLUSION**

In accordance with the foregoing, the court finds that defendants' motion must be GRANTED and that the claims of the foreign plaintiffs must be DISMISSED. Because the court finds that amendment would be futile, the dismissal is WITH PREJUDICE.

## **IT IS SO ORDERED.**

Dated: July 20, 2005

PHYLLIS J. HAMILTON

United States District Judge

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## Lundsford v. Callaway Golf Co.

United States District Court for the Eastern District of Tennessee

July 20, 2005, Filed

No. 3:04-cv-442

**Reporter**

2005 U.S. Dist. LEXIS 59896 \*

JAMES P. LUNDSFORD, individually and on behalf of all others similarly situated, Plaintiff, v. CALLAWAY GOLF COMPANY, a Delaware corporation and CALLAWAY GOLF SALES COMPANY, a California Corporation, Defendants.

### **Core Terms**

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retailers, products, class action, manufacturer, golf, golf club, damages, class member, dealer, class certification, anti trust law, summary judgment, minimum price, predominate, representative plaintiff, distributors, antitrust, consumers, putative class, termination, discount, prices, sales, injunctive relief, plaintiff's claim, Sherman Act, depositions, conspiracy, partial summary judgment, common question

**Counsel:** [\*1] For James P Lundsford, individually and on behalf of all others similarly situated, Plaintiff: Gordon Ball, LEAD ATTORNEY, Gordon Ball Lw Office PLLC, Knoxville, TN USA; Stephen G Kabalka, Maddox & Anderson, PLLC, Chattanooga, TN USA.

For Callaway Golf Co, a Delaware Corporation, Callaway Golf Sales Company, a California Corporation, Defendants: David Ettinger, LEAD ATTORNEY, Honigman, Miller, Schwartz & Cohen, Detroit, MI USA; Edward Wasmuth, Jr, Thomas W Rhodes, LEAD ATTORNEYS, Smith, Gambrell and Russell, Atlanta, GA USA; John A Lucas, Howard & Howard, PC, Knoxville, TN USA.

**Judges:** James H. Jarvis, UNITED STATES DISTRICT JUDGE.

**Opinion by:** James H. Jarvis

### **Opinion**

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#### **MEMORANDUM OPINION**

This putative class action arises out of claims of illegal restraint of trade and anticompetitive conduct by Callaway Golf Company and Callaway Golf Sales Company throughout the United States occurring since March 30, 2000. The plaintiff claims to have been injured in that they have paid more for Callaway golf clubs than they otherwise would have paid absent Callaway's allegedly unlawful conduct. The plaintiff seeks a determination that this action is a proper class action maintainable pursuant to [Rule 23 of the Federal Rules of Civil Procedure](#), a declaration that the defendant's [\*2] alleged conduct violated the Sherman Act, an order enjoining Callaway from the alleged illegal conduct in the future, and an award of legal costs and damages. The motions currently pending in this action are: (1) the plaintiff's motion for partial summary judgment as to liability under [Section 1](#) of the Sherman Act, [15 U.S.C. § 1](#) [Court File 11], and (2) the plaintiff's motion for class certification [Court File 14]. For the reasons that follow, the motion for partial summary judgment is denied, and the motion for class certification is denied.

**I.*****Factual Background***

The original complaint and amended complaint names James P. Lundsford, a resident of Jefferson County, Tennessee, as the sole putative class representative. During the putative Class Period, the plaintiff purchased Callaway golf clubs from Wynn's Sports World in Sevierville, Tennessee, a retail dealer in golf equipment and supplies.

Defendant Callaway Golf Company is a Delaware corporation transacting business across the United States, with its principal place of business in Carlsbad, California. Defendant Callaway Golf Sales Company is a California corporation transacting business across the United States. Callaway is the largest manufacturer of [\*3] golf clubs in the United States, distributing them through retail dealers located throughout the country.

In 2000, Callaway implemented the New Product Introduction Policy ("NPIP"). The policy stated that Callaway would only supply retailers that sold directly to golfers, that did not discount the products, that did not engage in bait-and-switch selling, that did not disparage the Callaway Golf product, and that complied with all laws. This new policy was part of Callaway's conscious decision to do business with full-price retailers rather than discounters. Callaway also claimed that discounting and bait-and-switch tactics by some of its retailers caused the company to fear degradation of the Callaway name brand. Among other things, the policy set a minimum price that retailers could sell Callaway products. Callaway claimed that the minimum price was set to allow for sufficient profit margins such that full-price retailers could provide fitting and training services to accompany Callaway products (e.g., 30-35% in the store where the representative plaintiff purchased clubs). Large, national retailers refuse to carry products that will not yield such profit margins.

The policy was developed [\*4] with the close advice of legal counsel to adhere to antitrust laws. The NPIP states on its face that it is a "unilateral statement" and "not a contract, or an offer," further stating that Callaway "does not ask, and will not accept, any agreement about [a retailer's] compliance with this Policy." Callaway expressly forbade its sales force from discussing the policy with retailers, forcing any communications about the policy to go through their legal department.

Twenty NPIPs were issued between September 8, 1999 and August 30, 2004 to an estimated 17,000 retailers nationwide. These NPIPs were separated by more than six months only three times, while two or fewer months separated the issuances ten times. Each new NPIP superseded the previous one, allowing Callaway to add new products, carry over existing products, and remove products based on each product's life cycle. Each new NPIP described Callaway's requirement for retailers selling its golf clubs, including the minimum resale price for the product. The original NPIP dated September 8, 1999 included a signature line for acknowledging receipt of the policy and denying that the policy is an agreement, but Callaway abandoned that practice [\*5] beginning with the NPIP dated October 18, 2000. Over 90% of Callaway's retailers received the NPIPs and had no other communication with Callaway about the policy.

Callaway attempted to enforce the policy, investigating each violation separately. Callaway's retailers generally fit into three categories: pro shops located on golf courses, stand-alone stores, and inside national sporting-goods stores. The NPIP was applied differently to different retailers. For example, in February 2001, Callaway excluded certain products sold in Tennessee by Dick's Sporting Goods. Similarly, "Mill River" plans sold at pro shops were originally not subject to the NPIP. They were included for a short time, and then excluded again. Callaway also treated violators of the policy differently. Some were sent letters stating that Callaway was aware of the violation and would refuse to accept new orders if the retailer continued to act contrary to the NPIP. Some had their shipments of the specific inventory item suspended for an indefinite amount of time, although Callaway would continue to accept orders for all other products carried by the retailer. The period of time in which Callaway would refuse to accept [\*6] new orders varied by customer and product, and also changed from year to year. For example, the store that the representative plaintiff bought clubs from claims to not have been able to order a

particular club for six months, while another store was allowed to purchase the same club again in an identical situation after only three months. Sometimes, Callaway elected not to enforce the NPIP at all, such as when retailers discounted products that were about to be taken off the NPIP.

Wynn's Sports World ("Wynn's") in Sevierville, Tennessee, was a retailer for Callaway. Mike Coughlin, the president of Wynn's, signed an NPIP covering certain Callaway products in January 2000. James D. Bowles, the director of golf operations at Wynn's, claims to have signed another NPIP the following year in 2001, but the last NPIP issued with a line for signature had an effective date of January 20, 2000. The first NPIP issued for the 2001 year had an effective date of May 1, 2001. In the summer of 2001, Callaway sent a letter to Wynn's advising them that they suspected Wynn's was selling Callaway's "Big Bertha Steelhead Plus Metal Woods" below the minimum price listed in the NPIP. When Wynn's did not stop [\*7] selling the Callaway clubs below the agreed price, Callaway refused to accept any more orders from them for that item. During the 2001 PGA show in Orlando Florida, Mike Coughlin and Robert Jones, the vice president of retail operations at Wynn's, met with Michael Rider, legal representative for Callaway, to discuss the problems. This meeting did not produce any results. The plaintiff claims that Wynn's was not able to purchase the item until it was no longer subject to the NPIP. However, the NPIP issued with an effective date of May 2, 2001 stated that the clubs in question were no longer "covered by the 2001 New Product Introduction Policy" (as did the subsequent NPIP with an effective date of August 24, 2001).

In November 2000, the plaintiff James P. Lundsford purchased a set of "Big Bertha Hawk Eye Irons" from Wynn's. He paid the minimum price of \$1249 as listed in the NPIP with the effective date of October 18, 2000. A few weeks later, the plaintiff also purchased from Wynn's a "Great Big Bertha Hawk Eye Driver" for \$459. This product does not appear in the NPIP effective at that time. There is no evidence to indicate that he retained his receipt or paid the NPIP price. Jerry Messer [\*8] was the salesman for Wynn's at the time, who later gave a copy of the NPIP to the plaintiff. At the time of the purchase, Callaway had not discussed the NPIP with Wynn's.

## II.

### ***Procedural History***

In 2001, the plaintiff filed an original class action in Tennessee state court regarding Tennessee and Kansas law. The plaintiff also filed an identical class action in Kansas, which was later stayed. [Rule 23.03 of the Tennessee Rules of Civil Procedure](#) states that class certification should be decided "[a]s soon as practicable after the commencement of an action brought as a class action." Three years later, the defendant filed a motion that the class should not be certified. The day before the hearing on that motion, the plaintiff filed this action. The Tennessee state court action has still not been certified.

In the complaint, the plaintiff alleged three causes of action.

Count I alleged a cause of action for illegal restraint of trade in violation of [Section 1](#) of the Sherman Act, [15 U.S.C. § 1](#). This Count was the subject of the plaintiff's motion for partial summary judgment. [Court File 11]. The plaintiff subsequently filed two affidavits supporting the motion. On March 30, 2005, the defendant filed a response in opposition of the motion, subsequently filing deposition [\*9] excerpts in support of the opposition. On April 7, the plaintiff filed a motion for leave to file a consolidated memorandum, in part replying to the defendant's opposition to the motion.

Count II was dismissed.

Count III alleged causes of action for violations of the antitrust laws of Tennessee, Kansas, South Carolina, and Oklahoma under the court's supplemental jurisdiction. However, the plaintiff now attempts to drop this Count III altogether in the proposed amended complaint. Defendant opposes this amendment.

**VI.*****Motion for Partial Summary Judgment for violation of Sherman Act § 1***

The plaintiff claims that summary judgment is proper in this case because "the undisputed facts show that Callaway and participating retail dealers have engaged in a contract, combination or conspiracy to fix prices on Callaway products, creating a *per se* violation of [Section 1](#) of the Sherman Antitrust Act, [15 U.S.C. § 1](#), and the antitrust statutes of Tennessee, Kansas, South Carolina and Oklahoma."

**a.**

***Standard of Review for Summary Judgment***

Pursuant to [Rule 56 of the Federal Rules of Civil Procedure](#), summary judgment shall be rendered when requested if the pleadings, depositions, answers to interrogatories, and admissions on file, together with affidavits, if any, show that there [\*10] is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. It is the burden of the party seeking summary judgment to show the court that, under uncontradicted facts, the moving party is entitled to judgment as a matter of law. Summary judgment is intended to provide a quick, inexpensive means of resolving issues as to which there is no dispute regarding material facts. [Celotex Corp. v. Catrett](#), [477 U.S. 317, 106 S. Ct. 2548, 91 L. Ed. 2d 265 \(1986\)](#). In assessing the validity of a summary judgment motion, the court views the pleadings, depositions, answers to interrogatories, admissions, and competent affidavits in the light most favorable to the opponent of the motion. However, the party opposing the motion for summary judgment may not rest upon the mere allegations or denials of his pleadings, but must set forth through competent and material evidence, specific facts showing that there is a genuine issue for trial. [Anderson v. Liberty Lobby, Inc.](#), [477 U.S. 242, 106 S. Ct. 2505, 91 L. Ed. 2d 202 \(1986\)](#). "[T]he mere existence of some alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment." *Id.* [Rule 56](#) mandates the entry of summary judgment, after adequate time for discovery and upon motion, against a party who fails to make a showing sufficient [\*11] to establish the existence of an essential element of that party's case, and on which the party will bear the burden of proof at trial. [Catrett, 477 U.S. at 322](#).

**b.**

***Federal Antitrust Claims***

"Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." [15 U.S.C.A. § 1](#). Although this section describes criminal penalties, the Clayton Act states that, "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee." [15 U.S.C.A. § 15](#) (formerly Clayton Act [§ 4](#)).

In *United States v. Colgate & Co.*, the Supreme Court held that a manufacturer has a near absolute right to select with whom it will deal, and to announce in advance the terms and conditions upon which it will do business. [250 U.S. 300, 307, 39 S. Ct. 465, 63 L. Ed. 992, 1919 Dec. Comm'r Pat. 460 \(1919\)](#). A manufacturer could announce that it would sell only to dealers charging a predetermined resale [\*12] price, and could terminate sales to any dealer which did not comply. *Id.* Later in *Monsanto Co. v. Spray-Rite Service Corp.*, the Court upheld minimum

prices set by manufacturers because "[t]he manufacturer often will want to ensure that its distributors earn sufficient profit to pay for programs such as hiring and training additional salesmen or demonstrating the technical features of the product, and will want to see that 'free-riders' do not interfere." [465 U.S. 752, 762-63, 104 S. Ct. 1464, 79 L. Ed. 2d 775 \(1984\)](#). No antitrust violation arises from a manufacturer's merely adopting a resale price policy and a retailer's following the policy to avoid termination of sales to the account. Under such antitrust laws, the retailer/distributor is "free to acquiesce in the manufacturer's demand in order to avoid termination." *Id.* Moreover, a plaintiff claiming resale-price agreement must show "both that the distributor communicated its acquiescence or agreement, and that this was sought by the manufacturer." *Id. at 764 n.9*. Unless the manufacturer seeks such a communication from the retailer/distributor and receives it, there is no "agreement." *Id.* Further, in *Business Electronics Corp. v. Sharp Electronics Corp.*, the Court held that there must be an "agreement [\*13] on the price or price levels to be charged by the remaining dealer" as well as an agreement between the manufacturer and a dealer to terminate a 'price cutter.'" [485 U.S. 717, 726, 108 S. Ct. 1515, 99 L. Ed. 2d 808 \(1988\)](#).

The plaintiff suggests that, under [United States v. Colgate & Co., 250 U.S. 300, 39 S. Ct. 465, 63 L. Ed. 992, 1919 Dec. Comm'r Pat. 460 \(1919\)](#), a manufacturer can suggest prices but has only one choice with respect to violators — immediate termination of product purchasing privileges with no warning, no second chances, and no continued shipments in response to assurances of future compliance. The plaintiff maintains that Callaway never intended that termination of a dealer was an option under the NPIP. However, Callaway *did* terminate the ability of Wynn's (the plaintiff's sole example) to purchase the golf clubs that were subject to the NPIP. Callaway only allowed Wynn's to again order the clubs once they were no longer subject to the NPIP.

Plaintiff further asserts that Callaway's conduct constitutes a "per se violation" of state and federal antitrust laws. "Per se rules of illegality are appropriate only when they relate to conduct that is manifestly anticompetitive." [Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 50, 97 S. Ct. 2549, 53 L. Ed. 2d 568 \(1977\)](#). The allegedly illegal practices, "because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable [\*14] and therefore illegal without elaborate inquiry as to the precise harm they have caused or the business excuse for their use." [Northern Pac. R. Co. v. United States, 356 U.S. 1, 5, 78 S. Ct. 514, 2 L. Ed. 2d 545 \(1958\)](#). Thus, the plaintiff is asking the court to find that Callaway's sales policy generally harms society, devoid of any accompanying benefit, without a substantial inquiry into the circumstances.

The court finds that this is not a per se violation of antitrust laws. The defendant has presented a plausible argument that the policy may be beneficial to the company, its suppliers, and the golf industry as a whole. The resale price policy, *inter alia*, protects reseller margins so that services such as fitting and testing can be provided, supports a premium brand image, facilitates investment into research and product development, and provides stability to combat destructive competition between retailers.

The plaintiff cites *Bender v. Southland Corp.* for the proposition that the "Supreme Court has long held that vertical price fixing is a per se violation of § 1 of the Sherman Act." [749 F.2d 1205, 1211-12 \(6th Cir. 1984\)](#). However, the court in that case maintained that the "practice is unlawful because it restricts the freedom of traders who are at lower levels of the product or service distribution system [\*15] to set their own prices." *Id.* (citing [Kiefer-Stewart, 340 U.S. 211, 71 S. Ct. 259, 95 L. Ed. 219 \(1951\); AAA Liquors, Inc. v. Joseph E. Seagram & Sons, Inc., 705 F.2d 1203 \(10th Cir. 1982\)](#)). The instant case is distinguishable because there are no lower levels in the distribution system. Callaway sells only to retailers who deal directly with consumers.

In adopting that policy with the assistance of experienced antitrust counsel, Callaway followed well-established **antitrust law** that allows a manufacturer to choose its retail customers — including those retailers who do not discount. Before implementing the policy, Callaway sought expert legal advice, devising both an unambiguous document and a vigilant method of executing the policy. In fact, Callaway appears to have made more than reasonable efforts to implement its NPIP as an independent action, not subject to negotiation or agreement with any of its retailers. Wynn's had the choice to discontinue business with Callaway, but they voluntarily chose to acquiesce to Callaway's sales policy requirements. There is no evidence to show that Callaway sought any sort of agreement from Wynn's to abide by its sales policy. Thus, the plaintiff has failed to show that he is entitled to judgment as a matter of law. In fact, the facts are uncontradicted at this point that the plaintiff has failed [\*16] to

come forward with evidence that at least two elements of a per se claim have been met, specifically (1) the existence of an agreement, and (2) harm to society with a lack of any accompanying benefit.

c.

### ***State Antitrust Claims***

The plaintiffs also maintain state law claims in their complaint. The relevant Tennessee law states that:

All arrangements, contracts, agreements, trusts, or combinations between persons or corporations made with a view to lessen, or which tend to lessen, full and free competition in the importation or sale of articles imported into this state, or in the manufacture or sale of articles of domestic growth or of domestic raw material, and all arrangements, contracts, agreements, trusts, or combinations between persons or corporations designed, or which tend, to advance, reduce, or control the price or the cost to the producer or the consumer of any such product or article, are declared to be against public policy, unlawful, and void. [Tenn. Code Ann. § 47-25-101](#) (1995). Any person who may be injured or damaged by any such arrangement, contract, agreement, trust, or combination described in this part may sue for and recover, in any court of competent jurisdiction, from any person operating such [\*17] trust or combination, the full consideration or sum paid by the person for any goods, wares, merchandise, or articles, the sale of which is controlled by such combination or trust. [Tenn. Code Ann. § 47-25-106](#) (1995).

The law was passed by Tennessee in 1891 to supplement the federal antitrust laws. See [Standard Oil Co. v. State, 117 Tenn. 618, 100 S.W. 705, 710 \(Tenn. 1907\)](#) ("The wrongs to trade which were intended to be corrected and punished were those being perpetrated against commerce within the state, which Congress could not reach, and for which there was then no efficient remedy."). Thus, Tennessee courts have held that state antitrust laws are consistent with the federal law in that they focus on the same illegal conduct. [Jo Ann Forman, Inc. v. Nat'l Council on Comp. Ins., Inc., 13 S.W.3d 365, 368 \(Tenn. Ct. App. 1999\)](#) ("The Legislature clearly intended to prohibit trusts, combinations, and agreements affecting all commerce not covered by the federal statute, and upon which it had a right to legislate.").

For the reasons stated above for the federal antitrust claims, the plaintiff has failed to show that he is entitled to judgment as a matter of law.

Plaintiff has filed a motion to amend his complaint to drop his state law antitrust claims [Court File #54]. Defendant objects contending that the only purpose for dropping the state law claims at this point would be to allow [\*18] the plaintiff to rebring the same lawsuit in state court should this court deny class certification. The court agrees with the defendant and finds that plaintiff has failed to show good cause for the amendment. Accordingly, the motion to amend [Court File #54] will be denied.

VIII.

### ***Class Certification***

The complaint defines the class as follows:

All persons who purchased Callaway golf clubs from dealers and co-conspirators in the United States that were subject to Callaway's and the dealers' agreements setting minimum prices from March 20, 2000 until the trial of this action is concluded. Excluded from the Class are all directors, officers, agents, and/or employees of Callaway.

Before a class may be certified under [Rule 23](#), the party seeking class certification must establish that the class satisfies all four prerequisites of [Rule 23\(a\)](#). *In re American Medical Sys., Inc.*, 75 F.3d 1069, 1079 (6th Cir. 1996). Pursuant to [Rule 23\(a\)](#), the burden is on the party seeking class certification to prove that: (1) the class is so numerous that joinder of all members is impractical; (2) there are questions of law or fact common to the class; (3) the claims of the representative plaintiffs are typical of the claims of the class; and (4) the named plaintiffs and class counsel are adequate representatives [\*19] for the class. [Fed. R. Civ. P. 23\(a\)](#). In addition, the party seeking class certification must also establish that the proposed class action qualifies for class treatment under one or more of the [Rule 23\(b\)](#) subcategories. [Fed. R. Civ. P. 23\(b\)](#).

Subtle differences distinguish some of these categories. For instance, there is an "extensive" overlap between [Rule 23\(a\)\(3\)](#) and [\(a\)\(4\)](#). 1 NEWBERG ON CLASS ACTIONS [§ 3.22](#), at 411. However, satisfaction of the typicality test "does not automatically mean that adequacy of representation is present." *Id.*, at 412. Additionally, "[t]here is considerable overlap between [Rule 23\(a\)\(2\)](#) and [\(b\)\(3\)](#)." 2 NEWBERG ON CLASS ACTIONS [§ 4.22](#), at 152. "The [Rule 23\(a\)\(2\)](#) prerequisite requires that common questions exist. [Rule 23\(b\)\(2\)](#) requires that they predominate." *Id.* Each will be addressed below.

a.

#### [Rule 23\(a\)\(1\)](#) Numerosity

[Rule 23\(a\)\(1\)](#) requires that "the class is so numerous that joinder of all members is impractical." [Fed. R. Civ. P. 23\(a\)\(1\)](#). In this case, numerosity is not in dispute.

b.

#### [Rule 23\(a\)\(2\)](#) Commonality

[Rule 23\(a\)\(2\)](#) requires that "there are questions of law or fact common to the class." [Fed. R. Civ. P. 23\(a\)\(2\)](#). One issue that is common to all class members is sufficient. *In re Cardizem*, 200 F.R.D. 326, 335 (E.D. Mich. 2001).

The defendant notes the vast number agreements comprised of various types of relationships and varying interactions between Callaway and its retailers. However, this argument is better suited for the higher threshold [\*20] set for predominance in [Rule 23\(b\)\(3\)](#), which is "an important check on this requirement." *In re American Medical Sys., Inc.*, 75 F.3d 1069, 1080 (6th Cir. 1996).

The plaintiff satisfies the commonality requirement because there are common questions of law and fact. Callaway's liability to individual purchasers depends upon the determination of the same issue of law, namely whether Callaway violated [Section 1](#) of the Sherman Act. As for common questions of fact, the plaintiff offers the following examples: whether Callaway possesses market power in the golf club market; whether Callaway used its market power ... to raise the prices of its golf clubs; whether competition in the golf club market and among Callaway's retailers was adversely affected; whether the members of the class suffered injury as a result.

It is worth noting that the defendant suggests the purchased golf clubs were not subject to the NPIP. If this is true, the plaintiff would not have a common question of fact with the putative class members, failing the commonality requirement. However, that question cannot be resolved at this point.

c.

### **Rule 23(a)(3) Typicality**

Rule 23(a)(3) requires that "the claims of the representative plaintiffs are typical of the claims of the class." Fed. R. Civ. P. 23(a)(3). "Typical claims arise from the same event or course of conduct [\*21] giving rise to the claims of other class members and is based on the same legal theory." [Court File 15] (citing Senter v. General Motors Corp., 532 F.2d 511, 525 (6th Cir. 1976), cert. denied, 429 U.S. 870 (1976)). Claims may satisfy this requirement, "even if members purchase different quantities and pay different prices." In re Cardizem, 200 F.R.D. 326, 335-36 (E.D. Mich. 2001) (quoting In re Playmobil Antitrust Litig., 35 F.Supp.2d 231, 242 (E.D.N.Y. 1998))."

The defendant alleges that the plaintiff does not meet the typicality requirement because his case is "[]encumbered by the presence of active participation by plaintiff's counsel," referencing the relationship between the plaintiff and counsel. However, the plaintiff satisfies the typicality requirement because the claims of the representative plaintiff are typical of the claims of the class. The sole putative class representative is James P. Lundsford. The plaintiff purchased a Callaway golf club during the class period from Wynn's Sports World, who was allegedly "subject to Callaway's and the dealers' agreements setting minimum prices." Claims brought by other members of the putative class would be substantially similar to the representative plaintiff.

The court again notes that the defendant suggests the purchased golf clubs were not subject to the NPIP. If this is true, the plaintiff would not have a claim typical of the putative [\*22] class members, failing the typicality requirement. Again, however, that question cannot be resolved at this point.

**d.**

### **Rule 23(a)(4) Adequacy**

Rule 23(a)(4) requires that "the named plaintiffs and class counsel are adequate representatives for the class." Fed. R. Civ. P. 23(a)(4). The plaintiff offers [Court File 15] two elements for this test: (1) the representative must have common interests with the unnamed class members, and (2) it must appear that the representative will vigorously prosecute the class action through qualified counsel. Senter v. General Motors Corp., 532 F.2d 511, 525 (6th Cir. 1976), cert. denied, 429 U.S. 870 (1976).

The plaintiff claims to meet the adequacy requirement because (1) "the named representative and the class members ... were similarly injured by the same illegal conduct," and (2) the plaintiff's counsel are qualified and experienced lawyers. [Court File 15]. Indeed, there appears to be no conflict between the representative plaintiff and the class members, and the qualifications of plaintiff's counsel are clearly sufficient. However, the plaintiff's failure to move to certify the class during the past three years is a "strong indication" that the plaintiff is not adequately representing the putative class. East Tex. Motor Freight Sys. v. Rodriguez, 431 U.S. 395, 404-405, 97 S. Ct. 1891, 52 L. Ed. 2d 453 (1977) (citing Beasley v. Kroehler Mfg. Co., 406 F.Supp. 926, 931 (D.C.Tex. 1976) ("The Court concludes that the plaintiff may not maintain her suit as [\*23] a class action due to her failure to pursue class representation diligently through the filing of a motion to certify her suit as a class action.")); see also McGowan v. Faulkner Concrete Pipe Co., 659 F.2d 554, 559 (5th Cir. 1981) ("the district judge might properly take into consideration the circumstance that the plaintiffs' counsel did not move for certification during the two years the suit was pending."). Here, I also conclude that the adequacy requirement has not been met because the plaintiff has failed to demonstrate that he will vigorously prosecute the class action through qualified counsel.

**e.**

### **Rule 23(b)(2) Injunctive Relief**

Rule 23(b)(2) applies when "the party opposing the class has acted ... on grounds generally applicable to the class, thereby making appropriate injunctive relief ... with respect to the class as a whole." Fed. R. Civ. P. 23(b)(2). The plaintiff maintains that the elements to this rule are that: (1) the claims of the class are cohesive, and (2) the relief sought is equitable in nature.

The plaintiff claims to meet the injunctive relief requirement because (1) the claims of the putative class are cohesive because they all share "a common characteristic subjected to [actions by the defendant]." Wetzel v. Liberty Mut. Ins. Co., 508 F.2d 239, \*250 (C.A.Pa. 1975). Also, (2) the plaintiff has asked for injunctive relief in their complaint. However, [\*24] class certification under Rule 23(b)(2) is appropriate only "so long as the predominant relief sought is injunctive or declaratory." Ford v. Nylcare Health Plans of Gulf Coast, Inc., 190 F.R.D. 422, 428 (S.D.Tex., 1999) (quoting Allison v. Citgo Petroleum Corp., 151 F.3d 402, 411 (5th Cir. 1998)). "[O]ne critical factor is whether the compensatory relief requested requires individualized damages determination or is susceptible to calculation on a classwide basis." Coleman v. GMAC, 296 F.3d 443, 448 (6th Cir., 2002). Because any damages assessed will have to be determined for every retailer of Callaway products due to factors such as market prices, damages are not "susceptible" to a classwide calculation. *Id.* Further, it is reasonable to assume that the primary relief sought in this case is monetary damages and attorney fees, based on the history of the case, conduct of the parties, and the nominal attention paid to injunctive relief by the plaintiff in the complaint and supporting briefs.

The plaintiff cites *Olden v. Lafarge Corp.* for the proposition that any class seeking injunctive relief should be certified under Rule 23(b)(2), 383 F.3d 495, 510 (6th Cir. 2004). However, the court in that case emphasized the "importance of the injunctive relief" itself. Indeed, the plaintiffs in that case were homeowners that were having their health and homes damaged by a large cement manufacturer emitting hazardous toxic waste in violation of a consent [\*25] decree. Moreover, there is virtually nothing in the record in this case to indicate that the predominant relief sought is injunctive.

f.

### Rule 23(b)(3) Predominance and Superiority

To be certified as a class under Rule 23(b)(3), "questions of law or fact common to the members of the class [must] predominate over any questions affecting only individual members, and [the class action must be] superior to other available methods for the fair and efficient adjudication of the controversy. The matters pertinent to the findings include: ... (D) the difficulties likely to be encountered in the management of a class action." Fed. R. Civ. P. 23(b)(3).

The plaintiff claims to meet the predominance and superiority requirement because the fact of injury and damages can be demonstrated with "common proof." According to the plaintiff, this case would establish the fact of injury for the entire class. As long as the injury was common to all class members, the variability of the damages from member to member does not matter. However, this argument is contrary to precedent in this circuit. In *Mekani v. Miller Brewing Co.*, the court addressed a similar argument in which the plaintiff alleged a beer manufacturer and its distributors were engaged in illegal [\*26] price fixing. 93 F.R.D. 506, 510 (D.C.Mich., 1982). The court held that:

The plaintiffs in the instant case have not satisfactorily demonstrated any method by which the distributors' participation in the conspiracy can be proved through any common set of facts. Plaintiffs' argument that there are common issues because there is only one conspiracy does not address the real issue. The complaint specifically alleges that the brewers, by agreement or coercion, imposed their plan on the distributors. Thus, the plaintiffs will necessarily have to show some sort of agreement or coercion between the brewers and each of the 180 distributors. Defendants contend, and the Court agrees, that the very process of proving the existence of the vertical arm of the conspiracy will raise questions which would require individual treatment. The case would degenerate into 180 separate trials and common questions would be overwhelmed by issues peculiar to individual parties. The plaintiffs' bald allegation that a conspiracy existed in violation of the antitrust laws does not insure that common questions will predominate.

*Id.* Further, the 6th Circuit has held that the refusal to certify a class on this basis is not an abuse of discretion. [Stout v. J.D. Byrider, 228 F.3d 709, 718 \(6th Cir. 2000\)](#) (holding [\*27] that the plaintiff did not meet the requirement of [Rule 23\(b\)](#) when any resolution of claims other than the representative plaintiff would be subject to an "individual assessment").

The putative class cannot be properly certified under [Rule 23\(b\)\(3\)](#) because the plaintiff has failed to show that "questions of law or fact common to the members of the class predominate over any questions affecting only individual members." [Fed. R. Civ. P. 23\(b\)\(3\)](#). Litigating the issue of whether Callaway's sales policy could be found to be an agreement with the nearly 17,000 other Callaway golf locations would devolve into an unmanageable tangle of fact-specific mini-trials. Individual issues that would have to be resolved for each class member would include whether there was an agreement, the scope of the agreement, the timeframe of the agreement, whether a class member was actually injured, and what the extent of the damages were.

"The central issue in each class member's case would be whether [a particular] retailer's decision to sell at the NPIP price or not in that specific transaction was the product of an 'agreement' with Callaway Golf." The effort and expense of both parties to determine the issues for just one such store should be noted, including [\*28] the numerous affidavits, depositions, subpoenas, and expert witnesses. There is no reason to believe that any class member would face any easier or shorter task. During the class period Callaway distributed products through shops at golf courses, stand-alone stores, and inside national sporting-goods stores. Even the plaintiff admits that Callaway made individual decisions and took varying actions against different retailers. The NPIP was not consistently and continually applied and Callaway considered other factors before choosing to pursue any particular retailer.

Even if the fact of an agreement was established, individual class members would have to litigate the scope and timeframe of the alleged agreement. The court would have to determine which products were subject to the agreement. This issue has already come up in the instant case, where the defendant contends the plaintiff did not purchase clubs subject to the NPIP.

The timing of the alleged agreement is an even more elusive issue. The period of "probation" given to violators of the policy varied in each circumstance. Callaway's decision would vary "product by product, and it would depend customer by customer, and it would [\*29] depend on what time period . . ." [Rider Deposition at 160]. Callaway would not tell the retailer, and the retailer would not know how long they would be unable to purchase the product. [Rider Deposition at 76]. The NPIPs do not include specific dates, only the item that it purports to cover. Callaway's variable treatment of individual retailers suggests that the length of time the policy remained in effect differed from retailer to retailer. Further, the plaintiff does not dispute that approximately 50% of products covered by the policy are discounted. Thus, the issue of whether the alleged agreement could be negated by the actions of the retailer's themselves would have to be addressed in many of the cases.

Additionally, any formula offered by the plaintiff could not calculate damages for the entire class. The issue of damages would have to be resolved with each individual retailer. First, the markets will fluctuate widely based on geographic location. No comparison of prices that would have been charged without the alleged illegal conduct could be made without litigating this issue. Second, the sales policy did not affect the actions of many retailers. For instance, many retailers [\*30] sold Callaway products at more than the minimum price. Also, many retailers willingly sold Callaway products at the suggested minimum price for other reasons, including the fact that the suggested price built in a substantial profit margin. Further, when consumers purchase golf equipment, they often receive discounts, store credit, or additional free items such as golf balls. The damages calculation would have to include any of the various means of affecting the actual price of the equipment.

Finally, it would be difficult at best for individual consumers to determine whether they were entitled to membership in the class. Individual consumers would have no reason to know about potential litigation connected with their purchase of Callaway products. Even if notice was sufficient to alert every person who purchased a Callaway product within the time period, there would be tremendous difficulty in determining which consumers had legitimate claims. Only the most diligent consumers keep receipts for recreational supplies such as golf clubs for any appreciable amount of time. The fact of purchase would then become a matter for the jury. [Johnston v. HBO Film](#)

*Management, Inc., 265 F.3d 178, 190 (3rd Cir. 2001)* ("In cases raising issues similar to those here, it [\*31] has become well-settled that, as a general rule, an action based substantially on oral rather than written communications is inappropriate for treatment as a class action."). The complaint also fails to address consumers who may have resold their clubs.

## IX.

### **Conclusion**

For the foregoing reasons, the motion for partial summary judgment [Court File #11] is DENIED and the motion for class certification [Court File #14] is DENIED. The plaintiff has not sustained the burden of proving that summary judgment is due under [Rule 56](#) or that this case should be certified as a class action under [Rule 23 of the Federal Rules of Civil Procedure](#). Plaintiff's motion to amend his complaint [Court File #54] is DENIED.

Order accordingly.

**s/ James H. Jarvis**

UNITED STATES DISTRICT JUDGE

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End of Document



## **Mothershed v. Justices of the Supreme Court**

United States Court of Appeals for the Ninth Circuit

April 15, 2005, Argued and Submitted, San Francisco, California ; July 21, 2005, Amended

No. 03-16878

**Reporter**

2005 U.S. App. LEXIS 14812 \*

GEORGE L. MOTHERSHED, Plaintiff-Appellant, v. JUSTICES OF THE SUPREME COURT; CLERK OF THE SUPREME COURT, STATE OF ARIZONA; SUPREME COURT OF ARIZONA DISCIPLINARY COMMISSION; HEARING OFFICER; BAR COUNSEL OF ARIZONA STATE BAR ASSOCIATION; STATE OF OKLAHOMA JUSTICES OF THE SUPREME COURT; OKLAHOMA PROFESSIONAL RESPONSIBILITY TRIBUNAL OF THE SUPREME COURT, Chief Master; OKLAHOMA PROFESSIONAL RESPONSIBILITY TRIBUNAL OF THE SUPREME COURT, Trial Panel of February 1, 2002; GENERAL COUNSEL OF OKLAHOMA BAR ASSOCIATION; TRIAL COUNSEL OF OKLAHOMA BAR ASSOCIATION; RUDOLPH HARGRAVE, Oklahoma Supreme Chief Justice; MADELINE HARGRAVE, Wife; ROBERT E. LAVENDER, Justice, Oklahoma Supreme Court; MAXINE LAVENDER, Wife; JOSEPH M. WATT, Vice-Chief Justice, Oklahoma Supreme Court; CATHY WATT, Wife; RALPH B. HODGES, Justice, Oklahoma Supreme Court; JANELLE HODGES, Wife; MARIAN P. OPALA, Justice, Oklahoma Supreme Court; JANE DOE OPALA, Wife; DANIEL J. BOUDREAU, Justice, Oklahoma Supreme Court; JANE DOE BOUDREAU, Wife; YVONNE KAUGER, Justice, Oklahoma Supreme Court; NED BASTOW, Husband; HARDY SUMMERS, Justice, Oklahoma Supreme Court; MARILYN SUMMERS, Wife; JAMES WINCHESTER, Justice, Oklahoma Supreme Court; SUSAN WINCHESTER, Wife; J. DANIEL MORGAN, Chief Master, Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE MORGAN, Wife; J. PATRICK KENT, Presiding Master, Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE KENT, Wife; ROBERT L. HERT, JR., Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE HERT, Wife; DANA WILLIAMS, Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; DALE CABINESS, Member of Trial Panel of the Professional Responsibility Tribunal of the Supreme Court of the State of Oklahoma; JANE DOE CABINESS, Wife; DAN MURDOCK, General Counsel, Supreme Court of Oklahoma; JANE DOE MURDOCK, Wife; ALLEN J. WELCH, Bar Counsel, Oklahoma Supreme Court; JANE DOE WELCH, Wife; CHARLES E. JONES, Chief Justice, Arizona Supreme Court; JANE DOE JONES, Wife; RUTH V. MCGREGOR, Vice Chief Justice, Arizona Supreme Court; JOHN DOE MCGREGOR, Husband; STANLEY FELDMAN, Justice, Arizona Supreme Court; JANE DOE FELDMAN, Wife; REBECCA WHITE BERCH, Justice, Arizona Supreme Court; JOHN DOE BERCH, Husband; MICHAEL D. RYAN, Justice, Arizona Supreme Court; JANE DOE RYAN, Wife; PETER CAHILL, Member of the Disciplinary Commission of the Supreme Court of Arizona; JESSICA GIFFORD FUNKHOUSER, Member of the Disciplinary Commission of the Supreme Court of Arizona; CYNTHIA L. CHOATE, Member of the Disciplinary Commission of the Supreme Court of Arizona; BARBARA ATWOOD, Member of the Disciplinary Commission of the Supreme Court of Arizona; C. ALAN BOWMAN, Member of the Disciplinary Commission of the Supreme Court of Arizona; CRAIG MEHRENS, Member of the Disciplinary Commission of the Supreme Court of Arizona; STEVEN G. NELSON, Member of the Disciplinary Commission of the Supreme Court of Arizona; LOREN J. BRAUD, Bar Counsel, Arizona Supreme Court aka Loren J. Broad; JANE DOE BRAUD, Wife aka Jane Doe Broad; JOHN PRESSLEY TODD, Hearing Office 7X, Arizona Supreme Court; JANE DOE TODD, Wife; NOEL K. DESSAINT, Clerk, Arizona Supreme Court; WILLIAM M. SPENCE, Attorney; JANE DOE SPENCE, Wife, Defendants-Appellees.

**Subsequent History:** Related proceeding at [State ex rel. Okla. Bar Ass'n v. Mothershed, 2011 OK 84, 2011 Okla. LEXIS 91 \(Okla., 2011\)](#)

**Prior History:** [\*1] Appeal from the United States District Court for the District of Arizona. D.C. No. CV-02-02375-RCB. Robert C. Broomfield, District Judge, Presiding.

[\*Mothershed v. Justices of the Supreme Court, 410 F.3d 602, 2005 U.S. App. LEXIS 10407 \(9th Cir. Ariz., 2005\)\*](#)

**Disposition:** AFFIRMED.

## Core Terms

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Antitrust, district court, disciplinary proceeding, regulation, practice of law, challenges, state court, disciplinary, state bar, Sherman Act, out-of-state, quotation, marks, subject matter jurisdiction, lower federal court, federal court, restrictions, lack subject matter jurisdiction, anti trust law, overbreadth, proceedings, state-court, decisions, licensed

## LexisNexis® Headnotes

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Civil Procedure > ... > Preclusion of Judgments > Full Faith & Credit > General Overview

### [\*\*HN1\*\* \[down arrow\] \*\*Preclusion of Judgments, Full Faith & Credit\*\*](#)

The Rooker-Feldman doctrine's applicability is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Preclusion of Judgments > Full Faith & Credit > General Overview

Civil Procedure > Appeals > Appellate Jurisdiction > State Court Review

Civil Procedure > ... > Jurisdiction on Certiorari > Considerations Governing Review > State Court Decisions

### [\*\*HN2\*\* \[down arrow\] \*\*Subject Matter Jurisdiction, Jurisdiction Over Actions\*\*](#)

Under Rooker-Feldman, lower federal courts are without subject matter jurisdiction to review state court decisions, and state court litigants may therefore only obtain federal review by filing a petition for a writ of certiorari in the Supreme Court of the United States. The doctrine does not, however, prohibit a plaintiff from presenting a generally applicable legal challenge to a state statute in federal court, even if that statute has previously been applied against him in state court litigation.

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Legal Ethics > Sanctions > Disbarments

Civil Procedure > ... > Preclusion of Judgments > Full Faith & Credit > General Overview

Civil Procedure > ... > Jurisdiction on Certiorari > Considerations Governing Review > State Court Decisions

### **HN3** Subject Matter Jurisdiction, Jurisdiction Over Actions

For purposes of the Rooker-Feldman doctrine, United States district courts have subject-matter jurisdiction over general challenges to state bar rules, promulgated by state courts in non-judicial proceedings, which do not require review of a final state-court judgment in a particular case. They do not have jurisdiction, however, over challenges to state-court decisions in particular cases arising out of judicial proceedings even if those challenges allege that the state court's action was unconstitutional. Review of those decisions may be had only in the United States Supreme Court.

Civil Procedure > ... > Preclusion of Judgments > Full Faith & Credit > General Overview

### **HN4** Preclusion of Judgments, Full Faith & Credit

The Rooker-Feldman doctrine is only operative where a federal suit is initiated after state court proceedings have ended. Proceedings end for Rooker-Feldman purposes when the state courts finally resolve the issue that the federal court plaintiff seeks to relitigate in a federal forum, even if other issues remain pending at the state level. A state supreme court's interlocutory ruling will therefore trigger the Rooker-Feldman doctrine's applicability where such ruling constitutes the final determination of an issue.

Antitrust & Trade Law > Sherman Act > General Overview

Governments > State & Territorial Governments > Licenses

### **HN5** Antitrust & Trade Law, Sherman Act

The Sherman Act, [15 U.S.C.S. §§ 1, 2](#), does not apply to certain categories of state action, and included in these categories is the licensing and regulation of attorneys by a state supreme court.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

### **HN6** Public Enforcement, State Civil Actions

The Arizona Uniform State Antitrust Act, [Ariz. Rev. Stat. § 44-1401 et seq.](#), is interpreted in conformity with the federal antitrust laws. To this end, the Arizona legislature clearly intended to strive for uniformity between federal and state antitrust laws. Indeed, [Ariz. Rev. Stat. § 44-1412](#) explicitly provides, it is the intent of the legislature that in construing the Uniform State Antitrust Act, the courts may use as a guide interpretations given by the federal courts to comparable federal antitrust statutes.

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > Erie Doctrine

### **HN7** Federal & State Interrelationships, Erie Doctrine

When interpreting state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Civil Procedure > ... > Justiciability > Standing > General Overview

Civil Procedure > ... > Justiciability > Standing > Third Party Standing

Constitutional Law > ... > Case or Controversy > Standing > Third Party Standing

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Standing

Governments > Legislation > Overbreadth

#### **HN8** [blue icon] **Judicial & Legislative Restraints, Overbreadth & Vagueness of Legislation**

A plaintiff generally must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties. This limitation is relaxed in the *First Amendment* context, however, because when there is a danger of chilling free speech, society's interest in having the statute challenged may outweigh the prudential considerations that normally counsel against third-party standing. A plaintiff's ability to invoke so-called "overbreadth standing" "has nothing to do with whether or not his own *First Amendment* rights are at stake but instead depends upon whether the plaintiff satisfies the requirement of "injury-in-fact," and whether he can be expected satisfactorily to frame the issues in the case.

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

#### **HN9** [blue icon] **Fundamental Freedoms, Freedom of Association**

The right to hire and consult an attorney is protected by the *First Amendment's* guarantee of freedom of speech, association and petition.

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Governments > Courts > Judges

Governments > State & Territorial Governments > Licenses

## [HN10](#) [blue speech bubble icon] Fundamental Freedoms, Freedom of Speech

While the Supreme Court has acknowledged that the right to consult with an attorney falls within the [First Amendment's](#) purview, the Court has also repeatedly emphasized that the States have broad power to regulate the practice of law. The Court has explained that the interest of the States in regulating lawyers is especially great since lawyers are essential to the primary governmental function of administering justice, and have historically been officers of the courts.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

## [HN11](#) [blue speech bubble icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

Time, place, and manner regulations are reasonable provided that the restrictions are justified without reference to the content of the regulated speech, that they are narrowly tailored to serve a significant governmental interest, and that they leave open ample alternative channels for communication of the information. The principal inquiry in determining content neutrality is whether the government has adopted a regulation of speech because of disagreement with the message it conveys. Speech restrictions are content-neutral when they can be justified without reference to the content of the regulated speech.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

Governments > Courts > Rule Application & Interpretation

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

Governments > State & Territorial Governments > Licenses

## [HN12](#) [blue speech bubble icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

Ariz. Sup. Ct. R. 33(d) and 34 are content-neutral time, place and manner restrictions for purposes of the [First Amendment](#) because the rules impose a generally applicable prohibition on the retention of out-of-state counsel without regard to the subject matter of the representation.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Time, Place & Manner Restrictions

## [HN13](#) [blue speech bubble icon] Judicial & Legislative Restraints, Time, Place & Manner Restrictions

A time, place, and manner regulation is narrowly tailored as long as the substantial governmental interest it serves would be achieved less effectively absent the regulation and the regulation achieves its ends without significantly restricting a substantial quantity of speech that does not create the same evils.

**Counsel:** George L. Mothershed, Phoenix, Arizona, argued the cause for the appellant and filed a brief.

LeslieAnn Haacke, Renaud Cook Drury Mesaros, P.A., Phoenix, Arizona, argued the cause for the appellees; Terry Goddard, Attorney General, Phoenix, Arizona, Rosa Mroz, Assistant Attorney General, Phoenix, Arizona, N. Todd McKay, Renaud Cook Drury Mesaros, P.A., Phoenix, Arizona, Charles K. Babb, Assistant Attorney General, Oklahoma City, Oklahoma, and Allen J. Welch, Oklahoma Bar Association, Oklahoma City, Oklahoma, were on the brief.

**Judges:** Before: Alfred T. Goodwin, Robert R. Beezer, and Diarmuid F. O'Scannlain, Circuit Judges. Opinion by Judge O'Scannlain.

**Opinion by:** Diarmuid F. O'Scannlain

## Opinion

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### AMENDED OPINION

O'SCANNLAIN, Circuit Judge:

We must decide whether a disbarred attorney may collaterally attack his state bar disciplinary proceedings in federal court.

I

In 1999, the State Bar of Arizona initiated disciplinary proceedings against George L. Mothershed, an attorney who was licensed by the Oklahoma Bar Association [\*2] but who lived and practiced in Arizona. In response to the disciplinary board's allegation that he had unlawfully practiced law in the State, Mothershed entered a special appearance and moved to dismiss the complaint on the ground that he had not received a summons. The hearing officer denied this motion, and Mothershed subsequently refused to participate further in the disciplinary proceedings. A default judgment was entered against him, and the Supreme Court of Arizona issued an order censuring Mothershed for engaging in the unauthorized practice of law. See [In re Mothershed, No. SB-01-0076-D, 2001 Ariz. LEXIS 63 \(2001\)](#).

The Oklahoma Bar Association thereafter initiated its own disciplinary proceedings against Mothershed. A three-member trial panel found that he had unlawfully practiced law in Arizona, and the Supreme Court of Oklahoma entered an order disbarring him. See [State ex rel. Okla. Bar Ass'n v. Mothershed, 2003 OK 34, 66 P.3d 420, 428 \(Okla. 2003\)](#).

Mothershed responded by filing suit in the United States District Court for the District of Arizona against the Justices of the Oklahoma Supreme Court, the three members of the Oklahoma disciplinary [\*3] trial panel, and several officials of the Oklahoma Bar Association (the "Oklahoma Defendants"). He also sued the Justices of the Arizona Supreme Court, the Clerk of the Arizona Supreme Court, the members of the Arizona Supreme Court Disciplinary Commission, the hearing officer in the Arizona disciplinary proceedings, and a state bar staff counsel (the "Arizona Defendants"). Mothershed alleged that the Arizona disciplinary proceedings were invalid because he had not been served with a summons. He contended that the Oklahoma proceedings were likewise defective because his hearing did not occur between thirty and sixty days after appointment of the trial panel, as required by Rule 6.7 of the

Oklahoma Rules Governing Disciplinary Proceedings.<sup>1</sup> Based upon these alleged procedural shortcomings, Mothershed asserted a claim under [42 U.S.C. § 1983](#) for due process and other constitutional violations, as well as state law tort claims for interference with contractual relationships, defamation, abuse of process, malicious prosecution, false light, and intentional infliction of emotional distress.

[\*4] Mothershed also contended that Arizona Supreme Court *Rules 33(d)* and *34*,<sup>2</sup> which set forth the *pro hac vice* admission requirements for out-of-state attorneys and the standards for admission to the State Bar of Arizona, violate Arizonans' [First Amendment](#) right to consult with an attorney and contravene both the Sherman Antitrust Act, [15 U.S.C. § 1](#), and the Arizona Uniform State Antitrust Act, [ARIZ. REV. STAT. § 44-1402](#). Mothershed requested damages totaling more than \$ 330 million and an injunction reinstating his membership in the Oklahoma Bar Association and prohibiting the defendants from interfering with his Arizona law practice.

[\*5] After the defendants moved to dismiss the complaint on various grounds, the district court dismissed the Oklahoma defendants due to the absence of personal jurisdiction. The court later dismissed the claims against the Arizona defendants on the ground that Mothershed was improperly seeking review of the Arizona bar disciplinary proceedings in a lower federal court and that subject matter jurisdiction was therefore absent under the *Rooker-Feldman* doctrine. Mothershed timely appealed.

## II

In the face of growing judicial uncertainty about the *Rooker-Feldman* doctrine's parameters, the Supreme Court recently reiterated that [HN1](#)<sup>↑</sup> its applicability "is confined to cases of the kind from which the doctrine acquired its name: cases brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments." [Exxon Mobil Corp. v. Saudi Basic Indus. Corp.](#), [161 L. Ed. 2d 454, 544 U.S. , 125 S. Ct. 1517, 1521-22 \(2005\)](#); see also [Rooker v. Fid. Trust Co.](#), [263 U.S. 413, 416, 68 L. Ed. 362, 44 S. Ct. 149 \(1923\)](#); [D.C. Court of Appeals v. Feldman](#), [460 U.S. 462, 486-87, 75 L. Ed. 2d 206, 103 S. Ct. 1303 \(1983\)](#). [\*6]

We must therefore decide whether Mothershed's claims fall within the *Rooker-Feldman* doctrine's narrowed scope.

## A

[HN2](#)<sup>↑</sup> Under *Rooker-Feldman*, lower federal courts are without subject matter jurisdiction to review state court decisions, and state court litigants may therefore only obtain federal review by filing a petition for a writ of certiorari in the Supreme Court of the United States. See [Rooker](#), [263 U.S. at 416](#) (holding that a federal district court lacked subject matter jurisdiction over a suit that effectively sought review of an Indiana state court's decision); [Feldman](#), [460 U.S. at 486-87](#) (holding that a federal district court was without subject matter jurisdiction to entertain a challenge to a decision of the District of Columbia Court of Appeals); see also [28 U.S.C. § 1257](#) ("Final judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court by writ of certiorari . . . ."). The doctrine does not, however, prohibit a plaintiff from presenting a generally applicable legal challenge to a state statute in federal court, even if that statute [\*7] has previously been applied against him in state court litigation.

<sup>1</sup> The rule provides:

The Chief Master or Vice-Chief Master of the Professional Responsibility Tribunal shall notify the respondent and the General Counsel of the appointment and membership of the Trial Panel and of the time and place for hearing, which shall not be less than thirty (30) nor more than sixty (60) days from the date of appointment of the Trial Panel. Extensions of this period may be granted by the Chief Master (or the Vice-Chief Master, in case of the unavailability of the Chief Master) for good cause shown.

<sup>2</sup> **Rule 33(d)** provides that a member in good standing of the bar of another State may be admitted to appear *pro hac vice* in Arizona upon approval by the court hearing the matter. **Rule 34** lists the requirements for admission to the State Bar of Arizona, which include passing the bar examination and being certified by the Committee on Character and Fitness as possessing good moral character.

This distinction is well illustrated by the *Feldman* decision itself. There, two aspiring attorneys had petitioned the District of Columbia Court of Appeals for a waiver of a D.C. bar rule requiring applicants to have graduated from an accredited law school. *Feldman*, 460 U.S. at 466. After the Court of Appeals denied their petitions, the plaintiffs filed suit in federal district court challenging both the D.C. bar rule's general constitutionality and the District of Columbia court's decision in their particular cases. *Id.* at 468, 472. The Supreme Court held that the district court possessed subject matter jurisdiction over the former claim but not the latter. *Id.* at 486-87. The Court explained:

**HN3**[<sup>1</sup>] United States district courts . . . have subject-matter jurisdiction over general challenges to state bar rules, promulgated by state courts in nonjudicial proceedings, which do not require review of a final state-court judgment in a particular case. They do not have jurisdiction, however, over challenges to state-court decisions in particular cases arising out of [\*8] judicial proceedings even if those challenges allege that the state court's action was unconstitutional. Review of those decisions may be had only in this Court.

*Id.* at 486; see also *id.* at 482 n.16 ("Orders of a state court relating to the admission, discipline, and disbarment of members of its bar may be reviewed only by the Supreme Court of the United States on certiorari to the state court, and not by means of an original action in a lower federal court." (quoting *MacKay v. Nesbett*, 412 F.2d 846, 846 (9th Cir. 1969)) (alteration in original)).

Similarly, in *Craig v. State Bar of California*, 141 F.3d 1353, 1354 (9th Cir. 1998) (per curiam), the plaintiff filed a § 1983 claim in federal court against the California bar after the state supreme court denied review of the California Committee of Bar Examiners' refusal to modify the new-attorney oath to comport with his religious beliefs. We held that subject matter jurisdiction was absent because the plaintiff was seeking review of his individual claim and did not present a general challenge to the California bar's policy. *Id.* We reasoned that a [\*9]

plaintiff can challenge the state supreme court's denial of bar admission to a particular applicant, the validity of the state's rules governing admission, or both. Lower federal courts lack subject matter jurisdiction over the first type of challenge . . . . In contrast, a general attack on a state's admissions rules may be heard by lower federal courts because a state supreme court acts in a nonjudicial capacity when it promulgates such rules.

*Id.* (citation omitted).

## B

Mothershed alleges that the Oklahoma defendants denied him due process and committed various state law torts because the Oklahoma bar disciplinary panel did not hold its hearing within the thirty-to-sixty-day time frame required by Rule 6.7 of the Rules Governing Disciplinary Proceedings. Because Mothershed does not contend that Rule 6.7 is systematically disregarded in all attorney disciplinary proceedings or that the rule is itself facially invalid, he is not asserting a "general challenge[] to [a] state bar rule[]." *Feldman*, 460 U.S. at 486. Rather, Mothershed is alleging that the Oklahoma defendants failed to apply Rule 6.7 during his own state bar disciplinary hearing, [\*10] which constitutes a "challenge[] to [a] state-court decision[] in [a] particular case[]." *Id.* Under the *Rooker-Feldman* doctrine, the district court lacked subject matter jurisdiction to review Mothershed's Oklahoma disciplinary proceedings,<sup>3</sup> [\*11] and we therefore affirm the dismissal of the Oklahoma defendants.<sup>4</sup>

<sup>3</sup> In *Exxon Mobil*, the Supreme Court clarified that **HN4**[<sup>1</sup>] the *Rooker-Feldman* doctrine is only operative where a federal suit is initiated after state court proceedings have ended. 125 S. Ct. at 1526 ("In both [*Rooker* and *Feldman*], the losing party in state court filed suit in federal court after the state proceedings ended . . . ."). Proceedings end for *Rooker-Feldman* purposes when the state courts finally resolve the issue that the federal court plaintiff seeks to relitigate in a federal forum, even if other issues remain pending at the state level. See *Federacion de Maestros de Puerto Rico v. Junta de Relaciones del Trabajo de Puerto Rico*, 410 F.3d 17, 25 (1st Cir. 2005) ("if the state court proceedings have finally resolved all the federal questions in the litigation, but state law or purely factual questions (whether great or small) remain to be litigated, then the state proceedings have 'ended' within the meaning of *Rooker-Feldman* on the federal questions at issue"). A state supreme court's interlocutory ruling will therefore trigger the *Rooker-Feldman* doctrine's applicability where such ruling constitutes the final determination of an issue. See *id.* at 28 (relying upon *Exxon Mobil* to conclude that *Rooker-Feldman* prohibited a federal district court from deciding an issue already finally resolved by an interlocutory ruling of the Puerto Rico Supreme Court because "the state court proceedings had ended with regard to the sole federal issue").

## C

Mothershed's claims premised upon the alleged absence of a summons directing him to appear at the Arizona disciplinary hearing are likewise barred by the *Rooker-Feldman* doctrine because these claims constitute a particularized challenge to the Arizona disciplinary proceedings' results. The district court therefore correctly concluded that it lacked subject matter [\*12] jurisdiction over Mothershed's [§ 1983](#) and state law tort claims against the Arizona defendants, all of which are premised upon his failure to receive a summons.

## D

Mothershed also alleges, however, that the admission requirements set forth in Arizona Supreme Court *Rules 33(d)* and *34* violate Arizonans' [First Amendment](#) right to consult an attorney of their choosing and contravene both the Sherman Antitrust Act and the Arizona Uniform State Antitrust Act. These claims pertain to the rules' validity as applied to all attorneys within Arizona (and, indeed, all Arizona residents) and thus do not present an individualized challenge to Mothershed's bar disciplinary proceedings. Rather--like the *Feldman* plaintiffs' general constitutional attack on the D.C. bar's accreditation requirement--these claims constitute a general challenge to the rules governing admission to the Arizona bar. See [Hoover v. Ronwin, 466 U.S. 558, 564-65, 80 L. Ed. 2d 590, 104 S. Ct. 1989 \(1984\)](#) (entertaining a Sherman Act challenge to the Arizona bar exam's grading methodology brought by an attorney who had earlier contested his own exam results in separate Arizona state court proceedings).

Because "a general attack [\*13] on a state's admissions rules may be heard by lower federal courts," [Craig, 141 F.3d at 1354](#), the district court erred by concluding that it lacked subject matter jurisdiction over Mothershed's [First Amendment](#) and antitrust claims against the Arizona defendants.

## III

Although the district court did indeed possess subject matter jurisdiction over Mothershed's general challenges to the Arizona Supreme Court rules, we "may affirm the district court's dismissal on any ground supported by the record." [Wolfe v. Strankman, 392 F.3d 358, 362 \(9th Cir. 2004\)](#). We first consider Mothershed's antitrust claims and then turn to his [First Amendment](#) challenge.

## A

In [Parker v. Brown, 317 U.S. 341, 352, 87 L. Ed. 315, 63 S. Ct. 307 \(1943\)](#), the Supreme Court held that [HN5](#)↑ the Sherman Act does not apply to certain categories of state action. Later decisions have held that one of these categories is the regulation of attorneys by a state supreme court. In [Bates v. State Bar of Arizona, 433 U.S. 350, 359, 53 L. Ed. 2d 810, 97 S. Ct. 2691 \(1977\)](#), for example, the plaintiffs alleged that an Arizona bar disciplinary rule prohibiting advertising by attorneys violated the Sherman [\*14] Act. The Court determined that the Arizona Supreme Court--not the state bar--was the "real party in interest." [Id. at 361](#). That court had "adopted the rules," *id.*, and was "the ultimate body wielding the State's power over the practice of law," [id. at 360](#). Because the advertising

Here, state court proceedings ended for *Rooker-Feldman* purposes when the Oklahoma Supreme Court denied Mothershed's request that it issue a writ of mandamus halting the Oklahoma bar disciplinary proceedings against him. That May 2002 state court ruling finally resolved that the disciplinary proceedings complied with Rule 6.7's timing requirements and that Mothershed's due process rights therefore were not violated, which represent the same issues that Mothershed subsequently sought to relitigate in federal district court.

<sup>4</sup>The district court's dismissal of the Oklahoma defendants was premised upon the absence of personal jurisdiction, not subject matter jurisdiction. Where "subject-matter jurisdiction will involve no arduous inquiry," however, "both expedition and sensitivity to state courts' coequal stature should impel the federal court to dispose of that issue first." [Ruhrgas AG v. Marathon Oil Co., 526 U.S. 574, 587-88, 143 L. Ed. 2d 760, 119 S. Ct. 1563 \(1999\)](#). Here, the subject matter jurisdiction inquiry involves a straightforward application of the *Rooker-Feldman* doctrine, and we accordingly adhere to the Supreme Court's admonition by relying upon the lack of subject matter jurisdiction to dismiss the Oklahoma defendants.

restrictions were "compelled by direction of the State acting as a sovereign," *id.* (internal quotation marks omitted), they were not amenable to a Sherman Act challenge.

Likewise, in *Hoover v. Ronwin*, 466 U.S. at 565, a plaintiff who had failed the Arizona bar exam filed suit against the members of the Committee on Examinations and Admissions alleging that the manner in which they graded the exam violated the Sherman Act. Although the individual members of the Committee were the named defendants, the Court concluded that the suit was barred by *Parker*'s state-action exception because the "Arizona Supreme Court necessarily delegated the administration of the admissions process to the Committee . . . and retained the sole authority to determine who should be admitted to the practice of law in Arizona." *Id.* at 573. Accordingly, the [\*15] conduct being "challenged was in reality that of the Arizona Supreme Court." *Id.*; cf. *Goldfarb v. Va. State Bar*, 421 U.S. 773, 790, 44 L. Ed. 2d 572, 95 S. Ct. 2004 (1975) (holding that a minimum fee schedule enforced by the Virginia state bar did not fall within the *Parker* exception because the fee schedule was not mandated by the Virginia Supreme Court and thus it could not "fairly be said that the State of Virginia through its Supreme Court Rules required the anticompetitive activities").

Here, Mothershed alleges that Arizona Supreme Court Rules 33(d) and 34 violate the Sherman Act. These claims are squarely foreclosed by *Bates* and *Hoover*. Although Mothershed's claim is nominally against certain state bar officials and the Supreme Court Justices in their individual capacities, it is the Supreme Court of Arizona that is the "real party in interest" because the state bar rules that Mothershed is challenging are promulgated by the court in its supervisory role over the practice of law in Arizona. See *In re Shannon*, 179 Ariz. 52, 876 P.2d 548, 571 (Ariz. 1994) ("the determination of who shall practice law in Arizona and under what condition is a function [\*16] placed by the state constitution in this court" (internal quotation marks omitted)). Rules 33(d) and 34 are therefore "compelled by direction of the State acting as a sovereign," *Bates*, 433 U.S. at 360 (internal quotation marks omitted), and are exempt from Sherman Act challenges.

## B

Mothershed also asserts a state antitrust claim under Arizona law. [HN6](#) The Arizona Uniform State Antitrust Act "is interpreted in conformity with the federal [antitrust laws]." *Arizona v. Maricopa County Med. Soc'y*, 643 F.2d 553, 554 n.1 (9th Cir. 1980), rev'd on other grounds, 457 U.S. 332, 73 L. Ed. 2d 48, 102 S. Ct. 2466 (1982); see also *Wedgewood Inv. Corp. v. International Harvester Co.*, 126 Ariz. 157, 613 P.2d 620, 623 (Ariz. Ct. App. 1979) ("The Arizona legislature clearly intended to strive for uniformity between federal and state antitrust laws."). Indeed, *ARIZ. REV. STAT. § 44-1412* explicitly provides, "It is the intent of the legislature that in construing [the Uniform State Antitrust Act], the courts may use as a guide interpretations given by the federal courts to comparable federal antitrust statutes." Cf. *Bunkers Glass Co. v. Pilkington, PLC*, 206 Ariz. 9, 75 P.3d 99, 102, 106 (Ariz. 2003) [\*17] (acknowledging the federal antitrust laws' general "importance" to the interpretation of the Uniform State Antitrust Act, while also observing that Arizona courts need not "rigidly follow federal precedent on every issue of antitrust law regardless of whether differing concerns and interests exist in the state and federal systems").

No court has previously had occasion to consider whether there exists a state-action exception to the Arizona antitrust laws. Nevertheless, in light of the Arizona legislature's avowed desire to achieve uniformity between the Uniform State Antitrust Act and the federal antitrust laws, the Arizona Supreme Court would most likely follow *Bates* and *Hoover* and hold that its rules governing attorney conduct are not amenable to state law antitrust challenges. See *Assurance Co. of Am. v. Wall & Assocs. LLC of Olympia*, 379 F.3d 557, 560 (9th Cir. 2004) [HN7](#) ("When interpreting state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue . . ." (internal quotation marks and citation omitted)). Mothershed's state [\*18] law antitrust claim therefore fails for the same reason as its federal counterpart.

## C

Mothershed contends that Arizona Supreme Court Rules 33(d) and 34 violate the *First Amendment* right of Arizonans to consult with a lawyer of their choosing. Because Mothershed does not allege that he has himself

suffered a *First Amendment* injury, we must first determine whether he has standing to pursue this claim on behalf of other Arizonans.

1

**HN8**[] A "plaintiff generally must assert his own legal rights and interests, and cannot rest his claim to relief on the legal rights or interests of third parties." *Warth v. Seldin*, 422 U.S. 490, 499, 45 L. Ed. 2d 343, 95 S. Ct. 2197 (1975). This limitation is relaxed in the *First Amendment* context, however, because "when there is a danger of chilling free speech, . . . society's interest in having the statute challenged" may outweigh the prudential considerations that normally counsel against third-party standing. *Secretary of Maryland v. Joseph H. Munson Co.*, 467 U.S. 947, 956, 81 L. Ed. 2d 786, 104 S. Ct. 2839 (1984). A plaintiff's ability to invoke so-called "overbreadth standing" "has nothing to do with whether or not [his] own *First Amendment* rights are at [\*19] stake" but instead depends upon whether the plaintiff "satisfies the requirement of 'injury-in-fact,' and whether [he] can be expected satisfactorily to frame the issues in the case." *Id. at 958*; see also *Gospel Missions of Am. v. City of Los Angeles*, 328 F.3d 548, 554 (9th Cir. 2003) ("the requirements of 'overbreadth standing' [are] injury-in-fact and the ability to frame the issues in the case satisfactorily").

In *Secretary of State v. Joseph H. Munson Co.*, 467 U.S. at 950, for example, a for-profit company that charged charities a fee for raising funds on their behalf brought a *First Amendment* challenge to a Maryland statute that prevented charities from paying more than 25% of their funds as expenses. Although the plaintiff was not itself a charity and did not allege that its own *First Amendment* rights were infringed, *id. at 955*, the Court concluded that the company had overbreadth standing to pursue the claim. The Court reasoned that, as a result of the statute, charities were reluctant to contract with the plaintiff because it charged fees in excess of 25% and that the plaintiff's impetus to challenge the [\*20] statute was therefore consonant with the charities' *First Amendment* interests. *Id. at 958* ("The activity sought to be protected is at the heart of the business relationship between Munson and its clients, and Munson's interests in challenging the statute are completely consistent with the *First Amendment* interests of the charities it represents."); see also *Clark v. City of Lakewood*, 259 F.3d 996, 1010-11 (9th Cir. 2001) (holding that the owner of an adult entertainment establishment had overbreadth standing to pursue a *First Amendment* challenge against provisions of an ordinance that required the employees of such establishments to obtain a license because the licensing scheme--although not directly applicable to the owner--threatened his business's viability).

Here, Mothershed alleges that the prohibitions embodied in *Rules 33(d)* and 34 have a chilling effect upon Arizonans' purported *First Amendment* right to consult with out-of-state counsel. Like the plaintiff in *Munson*, Mothershed--though not alleging any *First Amendment* harm to himself--has incurred a financial injury because these rules prevent him from practicing law in the State. Mothershed's [\*21] violation of these provisions has also resulted in his being censured by the Arizona Supreme Court. Moreover, Mothershed has a strong interest in obtaining the invalidation of *Rules 33(d)* and 34 because he desires to practice law in Arizona without being admitted to the state bar. Mothershed therefore satisfies our requirements for overbreadth standing because he has suffered an injury-in-fact and can be expected to pursue the *First Amendment* claim vigorously. See *id. at 1011* (concluding that the owner of the adult entertainment establishment could "satisfactorily frame the issues in the case" because he "had a vested interest in having the [licensing] Ordinance overturned").

2

Although the *First Amendment's* applicability in the area of lawyer-client relations is not well-defined, we recognize that--at least as a general matter--**HN9**[] the "right to hire and consult an attorney is protected by the *First Amendment's* guarantee of freedom of speech, association and petition." *Denius v. Dunlap*, 209 F.3d 944, 953 (7th Cir. 2000); see also *United Mine Workers v. Illinois State Bar Ass'n*, 389 U.S. 217, 221-22, 88 S. Ct. 353, 19 L. Ed. 2d 426 (1967) (holding [\*22] that a union had a *First Amendment* right to employ a salaried attorney to represent members pursuing workers' compensation claims); *DeLoach v. Bevers*, 922 F.2d 618, 620 (10th Cir. 1990) ("The right to retain and consult an attorney . . . implicates . . . clearly established *First Amendment* rights of association and free speech.").

**HN10**[] While the Supreme Court has acknowledged that the right to consult with an attorney falls within the *First Amendment's* purview, the Court has also repeatedly emphasized that "the States have broad power to regulate the practice of law." *III. State Bar Ass'n*, 389 U.S. at 222. The Court has explained that the "interest of the States in regulating lawyers is especially great since lawyers are essential to the primary governmental function of administering justice, and have historically been 'officers of the courts.'" *Goldfarb*, 421 U.S. at 792.

In order to further its substantial interest in regulating the legal profession, the State of Arizona may institute reasonable time, place, and manner restrictions on Arizonans' *First Amendment* right to consult with an attorney.

**HN11**[] Time, place, and manner regulations are [\*23] reasonable provided that "the restrictions 'are justified without reference to the content of the regulated speech, that they are narrowly tailored to serve a significant governmental interest, and that they leave open ample alternative channels for communication of the information.'" *Kuba v. 1-A Agric. Ass'n*, 387 F.3d 850, 858 (9th Cir. 2004) (quoting *Ward v. Rock Against Racism*, 491 U.S. 781, 791, 105 L. Ed. 2d 661, 109 S. Ct. 2746 (1989) (internal quotation marks omitted)).

"The principal inquiry in determining content neutrality . . . is whether the government has adopted a regulation of speech because of disagreement with the message it conveys. Speech restrictions are content-neutral when they can be justified without reference to the content of the regulated speech." *Honolulu Weekly, Inc. v. Harris*, 298 F.3d 1037, 1043 (9th Cir. 2002) (internal quotation marks and citation omitted). **HN12**[] Arizona Supreme Court *Rules* 33(d) and 34 are content-neutral because they impose a generally applicable prohibition on the retention of out-of-state counsel without regard to the subject matter of the representation. (The rules do not, for example, prohibit out-of-state [\*24] counsel from undertaking only certain categories of representation, such as suits against the State or against tobacco companies).

**HN13**[] A time, place, and manner regulation is narrowly tailored as long as the substantial governmental interest it serves "would be achieved less effectively absent the regulation and the regulation achieves its ends without . . . significantly restricting a substantial quantity of speech that does not create the same evils." *Galvin v. Hay*, 374 F.3d 739, 753 (9th Cir. 2004) (internal quotation marks omitted; alteration in original). As already noted, the State of Arizona has a significant interest in regulating the practice of law within its boundaries, see *Bates*, 433 U.S. at 361 ("the regulation of the activities of the bar is at the core of the State's power to protect the public"), and Supreme Court *Rules* 33(d) and 34 further that interest by ensuring that attorneys practicing in the State are qualified and possess a familiarity with Arizona law. The rules' narrow tailoring is further evidenced by the fact that they do not impose a blanket prohibition on the appearance of out-of-state attorneys in Arizona courts. Rather, [\*25] they provide that a qualified out-of-state attorney may be admitted *pro hac vice* by an Arizona court.

Lastly, *Rules* 33(d) and 34 leave open ample alternative channels through which Arizonans can obtain legal representation. Notwithstanding the restrictions on out-of-state attorneys, Arizonans have access to legal representation from the thousands of attorneys licensed by the Arizona bar.

Because Arizona Supreme Court *Rules* 33(d) and 34 are reasonable time, place, and manner regulations of Arizonans' *First Amendment* right to retain and consult with a lawyer, Mothershed's *First Amendment* claim fails as a matter of law.

#### IV

For the foregoing reasons, the judgment of the district court is

**AFFIRMED.**

## In re Enron Corp.

United States Bankruptcy Court for the Southern District of New York

July 22, 2005, Decided

Chapter 11, Case No. 01 B 16034 (AJG), (Confirmed)

**Reporter**

2005 Bankr. LEXIS 3472 \*; 2005 WL 3873894

In re: ENRON CORP., et al., Reorganized Debtors.

**Notice:** NOT FOR PUBLICATION

### **Core Terms**

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filed rate doctrine, electricity, preemption, tariff, rates, wholesale, energy, market-based, cases, state law claim, anti trust law, regulation, preempted, markets, sales, state law, anti-competitive, interstate, violations, manipulation, transactions, antitrust, refunds, Federal Power Act, commerce, entities, reasons

### **LexisNexis® Headnotes**

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Constitutional Law > Supremacy Clause > Federal Preemption

#### [HN1](#) [] **Supremacy Clause, Federal Preemption**

Federal preemption of state law is rooted in the [Supremacy Clause, U.S. Const. art. VI, cl. 2](#). Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction.

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > Preemption

#### [HN2](#) [] **Federal Common Law, Preemption**

In the absence of an express preemption by Congress, state law is preempted (1) when Congress intends that federal law occupy a given field (field preemption), and (2) to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress.

Constitutional Law > Supremacy Clause > Federal Preemption

Energy & Utilities Law > Electric Power Industry > Federal Power Act > Judicial Review

### **HN3[] Supremacy Clause, Federal Preemption**

State actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by the Federal Power Act, 16 U.S.C.S. § 824-824m, because the conduct the state sought to condemn was expressly governed by tariffs, and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to Federal Energy Regulatory Commission (FERC), to enforce and to seek remedy.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN4[] Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) has been granted broad authority by Congress, in addition to the authority to determine the just and reasonable rates for wholesale power. The statute delegates to the FERC exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states. Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states. 16 U.S.C.S. § 824-824m.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN5[] Federal Power Act, Federal Rate Regulation**

See [16 U.S.C.S. § 824e](#).

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

### **HN6[] Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. FERC can proceed by rule making rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. [16 U.S.C.S. §§ 824d, 824e; 42 U.S.C.S. § 7173\(c\)](#).

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

### **HN7[] Regulated Practices, Market Definition**

"Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include (a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; (b) unexplained or unusual redeclarations of availability; (c) unusual trades or transactions; (d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and (e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### **HN8** **Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) can order disgorgement of unjust profits for tariff violations that occurred after October 2, 2000. Further, implicit in FERC orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards are subject to revocation of their market-based rate authority.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

#### **HN9** **Electric Power Rates, Filed Rate Doctrine**

The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### **HN10** **Federal Power Act, Federal Rate Regulation**

The Federal Energy Regulatory Commission (FERC) requires each seller to file quarterly reports pursuant to [16 U.S.C.S. § 824d\(c\)](#) on transaction-specific information about its sales and purchases at market-based rates. While market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

#### **HN11** **Federal Power Act, Federal Rate Regulation**

Implicit in Federal Energy Regulatory Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## [\*\*HN12\*\*](#) [L] **Federal Power Act, Federal Rate Regulation**

Where marketers have not properly reported to the Federal Energy Regulatory Commission (FERC) and such improper reporting affected the reasonableness of the tariff approved by FERC the application of the filed rate doctrine.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## [\*\*HN13\*\*](#) [L] **Federal Power Act, Federal Rate Regulation**

Without the availability of retroactive refunds, parties aggrieved by an illegal rate would have no remedy before the Federal Energy Regulatory Commission, and the filed rate doctrine would preclude a direct action against an offending seller. Such a result does not comport with the underlying theory or the regulatory structure established by the Federal Power Act.

Antitrust & Trade Law > Regulated Practices > Price Discrimination > General Overview

## [\*\*HN14\*\*](#) [L] **Regulated Practices, Price Discrimination**

An injury implies violation of a legal right.

Antitrust & Trade Law > Regulated Practices > Price Discrimination > General Overview

## [\*\*HN15\*\*](#) [L] **Regulated Practices, Price Discrimination**

A rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade. What rates are legal is determined by the Act to Regulate Commerce. Under the latter act the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## [\*\*HN16\*\*](#) [L] **Federal Power Act, Federal Rate Regulation**

Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged.

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## [\*\*HN17\*\*](#) [L] **Federal Power Act, Federal Rate Regulation**

Remedies for breach and non-performance of the Federal Energy Regulatory Commission (FERC)-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC.

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine

## **HN18** [+] **Electric Power Rates, Filed Rate Doctrine**

The filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate making process would subvert the authority of rate-setting bodies and undermine the regulatory regime.

**Counsel:** [\*1] For Reorganized Debtors, Special Counsel: Edward A. Smith, Esq., Of Counsel, CADWALADER, WICKERSHAM & TAFT LLP, New York, NY; Mark C. Ellenberg, Esq., David F. Williams, Esq., Of Counsel, Washington, DC.

For Valley Center Municipal Water District, Sweetwater Authority, and Padre Dam Municipal Water District: C. Michael Cowett, Esq., Robert J. Hanna, Esq., James B. Gilpin, Esq., Mary E. Coburn, Esq., Of Counsel, BEST BEST & KRIEGER LLP, San Diego, California.

**Judges:** Arthur J. Gonzalez, UNITED STATES BANKRUPTCY JUDGE.

**Opinion by:** Arthur J. Gonzalez

## **Opinion**

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OPINION SUSTAINING DEBTORS' OBJECTION TO PROOF OF CLAIM NO. 12231 FILED BY VALLEY CENTER MUNICIPAL WATER DISTRICT; TO PROOF OF CLAIM NO. 12238 FILED BY SWEETWATER AUTHORITY; AND TO PROOF OF AMENDED CLAIM NO. 23154 FILED BY PADRE DAM MUNICIPAL WATER DISTRICT REGARDING STATE LAW CLAIMS IN ELECTRICITY MARKET

ARTHUR J. GONZALEZ

United States Bankruptcy Judge

On October 11, 2002, plaintiff's counsel filed separate proofs of claims ((Claim Nos. 12231, 12238, and 23154 (amending and superseding Claim No. 12232), collectively the "Claims")) in unliquidated amounts on behalf of Valley Center Municipal Water District, Sweetwater Authority, and Padre Dam Municipal Water District [\*2] (collectively, the "Claimants") against Enron Corporation ("Enron") and certain of its affiliated entities (collectively, the "Debtors"). The Claims are based on actions filed by the Claimants and other plaintiffs against Enron Energy Services, Inc. ("EESI"), Enron Power Marketing, Inc. ("EPMI") and other defendants in the Superior Court of the State of California for San Diego County.

The Claimants allege that the Debtors manipulated energy markets in California and overcharged for energy through unlawful and anti-competitive acts during the western power crisis of 2000 and 2001. They maintain the alleged manipulation in the electricity market constitutes a violation of state **antitrust law** and unfair competition law, and seek disgorgement, restitution, actual and treble damages together with interest and injunctive relief.<sup>1</sup> On February 18, 2005, the Debtors filed objections to the Claimants' state law claims and argued that the Federal Power Act (the "FPA") preempts the state laws and the filed rate doctrine precludes consideration of these claims.

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<sup>1</sup> California **Antitrust Law**, Business & Professional Code [§ 16720 et.seq.](#) (The Cartwright Act) and California Unfair Competition Law, Business [\*3] & Professional Code [§ 17200](#). Claimants allege that the Debtors' violation of the Cartwright Act, by engaging in acts and practices which constitute anti-competitive practices, violates Business & Professional Code [§ 17200](#)'s proscription against engaging in unlawful business acts and practices.

The issues before the Court are whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine. The Court finds that because the Federal Energy Regulatory Commission ("FERC") has exclusive jurisdiction over interstate sales of wholesale electricity, the state law claims sought to be enforced by Claimants in the prosecution of the Claims are preempted by the FPA. Further, the filed rate doctrine precludes consideration of such Claims.

## I. BACKGROUND

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the "Plan") in these cases. The Plan became effective on November [\*4] 17, 2004.

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, the California legislature had passed Assembly Bill 1890<sup>2</sup>(the "Bill") to create two non-governmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and the ISO were organized under California law, but regulated by FERC. [California v. Dynegy, Inc., 375 F.3d 831, 850 \(9th Cir. 2004\)](#). The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC found that the Debtors engaged in gaming<sup>3</sup> in the form of inappropriate trading strategies and further engaged in the deliberate submission of false information or the deliberate omission of material [\*5] information. [Enron Power Mktg., Inc., et al., 106 FERC ¶ 61,024 \(2004\)](#). Both proceedings are ongoing, including the determination of remedies by FERC.

## II. DISCUSSION

### A. Legal Standard of Preemption

[HN1](#) [↑] "Federal preemption of state law is rooted in the [Supremacy Clause, Article VI, clause 2, of the United States Constitution](#)." *Transmission Agency of Cal. v. Sierra Pacific Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. [Metro. Life Ins. Co. v. Taylor, 481 U.S. at 63-64, 107 S. Ct. 1542, 95 L. Ed. 2d 55 \(1987\)](#). Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction. [Caterpillar, Inc. v. Williams, 482 U.S. at 393, 107 S. Ct. 2425, 96 L. Ed. 2d 318 \(1987\)](#).

Here, neither [\*6] party raises the argument that complete preemption is applicable, nor is there any evidence in the record that would support the conclusion that Congress intended for complete preemption to apply in this case. [HN2](#) [↑] In the absence of an express preemption by Congress, state law is preempted (1) "when Congress intends that federal law occupy a given field." [Silkwood v. Kerr-McGee Corp., 464 U.S. 238, 248, 104 S. Ct. 615, 78 L. Ed. 2d 443 \(1984\)](#) ("Field Preemption"), and (2) "to the extent that state law actually conflicts with federal law, that is,

<sup>2</sup> 1996 Cal. Stat. 854

<sup>3</sup> The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule ... to the detriment of the efficiency of, and of consumers in, the ISO markets." [Am. Electric Power Service Corp., et al., 103 FERC ¶ 61,346 \(2003\)](#).

when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* ("Conflict Preemption").

## B. Preemption

### 1) Field Preemption

The Debtors, in support of their position that the state law claims should be barred by FERC's exclusive jurisdiction, cite to *Grays Harbor v. Idacorp Inc., 379 F.3d 641 (9th Cir. 2004)*, *Dynegy, and Snohomish County v. Dynegy Power Marketing Inc., 384 F.3d 756 (9th Cir. 2004)*. These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The Debtors argue that state law claims in the [\*7] instant case, alleging violations of state antitrust and unfair competition law, are nearly identical to those involved in the cited cases, and for the reasons set forth in those cases, field preemption is applicable here.

The *Dynegy* court ruled that [HN3](#) "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." [375 F.3d at 852](#).

The Court finds that the statute's framework under the FPA supports the conclusion in *Dynegy* that [HN4](#) FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states . . . . Retail sales of electricity and wholesale intrastate sales [\[\\*8\]](#) are within the exclusive jurisdiction of the states." Federal Power Act, [16 U.S.C. § 824-824m](#).

Claimants do not dispute that the transactions at issue involved wholesale interstate sales. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute should be characterized as either retail sales of electricity or wholesale intrastate sales. The statute provides that upon a determination by FERC that [HN5](#) "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, *the Commission shall determine* the just and reasonable rate, charge, classification, rule, regulation, *practice, or contract* to be thereafter observed and in force, and shall fix the same by order." Federal Power Act, [16 U.S.C. § 824e](#) (emphasis added).

Moreover, pursuant to the statute, [HN6](#) FERC possesses broad remedial authority to address anti-competitive behavior, specifically through profit [\[\\*9\]](#) disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. Federal Power Act, [§§ 205, 206\(a\)](#), as amended, [16 U.S.C.A. §§ 824d, 824e](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.A. § 7173\(c\)](#).

In addition, after the deregulation of California energy markets, the central transactions and the wholesale sales of energy in interstate commerce were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded, "FERC is doing enough regulation to justify federal preemption of state laws under the market-based system of setting wholesale electricity rates." [Snohomish, 384 F.3d at 760-61](#). For instance,

- (1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and the ISO. FERC approved the market-based tariffs only upon [\[\\*10\]](#) a showing that the seller

lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under [FPA §205\(c\)](#) [16 U.S.C. §824d\(c\)](#). (3) FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, "[e]ach participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market." *Id.*

The Court also recognizes that "entities that transact through the ISO or [the] PX and engage in improper practices<sup>4</sup> are in violation of filed tariffs . . . . FERC and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement." [103 FERC ¶ 61,346](#). Here, Claimants do not dispute the fact that it procured electricity through the market administered by the ISO.

Moreover, the Court finds that [Otter Tail Power Co. v. United States](#), 410 U.S. 366, 93 S. Ct. 1022, 35 L. Ed. 2d 359 (1973), and [California v. Federal Power Commission](#), 369 U.S. 482, 82 S. Ct. 901, 8 L. Ed. 2d 54 (1962) are not controlling in the instant case. In both cases, the Supreme Court found that Congress does not intend to bar governments from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions. However, two important differences exist. First, both cases discussed issues of the interaction between federal administrative law [**\*12**] and federal **antitrust law**; thereby no state law preemption issue was presented in these cases. In *California v. Federal Power Commission*, a gas company filed a motion to dismiss the antitrust suit pursuant to the Clayton Act, [§ 7](#) as amended [15 U.S.C.A. §18](#), or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's assets pursuant to the Natural Gas Act (the "NGA"), [§ 7\(c\)](#) as amended [15 U.S.C.A. §717f\(c\)](#), before the Power Energy Commission. [369 U.S. at 483](#). In *Otter Tail Power*, the government brought an action against an electric power company to enjoin violations of the Sherman Act, [15 U.S.C.A. §2](#). [410 U.S. at 368](#). In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws. The Court will not address whether, as a result, Congress has left room for enforcement of state antitrust laws.

Second, and more importantly, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC. As the Court discussed above, the statute under [16 U.S.C.A. §§ 824d, 824e\(a\)](#) provides [**\*13**] FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations.[HN8](#)<sup>↑</sup> It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." [103 FERC ¶ 61,346](#). Further, "implicit in Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority." [106 FERC ¶ 61,024](#).

In contrast, the court in *California v. Federal Power Commission* concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the Clayton Act. [369 U.S. at 485](#). "The Commission's standard, [**\*14**] set forth in [§ 7 of the NGA](#), will serve 'the public convenience and necessity.' If existing natural gas companies violate the antitrust laws, the Commission is directed by [§ 20\(a\)](#) to 'transmit such evidence' to the

<sup>4</sup> Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. [HN7](#)<sup>↑</sup> "Anomalous market behavior" is (1) behavior that departs [**\*11**] significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges." [Am. Elec. Power Serv. Corp. et al., 103 FERC ¶ 61,346\(2003\)](#).

Attorney General." *Id. at 486*. Similarly, the Court in *Otter Tail Power* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the Sherman Act. *410 U.S. at 375*. Moreover, the Supreme Court in *Carnation Co. v. Pacific Westbound Conference*, *383 U.S. 213, 383 U.S. 932, 86 S. Ct. 781, 15 L. Ed. 2d 709 (1966)* declined to grant antitrust immunity to a shipping company because "the provisions of the Shipping Act, 46 U.S.C.A. §801, can not reasonably be construed as an implied repeal of antitrust regulation of the shipping industry's rate-making activities." *Id. at 217*. The Shipping Act does not give the Federal Maritime Commission (the "FMC") any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. *Square D Co. v. Niagara Frontier Tariff Bureau*, *476 U.S. 409, 422, 106 S. Ct. 1922, 90 L. Ed. 2d 413 (1986)*.

The Court further finds that *Grays Harbor and Gulf States Util. Co. v. Alabama Power Co.*, *824 F.2d 1465 (5th Cir. 1987)* are not [\*15] applicable in the instant case. The courts in both cases concluded that the state law claims concerning contractual disputes were not within the scope of FERC's jurisdiction. The facts here are distinguishable. First, the state law claims in the cited cases were related to contractual issues, which exclusively fall within a state's jurisdiction. The court in *Grays Harbor* granted the utility leave to amend its complaint to seek declaratory relief only as to issues of contract formation. *379 F.3d. at 652-53*. Similarly, the court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. *824 F.2d at 1474*. Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily intrude upon the rate-setting jurisdiction of FERC. *Grays Harbor*, *379 F.3d. at 653*. Therefore, field preemption bars the Claimants from pursuing its state law claims before the Court.

### C. Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court concludes that FERC has broad authority concerning anti-competitive [\*16] activities related to the filed rate, apart from that FERC has authority to determine the "just and reasonable" rates for wholesale power. A conflict between the FPA in which grants FERC jurisdiction over the anti-competitive acts and state antitrust claims exists. Accordingly, conflict preemption also bars the Claimants from pursuing state law claims before the Court.

### D. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. *HN9*<sup>↑</sup>] The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. *E. & J. Gallo Winery v. Encana Energy Servs., Inc.*, Case No. CV F 03-5412 AWILJO. at 15. The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority."

[\*17] *Ark. L.A. Gas Co. v. Frank Hall*, *453 U.S. 571, 577-78, 101 S. Ct. 2925, 69 L. Ed. 2d 856 (1981)*. The Court also acknowledges that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant." *City of Cleveland v. FPC*, *525 F.2d 845, 854, 174 U.S. App. D.C. 1 (D.C. Cir. 1976)*.

In addition, *HN10*<sup>↑</sup>] FERC required each seller to file quarterly reports pursuant to FPA §205(c) *16 U.S.C. §824d(c)* on transaction-specific information about its sales and purchases at market-based rates. The court in *Grays Harbor* concluded "while market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine." *379 F.3d at 651*.

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that "the reporting requirements are an integral part of a tariff, with FERC's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [383 F.3d at 1016](#). On August 13, 2002, FERC's Initial Report [[\\*18](#)] in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.<sup>5</sup> Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. [106 FERC ¶ 61,024](#). As noted by FERC,

[HN11](#)[[↑](#)] implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in status (which would include changes in their generation market shares) that reflect a departure from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized [HN12](#)[[↑](#)] the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. [383 F.3d at 1016](#).

[HN13](#)[[↑](#)] Without the availability of retroactive refunds, "[p]arties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

The Court finds that determining the liability or the legal right of Claimants against the Debtors for violation of the antitrust laws would have to be measured by the tariff. Therefore, the filed rate doctrine would be applicable.

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the Supreme Court in [Keogh v. Chicago & N.W.R.Y. Co., 260 U.S. 156, 43 S. Ct. 47, 67 L. Ed. 183 \(1922\)](#), stated that [HN14](#)[[↑](#)] "[i]njury implies violation of a legal right." [Id. at 163](#). The Supreme Court concluded that [[\\*20](#)] "the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff." [Id. at 163](#). Justice Brandeis explained [HN15](#)[[↑](#)] "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Anti-Trust Act. What rates are legal is determined by the Act to Regulate Commerce. Under [Section 8](#) of the latter act . . . the exaction of any illegal rate makes the carrier liable to the 'person injured thereby for the full amount of damages sustained in consequence of any such violation.'" [Id. at 162](#). Thus, the finding of liability in antitrust laws would be integral to the Court's determination of whether the Debtors are liable due to their violations of state **antitrust law** and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. "In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* [[\\*21](#)] contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company." [453 U.S. at 579](#). The Supreme Court rejected this argument by reasoning that "the mere fact that respondents brought this suit under state law would not rescue it, for when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce . . . [HN16](#)[[↑](#)] Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged." [Id. at 580-84](#).

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<sup>5</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, [[\\*19](#)] as required under their market-based rate authorization. [106 FERC ¶ 61,024](#).

Moreover, to award monetary relief, the Court would have to determine a "fair price." Thus, the filed rate doctrine bars the Court from awarding monetary damages sought by Claimants. Nonetheless, the Court finds that injunctive relief would also be unavailable to Claimants. The Court agrees with the Ninth Circuit's decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. [384 F.3d at 762](#). [HN17](#) [↑] "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate [\*22] wholesale electricity market fall within the exclusive domain of FERC." [Dynegy, 375 F.3d at 836](#).

The decisions from the Second Circuit in [Sun City Taxpayers' Association v. Citizens Utilities Co., 45 F.3d 58](#) (2d Cir. 1995) and [Wegoland Ltd. v. NYNEX Corp., 27 F.3d 17](#) (2d Cir. 1994), provide an additional basis for dismissal of the Claims sought by Claimants. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. [Sun City Taxpayers' Ass'n v. Citizens Utils. Co., 847 F.Supp. 281, 291 \(D. Conn. 1994\)](#). The Second Circuit in *Wegoland* recognized that [HN18](#) [↑] the filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making [\*23] process would subvert the authority of rate-setting bodies and undermine the regulatory regime. [27 F.3d at 21](#).

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects Claimants' challenge to the application of the filed rate doctrine. Accordingly, the filed rate doctrine bars the relief sought by Claimants.

### III. Conclusion

For the foregoing reasons, the Court concludes that the state law claims sought by Claimants concerning electricity market manipulation are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims.

Counsel for the Debtors is directed to settle an order consistent with this opinion.

Dated: New York, New York

July 22, 2005

**/s/ Arthur J. Gonzalez**

UNITED STATES BANKRUPTCY JUDGE



## **Loeffel Steel Prods. v. Delta Brands, Inc.**

United States District Court for the Northern District of Illinois, Eastern Division

July 22, 2005, Decided ; July 22, 2005, Filed

No. 01 C 9389

**Reporter**

387 F. Supp. 2d 794 \*; 2005 U.S. Dist. LEXIS 15718 \*\*; 2005 WL 6200338

LOEFFEL STEEL PRODUCTS, INC., Plaintiff, vs. DELTA BRANDS, INC., d/b/a DBI; and SAMUEL F. SAVARIEGO, individually, Defendants.

**Subsequent History:** Partial summary judgment denied by, Motion to strike denied by [Loeffel Steel Prods. v. Delta Brands, Inc., 379 F. Supp. 2d 968, 2005 U.S. Dist. LEXIS 15278 \(N.D. Ill., July 28, 2005\)](#)

**Prior History:** [Loeffel Steel Prods. v. Delta Brands, 372 F. Supp. 2d 1104, 2005 U.S. Dist. LEXIS 11601 \(N.D. Ill., 2005\)](#)

## **Core Terms**

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Loeffel, steel, economic loss, metal, processing, damages, reliability, deposition, defendants', machine, service center, products, lost profits, methodology, cases, expert opinion, calculation, comparable, expertise, expert testimony, Declaration, customers, employees, expert witness, manufactured, automotive, profits, certified public accountant, district court, customer base

## **LexisNexis® Headnotes**

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Civil Procedure > Judicial Officers > Judges > General Overview

Evidence > Admissibility > Expert Witnesses

Evidence > ... > Procedural Matters > Preliminary Questions > General Overview

Evidence > Admissibility > Scientific Evidence > Standards for Admissibility

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > Admissibility > Expert Witnesses > Helpfulness

## **[HN1](#) [blue download icon] Judicial Officers, Judges**

In the context of determining the admissibility of expert testimony, the United States Supreme Court stressed the trial judge's obligation to act as a gatekeeper to ensure that expert testimony is reliable. The insistence on reliability

helps to ensure the integrity of the judicial process. That goal is of such obvious and transcendent importance that judges can act sua sponte to prohibit testimony that does not pass muster under the Daubert standard.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Procedural Matters > Preliminary Questions > General Overview

Evidence > Admissibility > Scientific Evidence > General Overview

Evidence > ... > Testimony > Examination > General Overview

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

## **HN2** [down arrow] Expert Witnesses, Daubert Standard

In the context of determining the admissibility of expert testimony, while Daubert reaffirmed the value of the adversary system generally and the capability of juries to understand scientific evidence and weigh the credibility of the competing experts, with their often absolutist and clashing conclusions, it also made clear that in those cases in which the proponent of an expert could not demonstrate the reliability of the methodology employed by the expert, the court was required to disallow the testimony. The opportunity for vigorous cross examination and the presentation of contrary evidence - the traditional and appropriate means of attacking shaky but admissible evidence, is not a basis for allowing otherwise inadmissible testimony to be admitted.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > Admissibility > Scientific Evidence > Standards for Admissibility

Evidence > ... > Testimony > Expert Witnesses > General Overview

## **HN3** [down arrow] Expert Witnesses, Daubert Standard

In the context of determining the admissibility of expert testimony, the Daubert factors are not applicable, semper ubique et ab omnibus. They need only be considered when doing so will aid in the determination of the testimony's reliability. The inquiry is always, and of necessity, highly fact- specific, and no one factor, even when applicable, is outcome-determinative.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

## **HN4** [down arrow] Expert Witnesses, Daubert Standard

In the context of determining the admissibility of expert testimony, Daubert cautions judges assessing a proffer of expert testimony under [Fed. R. Evid. 702](#) to be mindful of other applicable rules, such as [Fed. R. Evid. 703](#), which

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permits an expert to base an opinion on information that need not itself be admissible, so long as it is the kind of information relied on by other experts in the field.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

#### **HN5** Expert Witnesses, Daubert Standard

In the context of determining the admissibility of expert testimony, overemphasis on qualifications over testimonial reliability reflects a pre-Daubert sensibility.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

#### **HN6** Expert Witnesses, Daubert Standard

In the context of determining the admissibility of expert testimony, no case holds that only a certified public accountant has the necessary expertise to testify about economic loss. In fact, being a certified public accountant does not ensure admissibility of testimony.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

Evidence > Admissibility > Expert Witnesses > Helpfulness

#### **HN7** Expert Witnesses, Daubert Standard

Anyone with relevant expertise enabling him to offer responsible opinion testimony helpful to judge or jury may qualify as an expert witness.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > Admissibility > Scientific Evidence > Standards for Admissibility

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

#### **HN8** Expert Witnesses, Daubert Standard

While the Daubert factors apply to valuation testimony, whether offered by certified public accountants or economists, the Daubert factors are not to be rigidly applied in this or any other context. In some context, they may not be applicable at all or may have diminished utility as measures of reliability. Some courts have held they do not conform easily to an analysis of economic theory. In determining the admissibility of expert testimony with respect to future lost profits, a trial judge has considerable leeway in determining the testimony's reliability.

Commercial Law (UCC) > Sales (Article 2) > Remedies > General Overview

Contracts Law > ... > Measurement of Damages > Foreseeable Damages > General Overview

Torts > ... > Types of Damages > Property Damages > Measurements

### **[HN9](#) [↓] Sales (Article 2), Remedies**

Both contract law and the Uniform Commercial Code provide the appropriate remedy for "economic loss" occasioned by diminished commercial expectations, not coupled with injury to person or property. Generally speaking, a defective product can cause three types of injury: personal injury, property damage, and economic loss. "Economic loss" has been defined as damages for inadequate value, costs of repair and replacement of the defective product, or consequent loss of profits - without any claim of personal injury or damage to other property as well as the diminution in the value of the product because it is inferior in quality and does not work for the general purposes for which it was manufactured and sold.

Business & Corporate Compliance > ... > Damages > Types of Damages > Consequential Damages

Contracts Law > ... > Sales of Goods > Warranties > General Overview

Commercial Law (UCC) > ... > Application & Construction > Remedies > Damages

Commercial Law (UCC) > Sales (Article 2) > General Overview

Commercial Law (UCC) > Sales (Article 2) > Remedies > General Overview

Commercial Law (UCC) > ... > Buyer Remedies > Damages > General Overview

Commercial Law (UCC) > ... > Buyer Remedies > Damages > Damages for Breach Following Acceptance

Commercial Law (UCC) > ... > Buyer Remedies > Damages > Consequential & Incidental Damages

Contracts Law > ... > Sales of Goods > Breach, Excuse & Repudiation > General Overview

### **[HN10](#) [↓] Damages, Consequential Damages**

The Uniform Commercial Code provides that the measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount. [810 III. Comp. Stat. 5/2-714\(2\)](#). In addition, a party may also recover incidental and consequential damages, [810 III. Comp. Stat. 5/2-715](#), including lost profits.

Torts > Business Torts > Fraud & Misrepresentation > General Overview

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## [\*\*HN11\*\*](#) [blue document icon] **Business Torts, Fraud & Misrepresentation**

The victim of a fraudulent misrepresentation is entitled to recover as damages those losses caused by the misrepresentation, including the difference between the value of what he has received in the transaction, and its purchase price or other value given for it.

Torts > Business Torts > Fraud & Misrepresentation > General Overview

## [\*\*HN12\*\*](#) [blue document icon] **Business Torts, Fraud & Misrepresentation**

The benefit of the bargain rule provides that the measure of damages is the difference between the actual value of what plaintiff received and its value had the representations been true.

Evidence > Admissibility > Expert Witnesses > Helpfulness

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN13\*\*](#) [blue document icon] **Expert Witnesses, Helpfulness**

Expert opinions that are contrary to law are inadmissible. They cannot be said to be scientific, to be reliable, or to be helpful to the trier of fact.

Criminal Law & Procedure > Counsel > Right to Counsel > General Overview

Legal Ethics > Client Relations > Duties to Client > Effective Representation

## [\*\*HN14\*\*](#) [blue document icon] **Counsel, Right to Counsel**

There is more in membership in the Bar than a license to sign a brief or intone a prosy argument. Justice is not a game, and zealous advocacy does not entitle a lawyer to hoodwink a judge or an opponent who is not otherwise.

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN15\*\*](#) [blue document icon] **Testimony, Expert Witnesses**

See [\*Fed. R. Evid. 703\*](#).

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN16\*\*](#) [blue document icon] **Expert Witnesses, Daubert Standard**

[\*Fed. R. Evid. 703\*](#)'s relaxation of the usual requirement of firsthand knowledge - a rule which represents a pervasive manifestation of the common law's insistence upon the most reliable sources of information - was premised on an assumption that the expert's opinion will have a reliable basis in the knowledge and experience of his discipline.

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Types of Evidence > Testimony > General Overview

### **HN17** [] **Testimony, Expert Witnesses**

While [Fed. R. Evid. 703](#) was intended to liberalize the rules relating to expert testimony, it was not intended to abolish the hearsay rule and to allow a witness, under the guise of giving expert testimony, to in effect become the mouthpiece of the witnesses on whose statements or opinions the expert purports to base his opinion.

Evidence > Admissibility > Expert Witnesses

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN18** [] **Admissibility, Expert Witnesses**

Under [Fed. R. Evid. 703](#), an expert may rely on hearsay in formulating his opinion - provided the requirements of [Fed. R. Evid. 702](#) are met - but the evidence is not admissible for the truth of the matters asserted.

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN19** [] **Testimony, Expert Witnesses**

[Fed. R. Evid. 703](#) was never intended to allow oblique evasions of the hearsay rule. The United States Court of Appeals for the Seventh Circuit acknowledged that it is common in technical fields for an expert to base an opinion in part on what a different expert believes on the basis of expert knowledge not possessed by the first expert.

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN20** [] **Testimony, Expert Witnesses**

A scientist, however well credentialed he may be, is not permitted to be the mouthpiece of a scientist in a different specialty. That would not be responsible science. An expert's "professional knowledge and ability" must be adequate to evaluate calculations and opinions upon which he based his opinion.

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN21** [] **Testimony, Expert Witnesses**

The rationale of [Fed. R. Evid. 703](#) is certainly not satisfied where the expert fails to demonstrate any basis for concluding that another individual's opinion on a subjective financial prediction was reliable, other than the fact that it was the opinion of someone he believed to be an expert who had a financial interest in making an accurate prediction.

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Evidence > ... > Testimony > Expert Witnesses > General Overview

Torts > ... > Proof > Custom > Expert Testimony

Torts > Business Torts > General Overview

## **HN22** [] **Testimony, Expert Witnesses**

In the context of determining the admissibility of expert testimony, in calculating lost future profits or lost business, the measure of damages is guided by analysis of comparable businesses in the area. The business used as a standard must be as nearly identical to the plaintiff's as possible. This is often referred to as the "yardstick approach." Absent the requisite showing of comparability, a damage model that predicts either the presence or absence of future profits is impermissibly speculative and conjectural. Of course, exact correlation is not necessary but the samples must be fair congeners. If they are not, the comparison is manifestly unreliable and cannot logically advance a material aspect of the proposing party's case. The United States Supreme Court refers to this second prong of the Daubert analysis as the fit requirement.

Antitrust & Trade Law > ... > Market Definition > Relevant Market > Geographic Market Definition

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

## **HN23** [] **Relevant Market, Geographic Market Definition**

In antitrust cases, proof of the relevant product and geographic market is absolutely essential. A determination of the geographic market must entail an analysis of several factors including the location of competitors and price data.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

## **HN24** [] **Expert Witnesses, Daubert Standard**

It cannot be too often repeated or too strongly emphasized that nothing in either Daubert or the Federal Rules of Evidence requires a district court to admit opinion evidence that is connected to existing data only by the ipse dixit of the expert. A court may conclude that there is simply too great an analytical gap between the data and the opinion proffered.

Evidence > Admissibility > Expert Witnesses

Evidence > ... > Testimony > Expert Witnesses > General Overview

## **HN25** [] **Admissibility, Expert Witnesses**

In the context of determining the admissibility of expert testimony, spending a few minutes on the internet does not make one an expert on any "industry" or on any topic.

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Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > Admissibility > Scientific Evidence > Standards for Admissibility

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

#### **HN26** [blue icon] **Expert Witnesses, Daubert Standard**

In the context of determining the admissibility of expert testimony, even where a witness is an expert in the relevant field, the evidentiary reliability demanded by Daubert is not present when his or her opinion is speculative or rests on an unsound basis.

Civil Procedure > Judicial Officers > Judges > General Overview

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

#### **HN27** [blue icon] **Judicial Officers, Judges**

Daubert requires that trial judges must ensure that any and all expert testimony is not only relevant, but reliable. To that end, a judge must undertake a preliminary assessment of whether the reasoning or methodology underlying the testimony is scientifically valid and whether that reasoning or methodology properly can be applied to the facts at issue. The judge must look behind the expert's ultimate conclusion and analyze the adequacy of its foundation. Expert opinion that is speculative is inadmissible.

Evidence > ... > Testimony > Expert Witnesses > General Overview

#### **HN28** [blue icon] **Testimony, Expert Witnesses**

Courts should be particularly wary of unfounded expert opinion when causation is the issue.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > ... > Testimony > Expert Witnesses > General Overview

Evidence > Admissibility > Expert Witnesses

Evidence > Admissibility > Expert Witnesses > Helpfulness

#### **HN29** [blue icon] **Expert Witnesses, Daubert Standard**

To be admissible, expert testimony must be not only reliable, but relevant. Testimony is relevant if it assists the trier of fact in understanding the evidence or in determining a fact at issue. An expert who supplies nothing but a bottom line supplies nothing of value to the judicial process.

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Civil Procedure > Discovery & Disclosure > Disclosure > Mandatory Disclosures

Civil Procedure > Discovery & Disclosure > Disclosure > General Overview

### **HN30** [ ] Disclosure, Mandatory Disclosures

*Fed. R. Civ. P. 26(a)(2)(B)*, requires that an expert report must disclose a complete statement of all opinions to be expressed and the basis and reasons therefor.

Civil Procedure > Discovery & Disclosure > Disclosure > Mandatory Disclosures

Civil Procedure > Discovery & Disclosure > Disclosure > General Overview

### **HN31** [ ] Disclosure, Mandatory Disclosures

See *Fed. R. Civ. P. 26(a)(2)(B)*.

Evidence > Admissibility > Expert Witnesses

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN32** [ ] Admissibility, Expert Witnesses

In the context of determining the admissibility of expert testimony, expertise is a rational process, and a rational process implies express reasons for judgment. An expert's opinion full of assertion but empty of reasons has no value and is devoid of persuasiveness and legal significance.

Evidence > ... > Testimony > Expert Witnesses > General Overview

### **HN33** [ ] Testimony, Expert Witnesses

An expert witness must demonstrate in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field.

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > Discovery & Disclosure > Disclosure > General Overview

Civil Procedure > Discovery & Disclosure > Disclosure > Mandatory Disclosures

### **HN34** [ ] Discovery, Methods of Discovery

*Fed. R. Civ. P. 26(a)(2)(B)* requires the disclosure of any other cases in which the witness has testified as an expert at trial or by deposition within the preceding four years. The report must be detailed and complete. Thus, the cases have generally defined the "listing of cases" requirement to include the name of the court, the name of the parties, the case number, and whether the testimony was given at deposition or trial.

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**Judges:** Magistrate Judge Jeffrey Cole.

**Opinion by:** Jeffrey Cole

## **Opinion**

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### **[\*797] MEMORANDUM OPINION AND ORDER**

#### **INTRODUCTION**

On June 9, 2005, I denied the Defendants' Motion to Bar the testimony of **[\*798]** Loeffel Steel Products' expert liability witness, Mr. Rudolph Toczył. See [Loeffel Steel Products v. Delta Brands, 372 F. Supp. 2d 1104, 2005 WL 1388076 \(N.D.Ill. 2005\)](#). The history of the parties' dispute is discussed in that opinion and need not be repeated. I address here the plaintiff's motion to bar the testimony of the defendants' damages expert, Mr. Robert Dohmeyer and Dohmeyer Valuation Corporation ("DVC").

Like Gaul, Mr. Dohmeyer's expert opinion and report may be divided into three parts. The first is a "preliminary critique" **[\*\*3]** of the report of Loeffel's damage expert, William Wiersema, contained in a letter dated February 27, 2004. The second and third components are contained in a separate, 41 (unnumbered) page document captioned, "Analysis of Economic Loss." ("the Analysis"). It, too, was dated February 27th.

The Analysis was a compendium of spreadsheets, reflecting 1) Mr. Dohmeyer's calculations of the \$ 248,000 economic loss he concluded was suffered by Loeffel, and 2) charts and graphs reflecting financial data for the period 1999 - 2002 for Loeffel and for eight, large, publicly traded companies, which were supposed to depict the economic conditions in the steel industry at that time.

Loeffel's present motion challenges Mr. Dohmeyer's qualifications to offer expert opinion on economic loss and his methodology and definition of economic loss, which Loeffel argues did not comply with the four, non-definitive

factors that *Daubert* said a court could use in determining testimonial reliability. *Daubert v. Merrell Dow Pharmaceuticals, Inc.*, 509 U.S. 579, 125 L. Ed. 2d 469, 113 S. Ct. 2786 (1993). Loeffel also contends that Mr. Dohmeyer should not be allowed to testify because of his unquestioning reliance on the defendants' [\*\*4] theory that the deficiencies in the Line could be cured by the addition of extra workers and additional shifts.<sup>1</sup> Lastly, the motion contends that Mr. Dohmeyer should not be allowed to testify about Mr. Wiersema's damage analysis, because his critique of February 27, 2004 did not comply with Rule 26(a)(2)(B).

I

## FACTUAL BACKGROUND

Prior to preparing his February 27th "preliminary critique" and his Analysis, Mr. Dohmeyer (and/or his two assistants at DVC) reviewed Loeffel's financial statements for the fiscal years ending November 30, 1999 through November 30, 2002, reviewed the deposition testimony of Loeffel's president, Maurice Loeffel [\*\*5] and that of Mr. Wiersema, compiled financial data from annual 10k reports and Standard & Poor's Stock Reports on eight large publicly traded companies in what Mr. Dohmeyer categorized as the "(steel) metals industry," and interviewed the defendants' employees.<sup>2</sup> As we shall see, these interviews would play a pivotal role in Mr. Dohmeyer's analysis of Loeffel's "economic loss."

The Analysis concluded that Loeffel had damages prior to August of 2003 of \$ 280,000, damages thereafter of \$ 142,339, and lost profits of \$ 50,000. The Analysis [\*799] itself has no textual elaboration or explanation, and the reader is left to divine its meaning from the headings, captions, and the figures on its charts and spreadsheets. A meaningful understanding can only be gained by reference to Mr. Dohmeyer's deposition testimony. The Analysis's damage spreadsheets differentiated between pre- [\*\*6] and post-August 2003 because, as Mr. Dohmeyer later explained, he assumed - based upon what he had been told by the defendants' employees - that the trouble with the magnets in the stacker had been alleviated or nearly so. (Dohmeyer Dep., at 39, 42-43). The Analysis then discounted the figures by \$ 225,000, which represented the amount of the purchase price held back by Loeffel.

The Analysis's second and core assumption was provided by defendants' employees, who assured Mr. Dohmeyer that the various deficiencies in the Line could be offset by adding two additional workers to production runs and increasing the number of shifts. Using this methodology, and based on his conclusions about "industry" conditions between 1999 and 2002 - as reflected by the financial data of eight publicly traded companies - Mr. Dohmeyer concluded that Loeffel's lost profits could not exceed \$ 50,000.

The Analysis begins with an estimate of the hourly wages of the two additional workers, based upon the rates in Texas, where the defendants were located. Adjusting those rates - \$ 13.00 for an operator and \$ 7.50 for a helper - to what would be comparable in the Chicago area, Mr. Dohmeyer arrived at a total [\*\*7] of \$ 26.65 for both positions. Factoring in benefits left the combined rate at \$ 39.98, which Mr. Dohmeyer arbitrarily increased to \$ 50.00 per hour. Over the 702 days Loeffel ran the machine prior to August of 2003, based upon one eight-hour shift per day, Mr. Dohmeyer arrived at a maximum "economic loss" figure of \$ 280,000, the amount that would compensate the two additional workers for the relevant period. (Analysis at 2; Dohmeyer Deposition at 26, 30, 33).

Mr. Dohmeyer then calculated future damages over a ten-year life of the Line, beginning in August of 2003. He began with the assumption, again based on what he was told by the defendants' employees, that Loeffel could process ten coils of steel on the Line every eight- hour shift. The "economic loss" figure was based on the defendants' assessment of the processing time. (Dohmeyer Deposition at 63-64). For this period, he was told by the

<sup>1</sup> Literally every facet of this labor-added theory and every bit of information regarding alleviation of the Line's problems - as well as information regarding prior claimed fixes - came from the defendants' employees. (Dohmeyer Dep., at 26-39, 42-45, 55-57, 61-63, 109). The Line is the Rotary Shear Multi-blanking machine that Loeffel purchased from Delta Brands.

<sup>2</sup> Although its title suggested that a more comprehensive and edifying analysis was to come, the "preliminary critique" underwent not a single change.

defendants that an additional five minutes of labor per coil would alleviate any problems remaining with the Line during that period.<sup>3</sup> Once again this was based on the twin assumptions that the problems with the stacker's magnets had been responsible for the vast majority of the deficiencies, [\*\*8] and that these problems had been rectified by August, 2003. (Dohmeyer Dep., at 39, 42-43).

The five-minute estimate was a product of the defendants' assurances that the remaining problem - leveling the steel - could be corrected manually in 30 seconds to one minute per coil, which Mr. Dohmeyer rounded up to five minutes to be "conservative." (Dohmeyer Deposition at 62-63). This amounted to fifty minutes of labor per shift which he rounded up to an hour. This figure was then multiplied by 468 shifts per year over the ten-year period. Discounting the resulting sum to account for present value, cost of capital, and inflation, Mr. Dohmeyer arrived at \$ 142,339 for future damages. (Analysis at unnumbered p. 3).

The lost profits calculations are a bit more difficult to discern, as the Analysis [\*800] simply says under the captioned "Lost Business (Max):"

Lost Business (Economic Profits - August 2003 > .10 Gauge \$ 50,000 60" Inch Line Sold in February 2003

(Analysis [\*\*9] at unnumbered page 5). The footnote after the \$ 50,000 figure says "Expected Value of Economic Profits - Max - See Industry Analysis." However, referring to the 1 1/2 page portion of the Analysis captioned "Industry Analysis" is a hopelessly uninformative exercise. All this part of the Analysis did was to summarize some unilluminating generalizations about the steel industry that Mr. Dohmeyer's DVC assistant had gotten off the internet.

At his deposition, Mr. Dohmeyer explained that the \$ 50,000 figure was drawn from his analysis for processing "high gauge" steel or "toll processing." (Dohmeyer Dep., at 104, 106). The problems processing "high gauge" steel or "toll processing" could not be corrected by additional labor - that business was lost. (Dohmeyer Dep., at 70-71, 102-104). Although it is unclear from the Analysis, this was apparently a new business that Loeffel hoped to get into by virtue of the Line, but could not due to the Line's shortcomings. (Dohmeyer Dep. at 106). In reaching the \$ 50,000 figure, Mr. Dohmeyer also considered his review of Loeffel's performance between 1999 and 2002, as well as the performance of the eight publicly traded companies selected as the sampling [\*\*10] against which Loeffel's prospects in that period were to be measured. (Analysis at unnumbered pp. 6-11; Dohmeyer Dep. at 116-128).

## II.

### THE ANALYTICAL FRAMEWORK FOR DETERMINING ADMISSIBILITY

[Loeffel Steel Products v. Delta Brands, 372 F. Supp. 2d 1104, 2005 WL 1388076 \(N.D.Ill. 2005\)](#) discussed the analytical backdrop of motions to bar the testimony of an expert, and that discussion is incorporated by reference. To it, the following should be added. [HN1](#) The Supreme Court in *Daubert* stressed the trial judge's obligation to act as a gatekeeper to ensure that expert testimony is reliable. The insistence on reliability helps to ensure the integrity of the judicial process. [Mid-State Fertilizer Co. v. Exchange Nat'l Bank of Chicago, 877 F.2d 1333, 1340 \(7th Cir. 1989\)](#). That goal is of such obvious and transcendent importance that judges can act *sua sponte* to prohibit testimony that does not pass muster under [Daubert, O'Conner v. Commonwealth Edison Co., 13 F.3d 1090, 1094 \(7th Cir. 1994\)](#).

[HN2](#) While *Daubert* reaffirmed the value of the adversary system generally and the capability of juries to understand scientific evidence and weigh the credibility [\*\*11] of the competing experts, with their often absolutist and clashing conclusions, it also made clear that in those cases in which the proponent of an expert could not demonstrate the reliability of the methodology employed by the expert, the court was required to disallow the testimony. The opportunity for vigorous cross examination and the presentation of contrary evidence - the traditional

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<sup>3</sup> Each coil of steel weighs as much as 60,000 lbs.

and appropriate means of attacking shaky but admissible evidence, [Daubert, 509 U.S. at 596](#) - is not a basis for allowing otherwise inadmissible testimony to be admitted.

[Kumho Tire Co. Ltd. v. Carmichael, 526 U.S. 137, 143 L. Ed. 2d 238, 119 S. Ct. 1167 \(1999\)](#) reaffirmed the teachings of *Daubert*, but emphasized that [HN3](#) the *Daubert* factors were not applicable, *semper ubique et ab omnibus*. They need only be considered when doing so will aid in the determination of the testimony's [\*801] reliability. [Id. at 142, 150](#). The inquiry is always, and of necessity, highly fact- specific, and no one factor, even when applicable, is outcome-determinative.

[HN4](#) *Daubert* also cautioned judges assessing a proffer of expert testimony under [Rule 702](#) to be mindful of other applicable rules, such as [\*\*12] [Rule 703](#), which permits an expert to base an opinion on information that need not itself be admissible, so long as it is the kind of information relied on by other experts in the field. [509 U.S. at 595](#).

## A

### Evaluation of Reliability of Mr. Dohmeyer's Testimony

I

#### Qualifications of Mr. Dohmeyer and his Firm

Mr. Dohmeyer has a bachelor's degree in finance and is an accredited senior appraiser with the American Society of Appraisers ("ASA"). That accreditation was, according to Mr. Dohmeyer, the equivalent of a CPA for valuation and financial analysts. (Dohmeyer Dep., at 13).<sup>4</sup> He has lectured on the valuation of privately held businesses, and he has given expert testimony in 32 cases involving "economic loss." (See Analysis, Qualifications of Principal Appraisers). At his deposition, Mr. Dohmeyer testified that DVC was primarily in the business of appraising privately held businesses and analyzing economic loss, which, Mr. Dohmeyer conceded could include the loss of profits due to poorly manufactured products. Mr. Dohmeyer estimated that perhaps one in ten of the economic loss cases he had handled involved equipment that failed to perform as [\*\*13] the seller had promised. (Dohmeyer Dep., at 8-12).

Mr. Dohmeyer was assisted in his analysis by Kevin Morrison and Sontwa Sinkala. Mr. Morrison has a bachelor's degree in business administration, accounting, and finance. Sontwa Sinkala has a master's degree in business administration, specializing in corporate finance, and a doctorate in economics and geography. Nonetheless, Loeffel contends that all three are unqualified to testify in this case since none is a certified public accountant, none has any expertise in the steel industry, none has experience in cases dealing with lost profits due to faulty machinery, and the USPAP guidelines were not followed in preparing the Analysis of Economic Loss. (Pl.Mem., at 6-9).

[\*\*14] The argument that only a CPA with expertise in the steel industry -- preferably, with regard to multi-blanking machines and a prior history of expert testimony in a case involving lost profits due to a poorly performing piece of machinery - is inconsistent with the liberal approach to expert witness qualification taken by [Rule 702](#). See [Holbrook v. Lykes Brothers Steam Ship, 80 F.3d 777, 782 \(3rd Cir. 1996\); Carroll v. Otis Elevator Co., 896 F.2d 210, 212 \(7th Cir. 1990\)](#). [HN5](#) Overemphasis on qualifications over testimonial reliability reflects a pre-*Daubert* sensibility. [Rushing v. Kansas City Southern Ry. Co., 185 F.3d 496, 507 \(5th Cir. 1999\)](#).

Mr. Dohmeyer's and his colleagues' educational background and experience qualify Mr. Dohmeyer and his colleagues to testify about, at least, certain of the matters presented in this case. Characterizing them as

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<sup>4</sup> The requirements for accreditation are completion of five years' experience in business appraisals, passing three technical exams, an ethics and the Uniform Standards of Professional Appraisal Practice ("USPAP") exam, and the submission of two appraisals for evaluation. (Dohmeyer Dep., at 13).

"appraisers" does not advance [\*802] analysis. Even appraisers can have sufficient expertise to rebut the testimony of certified public accountants in appropriate cases. See, e.g., *Frymire-Brinati v. KPMG Peat Marwick, 2 F.3d 183, 186-87 (7th Cir. 1993)*(district court erred [\*\*15] in precluding a real estate appraiser to rebut a CPA's opinion about real estate values in financial statement).

**HN6**[<sup>1</sup>] No case of which we are aware remotely suggests, let alone holds, that only a certified public accountant has the necessary expertise to testify about economic loss. In fact, being a certified public accountant does not ensure admissibility of testimony. See e.g., *Frymire-Brinati, 2 F.3d at 186-87* (under *Daubert*, expert testimony of certified public accountant should not have been admitted); *SEC v. Lipson*, 46 F. Supp. 2d 758, 762 (N.D.Ill. 1999) (applying *Daubert* to bar testimony of certified public accountant on reliability grounds); *De Jager Construction, Inc. v. Schleininger*, 938 F.Supp. 446, 449-455 (W.D.Mich. 1996) (excluding certified public accountant expert opinion testimony that blurred the distinction between substantive liability and a calculation of damages); *Lithuanian Commerce Corp Ltd. v. Sara Lee Hosiery*, 179 F.R.D. 450 (D.N.J. 1998) (excluding certified public accountant's damage calculations because they relied on speculative and unsupported assumptions).

In *Tuf Racing Products, Inc. v. American Suzuki Motor Corp.*, 223 F.3d 585 (7th Cir. 2000), [\*\*16] the court rejected as unsound the notion that *Daubert* required particular credentials for an expert witness, finding that **HN7**[<sup>1</sup>] "anyone with relevant expertise enabling him to offer responsible opinion testimony helpful to judge or jury may qualify as an expert witness." *Id. at 591*. Thus, Mr. Dohmeyer's admitted lack of specific experience with multi-blanking machines is not a disqualifying factor. See *Loeffel Steel Products v. Delta Brands*, 372 F. Supp. 2d 1104, 2005 WL 1388076 at \*7.<sup>5</sup>

[\*\*17] We turn then to the second prong of the inquiry, namely the reliability of the method that Mr. Dohmeyer and his associates employed to arrive at their damage figures.

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### The Methodology Underlying The Analysis of Economic Loss

There are two aspects to Mr. Dohmeyer's methodology that trouble Loeffel. The first is Mr. Dohmeyer's use of a definition of "economic loss" that he devised, and the second is his reliance on the defendants' employees for the theory and supporting information that any deficiencies in the Line can be rectified by additional labor and extra shifts.

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### Mr. Dohmeyer's Definition Of Economic Loss

The Analysis defined "economic loss" as: "the dollar sum, exclusive of prejudgment interest and professional fees, required as payment in full necessary to make the damaged party equal on an economic basis." The definition, at least semantically, seems straightforward and consistent with the general Uniform Commercial Code ("UCC") and contract damage theory that the fundamental purpose of any damage [\*803] award is to place the plaintiff in the

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<sup>5</sup> See also *Maiz v. Virani*, 253 F.3d 641 (11th Cir. 2001) (allowing economist with no real estate development experience to testify about expected returns from real estate investment); *Quinton v. Farmland Industries*, 928 F.2d 335, 336 (10th Cir. 1991) (veterinarian need not be a specialist in toxicology to testify on toxic effect of a substance on cows); *Ashland Oil, Inc. v. Delta Oil Prods. Corp.*, 685 F.2d 175, 178 (7th Cir. 1982), cert. denied, 460 U.S. 1081, 76 L. Ed. 2d 343, 103 S. Ct. 1769 (1983) (trial court properly relied on testimony of expert in chemistry despite lack of expertise in polyurethane chemistry).

position it would have been in had there been no breach, but not to place it in a better position or provide [\*\*18] it with a windfall. [Platinum Technology, Inc. v. Federal Insurance Co., 282 F.3d 927, 932 \(7th Cir. 2002\)](#).<sup>6</sup>

This apparent consonance was delusive, however, for Mr. Dohmeyer boasted in his deposition that "many years ago" he and his boss devised the definition: "this is *our* definition of what we *believe* the question is, what answer we are giving." (Dohmeyer Dep., at 19) (Emphasis supplied). If this definition of economic loss were faithful to basic damage theory, there would have been no need for Mr. Dohmeyer to have devised and employed his own definition. Cf. [Schenck v. United States, 249 U.S. 47, 48, 39 S. Ct. 247, 63 L. Ed. 470, 17 Ohio L. Rep. 26, 17 Ohio L. Rep. 149 \(1919\)](#)(Holmes, [\*\*19] J.)("Of course the document would not have been sent unless it had been intended to have some effect. . . ."); [United States v. Ladish Malting Co., 135 F.3d 484, 490 \(7th Cir. 1998\)](#)("The prosecutor must have thought that the instruction mattered; why else so vigorously oppose Ladish's request for an actual-knowledge instruction").

Mr. Dohmeyer's admissions about the origin and uniqueness of his definition - he conceded the definition was not to be found anywhere else (Dohmeyer Dep., at 18-19) - would seem to trigger the principle that the opinion of an expert need not be accepted when based on nothing more than personal opinion or belief instead of an understandable scientific basis. [Turpin v. Merrell Dow Pharmaceuticals, Inc., 959 F.2d 1349, 1360 \(6th Cir.\), cert. denied 506 U.S. 826, 121 L. Ed. 2d 47, 113 S. Ct. 84 \(1992\); Thomas v. FAG Bearings Corp., 846 F.Supp. 1382, 1393 \(W.D.Mo. 1994\)](#). But this is only the beginning.

Mr. Dohmeyer's definition was the basis for a damage theory and calculation that is impermissible as a matter of law. It is not merely that the definition was not peer reviewed, not tested, and not generally accepted, as Loeffel [\*\*20] correctly argues.<sup>7</sup> In addition, Mr. Dohmeyer's theory and methodology led him to exclude as a component of "economic loss" any amount attributable to the diminished value of the Line, itself.

[\*\*21] [HN9](#) Both contract law and the UCC provide the appropriate remedy for "economic loss" occasioned by diminished commercial expectations, not coupled with injury to person or property. See [In re Chicago Flood Litigation, 176 Ill.2d 179, 200, 680 N.E.2d 265, 275, 223 Ill. Dec. 532 \(1997\); Mars, Inc. v. Heritage Builders of Effingham, Inc., 327 Ill.App.3d 346, 351, 763 N.E.2d 428, 434, 261 Ill. Dec. 458 \(4th Dist. 2002\).](#)

[\*804] "Generally speaking, a defective product can cause three types of injury: personal injury, property damage, and economic loss." [Trans States Airlines v. Pratt & Whitney Can., 177 Ill.2d 21, 27, 682 N.E.2d 45, 48, 224 Ill. Dec. 484 \(1997\)](#). In [Moorman Mfg. Co. v. National Tank Co., 91 Ill.2d 69, 82, 435 N.E.2d 443, 449, 61 Ill. Dec. 746 \(1982\)](#), the Illinois Supreme Court held that "economic loss"

"has been defined as 'damages for inadequate value, costs of repair and replacement of the defective product, or consequent loss of profits - without any claim of personal injury or damage to other property' (Note, Economic Loss in Products Liability Jurisprudence, 66 Colum. L.Rev. 917, 918 (1966)(economic loss)) as well as 'the diminution in the value of the [\*\*22] product because it is inferior in quality and does not work for the general purposes for which it was manufactured and sold.'"

<sup>6</sup> Accord [810 ILCS 5/2-106\(1\)](#)(UCC remedies "shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed."); [Dynamic Recycling Services, Inc. v. Shred Pax Corp., 210 Ill.App.3d 602, 615, 569 N.E.2d 570, 578, 155 Ill. Dec. 389 \(1st Dist. 1991\)](#).

<sup>7</sup> [HN8](#) While *Daubert* applies to valuation testimony, whether offered by people like Mr. Dohmeyer, certified public accountants, or economists, [Frymire-Brinati v. KPMG Peat Marwick, 2 F.3d 183 \(7th Cir. 1993\)](#), the *Daubert* factors are not to be rigidly applied in this or any other context. In some context, they may not be applicable at all or may have diminished utility as measures of reliability. [Loeffel Steel Products v. Delta Brands, 372 F. Supp. 2d 1104, 2005 WL 1388076 at \\*6](#). Some courts have held they "do not conform easily to an analysis of economic theory." [Bailey v. Allgas, Inc., 148 F.Supp.2d 1222, 1235 \(N.D.Ala. 2000\)](#). In determining the admissibility of expert testimony with respect to future lost profits, a trial judge has considerable leeway in determining the testimony's reliability. [ID Security Systems Canada, Inc. v. Checkpoint Systems, Inc., 249 F.Supp.2d 622, 690 \(E.D.Pa. 2003\)](#).

91 Ill.2d at 82, 435 N.E.2d at 449 (Emphasis supplied)(Parentheses in original).

In their Response to Loeffel's motion, the defendants have "changed positions as nimbly as if dancing a quadrille." Orloff v. Willoughby, 345 U.S. 83, 87, 97 L. Ed. 842, 73 S. Ct. 534 (1953), for they now insist that Mr. Dohmeyer's definition is "entirely consistent" with traditional breach of contract damages theory, as expressed in *Moorman*. However, the Response ignores Mr. Dohmeyer's testimony in which he said that he created the definition years ago, and that it was to be found nowhere else. Nor does it attempt to explain why he would have insisted on using such a definition if it was consistent with the traditional and legal definition. (Response at 10).

In quoting from *Moorman*, the Response placed a period after the word "property," and ended the quote, thus conveying to the reader the impression that there was nothing further in the sentence. Omitted was the reference to the Columbia Law Review article and this critical phrase:

". . . as well [\*\*23] as 'the diminution in the value of the product because it is inferior in quality and does not work for the general purposes for which it was manufactured and sold.'"

HN10 [↑] The UCC provides that "the measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount." 810 ILCS 5/2-714(2). In addition, a party may also recover incidental and consequential damages, 810 ILCS 5/2-715, including lost profits. See Arcor, Inc. v. Textron, Inc., 960 F.2d 710, 713-14 (7th Cir. 1992) (buyer of a machine that failed to live up to its warranty was entitled to not only the difference between the value of the machine as warranted and its actual value, but lost profits as well); Mercer v. Long Mfg., N.C., Inc., 665 F.2d 61, 69 (5th Cir. 1982) (in case involving faulty combine, economic loss consists of difference in value between combine as warranted and as received and any lost profits on crops resulting [\*\*24] from inability to use combine for harvesting); Cognitest Corp. v. Riverside Publ. Co., 107 F.3d 493, 496 (7th Cir. 1997).<sup>8</sup>

[\*805] The measure of damages under Loeffel's fraud claim (Count V) is the same. HN11 [↑] The victim of a fraudulent misrepresentation is entitled to recover as damages those losses caused by the misrepresentation, "including (a) the difference between the value of what he has received in the transaction, and its purchase price or other value given for it. . ." Restatement (2d) Torts § 549 [\*\*25] (1977). Accord DiRose v. PK Management Corp., 691 F.2d 628, 631 (2nd Cir. 1982); FDIC v. Palermo, 815 F.2d 1329, 1341 (10th Cir. 1987); Four S Alliance Inc. v. American National Bank, 104 Ill. App.3d 636, 432 N.E.2d 1213, 60 Ill. Dec. 314 (1st Dist. 1982); Dobbs, Remedies, § 9.2 at 594-95 (1973) ("If a plaintiff has been induced to buy a house because of an intentional false representation that it is free from termites, the plaintiff is entitled to recover the difference between the value of the house as it actually exists and the value it would have had if it had not had termites. This rule puts him in the same financial position as if the fraudulent representations had been true.").

An examination of Mr. Dohmeyer's deposition testimony reveals the likely reason for the omission from the *Moorman* quotation. He testified that his assessment of economic loss necessarily omitted any consideration of the difference between the value of the Line as warranted and its diminished value resulting from the Line's flaws. He attempted to illustrate the point with the following hypotheticals.

A: Well, if you paid - if you bargain to buy a machine for [\*\*26] \$ 10 and you allege once you got it you only paid nine because you hold back a dollar until it works right, but you say, hey, this machine doesn't work right; in fact, the damages on the machine the way it doesn't work are \$ 2.00. So pay me the two. Well, he's going to go, I'm not going to pay you the two, I'll pay you one, because you already owe me one.

<sup>8</sup> In a lengthy "Declaration" belatedly submitted by the defendants in response to the present motion, Mr. Dohmeyer insisted that there is no authoritative text regarding the calculations of damages due to a machine that operates at a rate below its specifications. (*Defendant's Response to Plaintiff's Motion to Bar*, Ex. A, P19). The controlling legal definitions of economic loss and the measure of damages available under Illinois law - which the defendants concede controls this case - would have been a starting point.

387 F. Supp. 2d 794, \*805L<sup>2005 U.S. Dist. LEXIS 15718, \*\*26</sup>

Q: Right. But couldn't I also take the position in your analogy that, hey, I paid you a million two hundred fifty thousand in the purchase price and a million five and the line I got isn't worth \$ 100,000.

A: No, because you'd be double-counting . . . you can only get your damages.

(Dohmeyer Dep., at 133; see also *id.* at 134).

Mr. Dohmeyer's second hypothetical is even more convoluted. He posited a machine sold for four dollars that was warranted to print one dollar every year for five years. (Dohmeyer Dep., at 135). Then he continued:

A: All right. So it doesn't print-it doesn't even print the dollars for you. Okay? So you say, I want my \$ 5.00, because the machine is defective, it didn't print money like you said it does. You want the machine back, too. That doesn't make any sense.

Q: I - I - **[\*\*27]** what I'm saying is, I'm not disagreeing with your contention. There's no way I can say, hey, I have lost profits, and I can't say, I needed the machine to create the profits I lost. I understand this. What I'm saying is, you're - you're assuming in your analogy, that because we didn't pay the other two hundred and fifty grand, the machine must have been worth a a[sic] million two hundred and fifty, and that's the part I'm disagreeing with.

A: Absolutely, it's worth that because your damages get you whole to make it worth that.

By its selective misquotation, the Response allowed the defendants to argue **[\*806]** that Mr. Dohmeyer's definition of economic loss was "consistent" with basic damage theory, without simultaneously revealing that it wasn't and without thereby revealing the unreliability of his methodology and his deposition testimony.

In his belatedly filed Declaration, Mr. Dohmeyer claimed what he had never claimed at his deposition, namely that his analysis of economic loss relied on a "benefit of the bargain theory," which he defined this way: "But for' the defendant's allegedly defective machine, Loeffel would have had a faster machine, (one capable of producing at the **[\*\*28]** rates provided in the contract specifications." (Parenthesis in original). Mr. Dohmeyer's newly claimed allegiance to the benefit of the bargain rule, is belied by and incompatible with his conclusion that diminution in value of a faulty piece of equipment and lost profits are mutually exclusive. [\*\*HN12\*\*](#)<sup>1</sup> The benefit of the bargain rule provides that the measure of damages is the difference between the actual value of what plaintiff received and its value had the representations been true. See *Gerill Corp. v. Jack L. Hargrove Builders, Inc.*, 128 Ill.2d 179, 538 N.E.2d 530, 537-38, 131 Ill. Dec. 155, cert. denied 493 U.S. 894, 107 L. Ed. 2d 193, 110 S. Ct. 243 (1989); *Out of Pocket or Benefit of the Bargain As Proper Rule of Damages for Fraudulent Representations Inducing Contract for the Transfer of Property*, 13 A.L.R.3d 875 (1967)(collecting cases).

[\*\*HN13\*\*](#)<sup>1</sup> Expert opinions that are contrary to law are inadmissible. *Langehennig v. Sofamor, Inc.*, 1999 U.S. Dist. LEXIS 19120, 1999 WL 1129683 at n.6 (D.Kan. 1999); *Bailey v. Allgas, Inc.*, 148 F.Supp.2d 1222, 1245-46 (N.D.Ala. 2000). They cannot be said to be scientific, to be reliable, or to be helpful to the trier of fact. Indeed, "it is not an 'expert' **[\*\*29]** opinion, but rather a personal opinion about what [damages Mr. Dohmeyer] believes should apply" in this case. *In re Diet Drugs Products Liability Litigation*, 2001 U.S. Dist. LEXIS 1174, 2001 WL 454586 at \*18 (E.D.Pa. 2001).

Whatever the motivation for the Response's misquotation or *Moorman*, it is deeply troubling. *Loeffel Steel Products*, 372 F. Supp. 2d 1104, 2005 WL 1388076 at \*11 [\*\*HN14\*\*](#)<sup>1</sup> "There is more in membership in the Bar than a license to sign a brief or intone a prosy argument." Cardozo, Law and Literature, 145-46 (1931). Justice is not a game, and zealous advocacy does not entitle a lawyer to "hoodwink a judge [or an opponent] who is not otherwise." *United States v. Paglia*, 190 F.2d 445, 448 (2nd Cir. 1951)(L. Hand, J.).<sup>9</sup>

<sup>9</sup> A similar kind of manipulation is found in the defendants' rendition of *Frymire-Brinati v. KPMG Peat Marwick*, 2 F.3d 183 (7th Cir. 1993). The discussion in the Response brief makes it appear as though the plaintiff's expert, a real estate appraiser, was improperly forbidden to testify that the plaintiff's expert, a certified public accountant, "bungled" his "valuation of damages." (Response at 16). "Similarly," the defendants say, they proffer "Mr. Dohmeyer, an economist, as its expert." *Id.* Mr. Dohmeyer isn't an economist, and the two cases are not similar. In *Brinati*, the chairman of the real estate committee of the American

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### The Reliability Of Mr. Dohmeyer's "Labor-Added" Methodology

Mr. Dohmeyer's damage model and calculation of economic loss suffer from the further flaw that they violate of Rule 703 of the Federal Rules of Evidence.<sup>10</sup> [\*807]

[\*\*31] Mr. Dohmeyer's calculation of economic loss is based on the assumption that the addition of extra labor and shifts would allow the Line to yield the same productivity as it would have running at faster speeds with fewer shifts. The theory and the precise number of traditional workers and shifts needed came from the defendants' employees, on whom Mr. Dohmeyer uncritically relied. It is undisputed that neither Mr. Dohmeyer nor his assistants at DVC had any expertise in blanking machines and were incapable of assessing the validity of the information provided by the defendants. (Dohmeyer deposition at 26, 33-38, 89). Cf. Bailey v. Allgas, 148 F.Supp.2d 1222, 1240 (N.D.Ala. 2000)(unquestioning reliance on opinions expressed by plaintiff's counsel not proper).

Proceeding from this "unquestioning reliance," Gentieu v. Tony Stone Images/Chicago, Inc., 214 F. Supp. 2d 849, 853 (N.D.Ill. 2002)(Shadur, J.), Mr. Dohmeyer calculated the amount it would cost Loeffel to pay the additional workers in order to produce as much finished steel as would have been produced had the Line operated properly. Mr. Dohmeyer's difficulty in explaining how the additional workers [\*\*32] would cure the situation demonstrates dramatically that he brought no expertise to bear on the underlying assumptions on which his economic loss theory was based:

Sure, just by having, you know, the kinds of things, you know - you have to, I guess, re - recalibrate the machine every time you put a new roll on it where it should have been automatic, you can have a guy standing there, you know, doing that kind of thing. You know, once again, I don't know the technical parts of it, and I understood them a lot better when I did the interview and when I prepared for this deposition last time, but I haven't gone back to re-talk to them about those specifics again for today's deposition . . . . (Dohmeyer Dep. at 37).

Yet, HN16[ Rule 703's relaxation of the usual requirement of firsthand knowledge - a rule which represents a pervasive manifestation of the common law's insistence upon the most reliable sources of information - was premised on an assumption that the expert's opinion will have a reliable basis in the knowledge and experience of his discipline. Daubert, 509 U.S. at 592. When pressed, Mr. Dohmeyer could not even say whether the additional labor would solve the [\*\*33] alleged problems and raise the level of production. For that information, one would, he said, have to check with Messrs. Barron, King and DaClue. (*Id.* at 37-38, 45, 89). Referring to his damage figure, he said:

All it really assumes is with the addition of this expense. And it would probably be labor, you know. . . It says with this much money thrown at the problem, probably - probably, in terms of labor, you can solve the production problems that are alleged. (Dohmeyer Dep. at 44-45).

Institute of Certified Public Accountants, *not* the appraiser, testified that the plaintiff's CPA had "bungled" by using historical rather than projected future income in his cash flow analysis. 2 F.3d at 187. It was in an effort to "move from theory to concrete valuation" that the appraiser was to testify thereafter about the accuracy of property values in the financial statements.

<sup>10</sup> Rule 703 provides:

HN15[ Bases of Opinion Testimony by Experts

The facts or data in the particular case upon which an expert bases an opinion or inference may be those perceived by or made known to the expert at or before the hearing. If of a type reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject, the facts or data need not be admissible in evidence in order for the opinion or inference to be admitted. Facts or data that are otherwise inadmissible shall not be disclosed to the jury by the proponent of the opinion or inference unless the court determines that their probative value in assisting the jury to evaluate the expert's opinion substantially outweighs their prejudicial effect.

[\*808] It is no answer to say that since [Rule 703](#) allows an expert to base an opinion on inadmissible evidence, Mr. Dohmeyer must be allowed to testify, even though the basis of the information on which he relied came from the defendants. First, the defendants have made no effort to carry their burden of proving by a preponderance of the evidence that the kind of information given to Mr. Dohmeyer is the kind "reasonably relied upon by experts in the particular field in forming opinions or inferences upon the subject. . . ." The argument is thus forfeited. [United States v. Baretz, 411 F.3d 867 \(7th Cir. 2005\)](#).

Second, and more importantly, [HN17](#) while [Rule 703](#) was intended to liberalize [\*34] the rules relating to expert testimony, it was not intended to abolish the hearsay rule and to allow a witness, under the guise of giving expert testimony, to in effect become the mouthpiece of the witnesses on whose statements or opinions the expert purports to base his opinion. See, e.g., [Dura Automotive Systems of Indiana, Inc. v. CTS Corp., 285 F.3d 609, 613 \(7th Cir. 2002\)](#); [TK-7 Corp. v. The Estate of Barbouti, 993 F.2d 722, 731-34 \(10th Cir. 1993\)](#); [In re James Wilson Assoc., 965 F.2d 160, 173 \(7th Cir. 1992\)](#).

[HN18](#) Under [Rule 703](#), an expert may rely on hearsay in formulating his opinion - provided the requirements of [Rule 702](#) are met - but the evidence is not admissible for the truth of the matters asserted. [United States v. Gonzales, 307 F.3d 906, 910 \(9th Cir. 2002\)](#); [TK-7 Corp. v. Estate of Barbouti, 993 F.2d 722, 734 \(10th Cir. 1993\)](#)("the hearsay is admitted for the limited purpose of informing the jury of the basis of the expert's opinion and not for proving the truth of the matter asserted."). Cf. [Gregory v. Oliver, 2002 U.S. Dist. LEXIS 24730, 2002 WL 31972165 at \\*3 \(N.D.Ill. Dec. 27, 2002\)](#)(Shadur, [\*35] J.).

[HN19](#) [Rule 703](#) was never intended to allow oblique evasions of the hearsay rule. In [Dura Automotive](#), the Seventh Circuit acknowledged that it "is common in technical fields for an expert to base an opinion in part on what a different expert believes on the basis of expert knowledge not possessed by the first expert." [285 F.3d at 613](#). For example, as the Committee Notes to the 1972 Proposed [Rule 703](#) observed, a physician, though not an expert in radiology, may rely for a diagnosis on an x-ray. *Id.* The Seventh Circuit extrapolated from there to make its point:

We too do not believe that the leader of a clinical medical team must be qualified as an expert in every individual discipline encompassed by the team in order to testify as to the team's conclusions. But suppose the soundness of the underlying expert judgment is in issue. Suppose a thoracic surgeon gave expert evidence in a medical malpractice case that the plaintiff's decedent had died because the defendant, a radiologist, had negligently failed to diagnose the decedent's lung cancer until it was too advanced for surgery. The surgeon would be competent to testify that the cancer was too advanced for [\*36] surgery, but in offering the additional and critical judgment that the radiologist should have discovered the cancer sooner he would be, at best, just parroting the opinion of an expert in radiology competent to testify that the defendant had x-rayed the decedent carelessly.

*Id.* The problem, then, is that the expert is vouching for the truth of what another expert told him - he is merely that expert's spokesman. But, [HN20](#) "[a] scientist, however well credentialed he may be, is not permitted to be the mouthpiece of a scientist in a different specialty. That would not be responsible science." [Id. at 614](#). See also [Grant v. Chemrex, Inc., 1997 U.S. Dist. LEXIS 6058, No. 93 C 0350, 1997 WL 223071, \\*8 \(N.D.Ill. Apr. 28, 1997\)](#) (expert's "professional knowledge and ability" were not adequate to evaluate calculations and opinions upon which he based his opinion).<sup>11</sup>

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<sup>11</sup> By way of example, the court in [Dura Automotive](#) said that a theoretical economist, who relied on the findings of an econometric study conducted by another economist, would not be allowed to testify if he lacked expertise in econometrics, and the study raised questions that only an econometrician could answer. [285 F.3d at 614](#). Even Judge Wood, who dissented, agreed with this example. [Id. at 620](#). See also [TK-7 Corp., 993 F.2d at 732 HN21](#) (the rationale of [Rule 703](#) "is certainly not satisfied in this case where the expert failed to demonstrate any basis for concluding that another individual's opinion on a subjective financial prediction was reliable, other than the fact that it was the opinion of someone he believed to be an expert who had a financial interest in making an accurate prediction.").

[\*\*37] That is precisely the situation here: If allowed to testify, Mr. Dohmeyer would be "hiding behind" Messrs. Barron, King and DaClue and acting as their "mouthpiece." *Id. at 615*. He would, in effect, be vouching for their labor-added methodology, when he has absolutely no knowledge of whether the theory is valid and reliable. See also *TK-7 Corp., 993 F.2d 722*. Thus, Mr. Dohmeyer's testimony cannot be used to prove that additional labor and shifts were in fact the medicament for the Line's ills. *In re James Wilson Associates, 965 F.2d 160, 173 (7th Cir. 1992)*(Posner, J.)

The example posed by Judge Posner in *James Wilson Associates* demonstrates the problem with Mr. Dohmeyer's testimony:

"If, for example, the expert witness (call him A) bases his opinion in part on a fact (call it X) that the parties lawyer told him, the lawyer cannot, in closing argument, tell the jury, 'see we proved X through our expert witness. A.'"

*Id. at 173. (Parenthesis in original).*

This was the kind of hand-off attempted in *James Wilson Associates*, where an architect attempted to testify to the value of a building based upon a report [\*\*38] provided to him by a consulting engineer, who had examined the building. The Seventh Circuit held that the trial judge "was entitled to exclude the architect's evidence as hearsay." *Id. at 172*. The issue was the state of the building, and the expert who had evaluated that state - the consulting engineer - was the one who should have testified. The architect could use what the engineer told him to offer an opinion *within the architect's domain of expertise*, but he could not testify for the purpose of vouching for the truth of what the engineer told him - "of becoming in short the engineer's spokesman." *Id. at 173*. It "is improper to use an expert witness as a screen against cross-examination (though the other side could always call him as an adverse witness, and cross-examine him)." *Id.* (Parenthesis in original).

Yet, without the testimony of Messrs. Barron, King and DaClue explaining and justifying their labor-added theory, Mr. Dohmeyer's testimony will "rest[] on air." *Dura Automotive, 285 F.3d at 615*. If the underlying assumptions cannot be proven by admissible, competent evidence, the very nature of which would appear [\*\*39] to require expert testimony, Mr. Dohmeyer's analysis of economic loss would have no evidentiary support and would be irrelevant. See *Rule 402, Federal Rules of Evidence*. Yet, the only expert disclosure in the case on the defendants' side is Mr. Dohmeyer's. Messrs. Barron, King and DaClue have not been designated as experts. Hence, it would appear that Mr. Dohmeyer's testimony, even if initially allowed, would ultimately have to be stricken.

The instant case is analytically congruent with *Dura Automotive*. There, the [\*810] court held that the expert could have testified that the well field was contaminated by volatile organic compounds and that *if* the defendant's plastics plant was within the well field's capture zone, some of the contamination may have come from that plant. It did not follow, however, that he could testify that the plant *was* within the well field's capture zone. *285 F.3d at 613-614*.

The defendant moved to bar the hydrogeologist's testimony and to dismiss Dura's claim. Dura responded with affidavits from the four employees who had prepared the models on which the hydrogeologist was basing his conclusions. The [\*\*40] defendant moved to strike the affidavits on the ground that the disclosure of additional expert witness was untimely. The district court granted the motion and held that without the affidavits, there was insufficient evidence of the reliability of the models, and the hydrogeologist's testimony could not prove that accuracy. The court barred the testimony and concluded that without it, Dura had no case. *285 F.3d at 612*.

The Court of Appeals affirmed. It held that to the extent the affidavits contained evidence that would have to be presented at trial by an expert witness or witnesses other than the hydrogeologist in order for Dura to withstand a motion of judgment as a matter of law, Dura's failure to have made timely disclosure of their experts' opinions invited application of *Rule 37(c)(1)* to bar the authors of the affidavits (or any other expert for that matter) from testifying. In the instant case, denying the motion to prohibit Mr. Dohmeyer's testimony and allowing him to testify when there will be no competent evidence to prove the truth of the underlying assumptions would result in allowing testimony that would have to be stricken as irrelevant. The law never requires [\*\*41] an idle thing to be done. *Brooklyn Life Insurance Co. v. Dutcher, 95 U.S. 269, 272, 24 L. Ed. 410 (1877)*.

*TK-7 Corp. v. Estate of Barbouti* is also instructive.<sup>12</sup> To support the plaintiff's claim and to calculate the amount of damages, the plaintiffs presented testimony from Dr. Boswell, a financial economist and professor of finance. Dr. Boswell predicated his calculations of lost profits on sales projections of one Werber. The district court initially allowed the testimony, but ultimately directed a verdict against the plaintiff, based on insufficiency of the evidence of damages. Mr. Werber was not called to testify, and the district court held that in order to prevail, the plaintiff had to present affirmative evidence on the projections that Dr. Boswell had assumed to be true. *Accord International Adhesive Coating Co. v. Bolton Emerson International*, 851 F.2d 540, 546. Since there was no such evidence, the plaintiff failed to carry its burden of proof. In affirming, the Tenth Circuit pointed out that Dr. Boswell had no familiarity with methods or reasoning used by Mr. Werber in arriving at his projections. In the instant case, Mr. Dohmeyer conceded a similar [\*\*42] lack of understanding or familiarity of the models crafted by Messrs. Barron, King and DaClue.

c

### **The Unreliability of The Methodology Underlying Mr. Dohmeyer's Conclusions Regarding Loeffel's Claim For Future Lost Profits And Business**

The third aspect of Mr. Dohmeyer's proposed expert testimony focuses on the Loeffel's claim for lost profits and business [\*811] resulting from deficiencies in the Line. The Analysis of Economic Loss was accompanied by a letter of transmittal containing a 1 1/2 page discussion of the "(steel) metals industry," under the caption, "Industry Discussion." (Parenthesis in original). It summarized isolated bits of information that Mr. Dohmeyer or one of his colleagues had read on "money.msn.com and cnnfn.com." (See letter of February 27, 2004). As one would expect given Mr. Dohmeyer's admitted lack of expertise in the steel/metals industry and the sources of the information on which [\*\*43] he relied, the 1 1/2 page discussion is superficial, generalized, and inexpert.

The discussion began by noting that the steel industry is made up of three tiers: primary metals producers, metals processors and/or service centers, and end users. The primary producers are the source of steel for the service centers, which "undertake value-adding services such as precision design and other pre-production processing as may be required by specific customers." These service centers, according to DVC, were formerly mostly distribution centers performing little processing. By the 1980s, however, they began to add processing capabilities that allowed them to add a broad range of value-added services.

Concurrently, the primary metals producers began concentrating on high volume production. As these industry changes continued, the discussion explained, many service centers found themselves unable to obtain processed products and had to begin outsourcing their customized metal processing to service centers with value-added capabilities. Recent challenges in the industry include the recession and frequent, unpredictable increases in domestic steel prices.

The Analysis of Economic Loss contained [\*\*44] 12 pages of graphs and charts reflecting financial data about 8 companies: A.M. Castle & Co.; Friedman Industries Inc.; Gibraltar Steel Corp.; Olympic Steel Inc.; Reliance Steel & Aluminum Co.; Ryerson Tull, Inc.; Steel Technologies Inc.; and Worthington Industries, Inc. The information was obtained from 10k's and Standard & Poor's reports. Mr. Dohmeyer could not explain how the companies were selected for inclusion in the sampling. This is the best he could say:

I think one of the guys did a search on one company that was - that had a *similar description* to the description for this kind of business, what they do.

(Dohmeyer's Dep. at 121)(Emphasis supplied). How the other seven were selected remains unexplained.

The charts reflected the total sales, gross profit margins, net income, equity, return on equity, stock price, book value, and market to book value of the 8 companies for the period 1999 - 2002. According to Mr. Dohmeyer, the

<sup>12</sup> *Barbouti* was cited approvingly in *Dura Automotive*. 285 F.3d at 613.

financial history of the eight companies during that period was relevant in evaluating Loeffel's potential for acquiring new business with the Line. (Dohmeyer Dep., at 119-121). But what that new business was to be, Mr. Dohmeyer [\*\*45] wasn't sure. He referred to it, variously, as "toll processing, [] heavier gauge or wider gauge or both, I don't know." (Dohmeyer Dep., at 126). Whatever it was to be, Mr. Dohmeyer explained, its net present value was a function of the competitive environment of the "industry," as reflected by the eight corporations that been chosen. (Dohmeyer Dep., at 126).

He testified that since the 8 companies had experienced financial difficulties between 1999 and 2002, Loeffel could not have hoped to do any better. (Dohmeyer Dep., at 120-122). The figures showed, among other things, *declines* in median total sales for the 8 companies from 2001 [\*812] to 2002. But Loeffel had a 5.3% *increase* in 2002, while the 8 companies had a median loss of 2.2%. Similarly, while the median *decline* from 2000 to 2001 in gross profit margins of the 8 companies was 5.8%, Loeffel had a 1.4% *increase*. From 2001 to 2002, there was a median increase in gross profit margin of the 8 companies of 6.7%, while Loeffel's increased 23.9%.

In order for the sampling chosen by DVC comparison to have the requisite predictive capacity and the reliability Daubert demands, Mr. Dohmeyer had to "select samples that [\*\*46] are truly comparable. To put it another way, care must be taken to be sure that the comparison is one between 'apples and apples' rather than one between 'apples and oranges.'" [Donnelly v. Rhode Island Board of Governors for Higher Education, 929 F.Supp 583, 591 \(D.R.I. 1996\)](#).

**HN22** [↑] In calculating lost future profits or lost business, the measure of damages is guided by analysis of "comparable businesses *in the area*." [Cates v. Morgan Portable Bldg. Corp., 591 F.2d 17, 21 n.7 \(7th Cir. 1979\)](#)(Emphasis supplied). "The business used as a standard must be as nearly identical to the plaintiff's as possible." [Lehrman v. Gulf Oil, 500 F.2d 659, 667 \(5th Cir. 1974\)](#), cert. denied, 420 U.S. 929, 43 L. Ed. 2d 400, 95 S. Ct. 1128 (1975). Accord [In re James O'Connell Co. Inc., 799 F.2d 1258, 1259 \(9th Cir. 1986\)](#); [National Farmers' Organization, Inc. v. Associated Milk Producers, Inc., 850 F.2d 1286, 1292 \(8th Cir. 1989\)](#). This is often referred to as the "yardstick approach." Absent the requisite showing of comparability, a damage model that predicts either the presence or absence of future profits is impermissibly speculative and conjectural. [\*\*47] Cf. [Home Placement Svc., Inc. v. The Providence Journal Co., 819 F.2d 1199, 1209 \(1st Cir. 1987\)](#); ABA Section of [Antitrust Law, Antitrust Law](#) Developments, 877-879 (5th ed. 2002)(and cases cited).

Of course, exact correlation is not necessary but the samples must be fair congeners. If they are not, the comparison is manifestly unreliable and cannot "'logically advance[] a material aspect of the proposing party's case. The Supreme Court [in Daubert] referred to this second prong of the analysis as the fit requirement.'" [Loeffel Steel Products v. Delta Brands, 372 F. Supp. 2d 1104, 2005 WL 1388076 at \\*16](#) (quoting Judge Kozinski's opinion on remand from the Supreme Court . [Daubert v. Merrell Dow Pharmaceuticals, Inc., 43 F.3d 1311, 1315 \(9th Cir.\)](#), cert. denied, 516 U.S. 869, 133 L. Ed. 2d 126, 116 S. Ct. 189 (1995)).

Undiscriminatingly labeling all nine companies "steel service centers," Mr. Dohmeyer tacitly assumed that they are necessarily monolithic, that they necessarily compete for the same customers, and thus the past financial profile of the eight is a reasonable predictor of how Loeffel would have performed. Stated more simply, Mr. Dohmeyer's argument [\*\*48] runs this way: 1) Loeffel and the eight companies are in the same "industry;" 2) all participants in "an industry" are necessarily competitors; 3) therefore, the financial performance of the eight companies in 1999-2002 is relevant to determining Loeffel's prospect for new business had the Line performed properly.<sup>13</sup> (Dohmeyer Dep., at 124). Here as always, "we must think things, not words, or at least we must constantly translate our words into facts [\*813] for which they stand, if we are to keep to the real and the true." Holmes, Law In Science and Science In Law, 12 Harv.L.Rev. 443, 460 (1889).

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<sup>13</sup> When asked at his deposition how, since he knew nothing about the customer base of Loeffel or the eight publicly traded companies, he could have concluded that Loeffel served the same customer market as the eight other service centers, Mr. Dohmeyer said:

Oh they have to. I mean it's -- you're in that industry, you're competing. You can't help -- once you're in an industry, you can't help but compete with other people in your industry. (Dohmeyer Dep., at 124).

[\*\*49] Mr. Dohmeyer's inexpert conclusion that each participant in "an industry" necessarily competes with every other participant in the industry is demonstrably false, as Dohmeyer's own report shows. He claimed that the "steels/metals industry" was comprised of three tiers. But as his report noted, the three categories of industry participants were not competitors, but enjoyed a symbiotic relationship. Bentleys and Kias are in the same "industry," but obviously don't compete for the same customers. Arnold Schwarzenegger and Anthony Hopkins never competed for the same roles, although they were both in the "movie industry."

Of course, these are matters of public knowledge. The inquiry becomes more difficult, when the "industry" is more complicated and less obvious. Perhaps, all "steel service centers" do compete; perhaps they don't, or perhaps they do only to an exceedingly limited degree, measured by the extent of the products and services they offer in common, and their geographic location. But only an expert in the field is qualified to say, and neither Mr. Dohmeyer nor his colleagues even begin to qualify. Cf. [Gentieu, 214 F.Supp.2d at 851](#). (What controls the admissibility [\*\*50] of an expert's opinion evidence, "depends on whether his claimed expertise qualifies him to opine on the specific matters that he seeks to address.").

A moment's reflection demonstrates the error in Mr. Dohmeyer's facile, and under-inclusive methodology. Suppose the eight companies selected by DVC had, as does Loeffel, blanking operations, but, in addition, offered a very large number of other diversified products and services, not offered by Loeffel. Assume further that unlike Loeffel with its localized customer base in the Midwest, the eight companies had nationwide or worldwide operations. In that event, the companies could scarcely be said to be comparable, and comparing their undifferentiated sales and income figures to those of Loeffel, would prove absolutely nothing. Cf. [Bailey v. Allgas, Inc., 148 F. Supp. 2d 1222, 1232 \(N.D.Ala. 2000\)](#).<sup>14</sup>

[\*\*51] Mr. Dohmeyer at his deposition admitted he knew nothing about the respective geographic or product markets or customer bases of the eight companies or of the quality of service or any other relevant factor that would bear upon the question of comparability. See [Home Placement Svc., Inc. v. The Providence Journal Co., 819 F.2d 1199, 1206 \(1st Cir. 1987\)](#). And the charts he compiled do not break out financial data by product or services. Hence, the raw financial data does not tell anything about the performance of the eight companies as to those products and services that they had in common with Loeffel. And it is only with respect to those products that they would be competitors -- at least for the purposes relevant to this case.

Even in cases involving far more comparability than is apparent here, courts have refused to allow the seemingly comparable companies to be used as a yardstick. [\*814] In [Eleven Line, Inc. v. North Texas State Soccer Ass'n, Inc., 213 F.3d 198 \(5th Cir. 2000\)](#), the plaintiff owned indoor soccer arenas. The court rejected soccer arenas in general as comparable businesses where there was no evidence offered regarding geographical location, [\*\*52] size or attractiveness of those facilities, the size and type of the market that they served, the relative costs of operation, the amounts charged, or the number years the facility was run. [Id. at 208](#). The Fifth Circuit stressed that employing such a broad category was like "arguing that because McDonald's franchises earn a certain average rate of return, a particular franchise will perform to the average." [Id. at 208-09](#). See also, [Kinesoft Development Corp. v. Softbank Holdings Inc., 139 F.Supp.2d 869, 910 \(N.D.Ill. 2001\)](#) (rejecting damages calculation where expert gave no consideration to any analysis of a comparable company selling comparable products).

**HN24** [↑] It cannot be too often repeated or too strongly emphasized that "nothing in either *Daubert* or the Federal Rules of Evidence requires a district court to admit opinion evidence that is connected to existing data only by the *ipse dixit* of the expert. A court may conclude that there is simply too great an analytical gap between the data and the opinion proffered." [Kumho Tire, 526 U.S. at 157](#). That caution applies with singular force to Mr. Dohmeyer's

<sup>14</sup> **HN23** [↑] In antitrust cases, proof of the relevant product and geographic market is absolutely essential. The relevant geographic market is generally defined as the area of effective competition, that is the area in which the product or its reasonably interchangeable substitutes are traded. A determination of the geographic market must entail an analysis of several factors including the location of competitors and price data. [Id.](#) Although this case presents different issues, for purposes of determining comparability, the analysis is much the same.

conclusion that [\*\*53] the eight publicly traded companies were comparable to Loeffel for purposes of assessing lost future business and profits.

Mr. Dohmeyer lacked the qualifications to conclude that merely because all nine companies could be classified as "service centers," they necessarily competed with Loeffel or that they were comparable. [HN25](#)<sup>15</sup> Spending a few minutes on the internet does not make one an expert on any "industry" or on any topic. Cf [Charter National Bank & Trust v. Charter One Financial, Inc., 2001 U.S. Dist. LEXIS 13919, 2001 WL 1035721 at \\*6 \(N.D.Ill. September 4, 2001\)](#)(assistant professor of law at the University of Chicago and a fellow in economics and public policy was not qualified as an expert on trademark law despite his extensive reading of trademark cases).<sup>15</sup>

[\*\*54] The eight congeners selected by DVC were large to massive, publicly traded companies. According to Mr. Dohmeyer's charts, their average *median* total sales for the period 1999 - 2002 was \$ 640 million, while Loeffel's was \$ 19 million.<sup>16</sup> Perhaps this alone is not enough to tip the balance. But, what does is Mr. Dohmeyer's inexplicable failure to have considered such critical factors as what services the companies provided, their customer base, the products they sold, the geographic markets in which they operated, their prices and other critical aspects of the businesses. In fact, Mr. Dohmeyer admitted at his deposition that neither he nor his colleagues [[\\*815](#)] researched Loeffel or the eight comparative companies' customer bases. Yet, unless Loeffel's customer base and the services and products it offered approximated those of the eight companies, they were not "comparable," and the latters' economic fortunes would not be a "reliable" predictor of how Loeffel would have fared in the period 1999-2002.

[\*\*55] The internet reveals the manifest unreliability of Mr. Dohmeyer's assumption about the uniformity of steel service centers -- an assumption that is the lynchpin in his theory of comparability. It also reveals the "fundamentally unsound basis [and] fatally deficient amount of data" on which Mr. Dohmeyer based his conclusion that the eight companies and Loeffel were comparable. [Thomas v. FAG Bearings Corp., 846 F.Supp. 1382 \(W.D.Mo. 1994\).](#)<sup>17</sup>

[\*\*56] Even a cursory search reveals that steel service centers are *not* monolithic and offer an extraordinary array of services and products, most of which are not offered by Loeffel, but are offered by the eight companies DVC selected.

In addition to cutting and slitting, coil processing, decoiling, bending, (and perhaps blade decambering) -- the services offered by Loeffel -- service centers also offer many services that Loeffel does not, such as: polishing, plasma profiling, grinding, gun drilling, tempering, stress relieving, annealing, heat treating, burning, abrasive and carbide blade sawing, computerized plasma cutting and automatic splice welding, piercing, notching, edging, ribbon and oscillate winding, punching, drilling, flame cutting, beam splitting. See [www.steelvillage.com](http://www.steelvillage.com). Similarly, the same internet site reveals a varied array of products offered by service centers, but not offered by Loeffel, including:

<sup>15</sup> The defendants have taken a somewhat inconsistent position on the question of Mr. Dohmeyer's expertise in the steel industry. First, they say that that expertise is "inconsequential." (Response at 9). Then, as an afterthought, they say that Mr. Dohmeyer "perform[ed] thorough research on the steel industry." Of course he did no such thing and saying it doesn't make it so. Finally, they say he consulted with the defendants' personnel, who have extensive experience in the steel industry. *Id.* There is nothing to support the claim that the defendants' employees are experts, and Mr. Dohmeyer never claimed that they imparted information beyond their labor-added theory. In any event, even if they had, that would not begin to satisfy the requirements of [Rule 702](#) or [703](#).

<sup>16</sup> In 2002, the actual sales for the eight companies ranged from \$ 99 million to \$ 2.296 billion. There was a similar range in gross profit margins ranging from a low of 6% to a high of 29.8% in 2002.

<sup>17</sup> [HN26](#)<sup>18</sup> Even where a witness is an expert in the relevant field, the evidentiary reliability demanded by *Daubert* is not present when his or her opinion is speculative or rests on an unsound basis. See [American Bearing Co. v. Litton Industries, Inc., 540 F.Supp. 1163, 1173 \(E.D.Pa. 1982\)](#), aff'd on other grounds, [729 F.2d 943 \(3rd Cir.\)](#), cert. denied [469 U.S. 854, 83 L. Ed. 2d 112, 105 S. Ct. 178 \(1984\)](#); [Lithuanian Commerce Corp Ltd. v. Sara Lee Hosiery, 179 F.R.D. 450 \(D.N.J. 1998\)](#)(assumptions of a certified public accountant with several advanced degrees).

pipe, rod, bar, aluminum, brass, bronze, tubing, carbon, alloy, high speed steels, alloy heat treated, abrasion resistant, high strength, HSLA plate, valves, fitting and flanges. *Id.*

Further dissimilarities abound. Loeffel is a small company with offices in [\*\*57] the greater Chicago area. It employs 70 people, and its customer base is largely in the Midwest. It is in the business of slitting and cutting raw steel into lengths and thicknesses according to customer specifications. Its customers include various industries, from filing cabinet manufacturers to metal building products and stock containers. (*Complaint*, P 1; [www.loeffel.com](http://www.loeffel.com)).

A.M. Castle & Co., specializes in the distribution of carbon, alloy and stainless steels; nickel alloys; aluminum; titanium; and brass and copper in a variety of product forms, including bar, plate, tube, sheet and coil. It operates a subsidiary, Total Plastics, Inc., through which it distributes a broad range of value-added industrial plastics. Through another subsidiary, Oliver Steel Plate, it has a market position in alloy and heavy gauge carbon plate products. Along with its affiliated companies, Castle has facilities in over 40 locations throughout North America. Its customer base includes numerous Fortune 500 companies as well as thousands of medium and smaller-sized firms spread across a wide [\*816] spectrum of industries. ([www.amcastle.com](http://www.amcastle.com)).

Friedman Industries, Inc. is in the flat roll sheet and plate [\*\*58] steel processing and distribution business. It operates two plants, in Texas and Arkansas, each capable of cutting-to-length, leveling, and temper passing hot roll steel coils. It operates a division selling excess prime, secondary, and transition steel coils, and a division that rolls and welds pipe for use in the water well industry, steel building columns, steel pipe piling, water and air lines, and many structural applications. ([www.friedmanindustries.com](http://www.friedmanindustries.com)).

Gibraltar Steel Corp.'s core business is producing value-added, high-margin steel products and services. It has expanded into the metal processing, building products, and commercial heat-treating markets, and is now the second-largest commercial heat-treater in North America and is a major supplier of metal building products. These operations utilize any one or a combination of more than 25 different processes and services to manufacture and deliver a variety of high-quality steel products and services. Gibraltar has expanded its customer base through the acquisition of 22 businesses and the investment of more than \$ 200 million in capital expenditures and now has 72 facilities in 26 states, Mexico, and Canada serving more [\*\*59] than 10,000 customers in a variety of industries. These customers are both domestic and international, including manufacturers and distributors and, to a lesser extent, end-users for a wide range of applications, and consumers through hardware and building products distributors and mass merchandisers. Gibraltar's major commercial markets include the automotive, automotive supply, building and construction, steel, machinery, and general manufacturing industries. ([www.gibraltar1.complaint](http://www.gibraltar1.complaint)).

Olympic Steel is a domestic steel service center with a primary focus on the direct sale and distribution of large volumes of processed carbon, coated and stainless flat-rolled sheet, coil and plate steel products. Its processing services include both traditional service center processes of cutting-to-length, slitting, and shearing and higher value-added processes of blanking, tempering, plate burning, laser welding, and precision machining of steel parts. Olympic operates 12 processing and distribution facilities in Connecticut, Georgia, Illinois, Iowa, Michigan, Minnesota, Ohio, and Pennsylvania, with over 800 employees. It participates in two joint ventures in Michigan that primarily service [\*\*60] the automotive market in the Detroit area. Its customers include both regional concerns and larger national and multi-location accounts, located throughout the midwestern, eastern and southern United States. ([www.olysteel.com](http://www.olysteel.com)).

Reliance Steel & Aluminum Co., which is traded on the New York Stock Exchange, is one of the largest metals service center companies in the United States. It operates a network of more than 100 locations in 30 states, Belgium, France and South Korea, providing value-added metals processing services. It distributes a full line of more than 90,000 metal products, including galvanized, hot-rolled and cold-finished steel, stainless steel, aluminum, brass, copper, titanium, and alloy steel. Reliance boasts more than 95,000 customers in a broad range of industries. ([www.rsac.com](http://www.rsac.com)).

Ryerson Tull, Inc. is a leading North American distributor and processor of metals with annual sales of over \$ 2.2 billion. With over 5,000 employees, it operates a network of service centers across the United States and Canada, has investments in additional service centers in Mexico and Asia, and maintains metal trading capabilities around the world. Recently, it [\*817] acquired Integris Metals, [\*\*61] Inc., North America's fourth largest metals service center with 2004 revenues of \$ 2 billion. Ryerson Tull processes stainless steel, aluminum, copper alloys, and industrial plastics, and maintains inventories over more than 100,000 metal and plastic items in a wide variety of grades, shapes, and sizes. ([www.ryersontull.com](http://www.ryersontull.com)).

Steel Technologies, Inc. is one of the largest independent steel processors in North America, and operates a network of 20 facilities throughout the eastern half of the United States and Mexico. It processes precision flatrolled products for various industries, including the automotive, appliance, lawn and garden, agricultural, office equipment and railcar industries. Steel Technologies employs over 1,000 people. ([www.steeltchnologies.com](http://www.steeltchnologies.com)).

Finally, Worthington Industries, is a global company that processes steel for use in the automotive, construction, hardware, aerospace and many other industries. With some 8,000 employees, Worthington operates 65 facilities in 10 countries across North America and Europe. It manufactures metal products such as metal framing, pressure cylinders, automotive past model service stampings, metal ceiling grid systems and laser [\*\*62] welded blanks. Worthington's metal framing subsidiary produces steel studs, floor joists, roof trusses, and other metal accessories for wholesale distributors and commercial and residential building contractors. Its pressure cylinder business caters to customers in the liquified petroleum gas and refrigeration industries, and manufactures cylinders to hold everything from acetylene for welding to oxygen for breathing. ([www.worthingtonindustries.com](http://www.worthingtonindustries.com)).

**HN27**[ [Daubert](#)] requires that trial judges must ensure that any and all expert testimony is not only relevant, but reliable. To that end, a judge must undertake a preliminary assessment of whether the reasoning or methodology underlying the testimony is scientifically valid and whether that reasoning or methodology properly can be applied to the facts at issue. [Frymire-Brinati, 2 F.3d at 186](#). The judge must look behind the expert's ultimate conclusion and analyze the adequacy of its foundation. [Mid-State Fertilizer, 877 F.2d at 1339](#). Expert opinion that is speculative is inadmissible. Cf. [Target Market Pub., Inc. v. ADVO, Inc., 136 F.3d 1139, 1143 \(7th Cir. 1998\)](#).

Mr. Dohmeyer's opinion [\*\*63] that the financial performance of the eight companies in the period 1999-2002 can be used in evaluating Loeffel's lost profits or business in that period is unreliable and speculative. The defendants' use the phrase, "junk science," to refer to Mr. Toczy's expert opinion. It was inappropriate there. [Loeffel Steel Products, supra](#). It is, however, appropriately applied to the sampling of supposedly comparable companies compiled by DVC. Mr. Dohmeyer's testimony will not be allowed. The oft-repeated caution that **HN28**[] courts should be particularly wary of unfounded expert opinion when causation is the issue applies here. See [In re Agent Orange Product Litigation, 611 F.Supp. 1223, 1249 \(E.D.N.Y. 1985\)](#), aff'd, [818 F.2d 187 \(2nd Cir. 1987\)](#), cert. denied sub nom., [Lombardi v. Dow Chemical Co., 487 U.S. 1234, 101 L. Ed. 2d 932, 108 S. Ct. 2898 \(1988\)](#); [Thomas v. FAG Bearings, 846 F.Supp. 1382, 1394 \(W.D.Mo. 1994\)](#).

## B

### Assessment of Relevance

**HN29**[] To be admissible, expert testimony must be not only reliable, but relevant. [Daubert, 509 U.S. at 597](#); [United States v. Allen, 390 F.3d 944, 949 \(7th Cir. 2004\)](#). Testimony [\*\*64] is relevant if it [\*818] assists the trier of fact in understanding the evidence or in determining a fact at issue. An expert, who, like Mr. Dohmeyer, supplies nothing but a bottom line supplies nothing of value to the judicial process. [Minasian v. Standard Chartered Bank, PLC, 109 F.3d 1212, 1216 \(7th Cir. 1997\)](#).

## III

## MR. DOHMEYER'S REPORT CRITIQUING MR. WIERSEMA'S ANALYSIS VIOLATED RULE 26(a)(2)

We come then to the argument that the defendants' failure to comply with the requirements of *Rule 26(a)(2)(B), Federal Rules of Civil Procedure*, requires barring testimony by Mr. Dohmeyer critical of Mr. Wiersema's conclusions. Recognizing that secrecy is not congenial to truth seeking, [HN30](#)<sup>18</sup> the Rule requires that an expert report must disclose "a complete statement of all opinions to be expressed and the basis and reasons therefor . . ." <sup>19</sup>

<sup>18</sup> [\\*\\*65\] Hoffman v. Caterpillar, Inc., 368 F.3d 709, 714 \(7th Cir. 2004\)](#)(Emphasis supplied). <sup>19</sup>

Mr. Dohmeyer's critique of Mr. Wiersema's report is his one page letter of February 27, 2004. Despite the clarity of *Rule 26*, and the fact that Mr. Dohmeyer was engaged specifically to analyze Mr. Wiersema's conclusions (Defendants' Response at 2), his report consisted of but five unadorned conclusions, set forth in bullet-point format:

- . the Report's model has multiple incorrect premises of damages;
- . The Report's model fails to incorporate risk/cost of capital procedures;
- . The Report's model adds the alleged lost profits of the equipment as represented and the cost of the machine;
- . The Report's model's methodology; and
- . The Report's model has [sic] other assumptive and methodological errors.

The letter concludes: "As a result of the foregoing, Mr. Wiersema's model and related opinions are not reliable."

At his [\\*\\*66\]](#) deposition, Mr. Dohmeyer conceded that his criticisms of Mr. Wiersema's report offered no explanation, no written opinions, no details, no analysis. (Dohmeyer Dep., at 76, 78). [HN32](#)<sup>20</sup> Expertise is a rational process, and a rational process implies express reasons for judgment. [Federal Power Commission v. Hope Natural Gas Co., 320 U.S. 591, 627, 88 L. Ed. 333, 64 S. Ct. 281 \(1944\)](#)(Frankfurter, J. dissenting). An expert's opinion full of assertion but empty of reasons has no value and is devoid of persuasiveness and legal significance.

[HN33](#)<sup>21</sup> An expert must demonstrate in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field. [Kumho Tire, 1819 526 U.S. at 152](#). At his deposition, Mr. Dohmeyer spoke of the rigorous standards for admission into the American Society of Appraisers. (Dohmeyer Dep., at 13). He would never have gained admission to the ASA had he submitted an appraisal for evaluation as devoid of explanation and reasoning as was the "preliminary critique" of Mr. Wiersema's report. "Why should a court rely on the sort of exposition [a responsible member of the ASA] would not tolerate in his professional life." [Mid-State Fertilizer Co., 877 F.2d at 1339](#). <sup>22</sup>

What Judge Shadur wrote in [Gregory, 2002 U.S. Dist. LEXIS 24730, 2002 WL 31972165 at \\*1](#), applies equally here: "There is frankly no justification that would permit any 'expert' witness, or any lawyer dealing with one, to tender a report that is so patently deficient in every one of those [things required by *Rule 26*] as the one that is at issue here." The deficiencies in the February 27th letter -- which was never supplemented -- are all the more inexcusable in light of Mr. Dohmeyer's involvement in hundreds of cases as an expert and the defendants' lawyers' experience and skill. <sup>23</sup>

<sup>18</sup> *Rule 26(a)(2)(B)* provides, in pertinent part:

[HN31](#)<sup>24</sup> Except as otherwise stipulated or directed by the court, this disclosure *shall*, with respect to a witness who is retained or specially employed to provide expert testimony in the case or whose duties as an employee of the party regularly involve giving expert testimony, be accompanied by a written report prepared and signed by the witness. The report *shall contain a complete statement of all opinions to be expressed and the basis and reasons therefor; the data or other information considered by the witness in forming the opinions; [and] any exhibits to be used as a summary or support for the opinions; . . .* (Emphasis supplied).

<sup>19</sup> Mr. Wiersema's report referred to approximately 1800 pages of exhibits, detailing expenses Loeffel claims to have incurred as a result of the Line's malfunctioning and the damages from claimed losses of current and prospective customers.

<sup>20</sup> To emphasize the extent of his experience as an expert witness, Mr. Dohmeyer's Declaration says that he has provided "expert witness testimony and analysis for over 15 years in hundreds of cases." [2002 U.S. Dist. LEXIS 24730, \[WL\] at 2](#).

The second aspect of Mr. Dohmeyer's report is the "Analysis of Economic Loss," to which was attached Mr. Dohmeyer's curriculum vitae. It contains the heading, "EXPERT WITNESS TESTIMONY."<sup>HN34</sup> Rule 26(a)(2)(B) requires the disclosure [\*\*68] of "any other cases in which the witness has testified as an expert at trial or by deposition within the preceding four years." The report must be "detailed and complete." *Salgado by Salgado v. General Motors Corp.*, 150 F.3d 735, 741 n.6 (7th Cir. 1998) (quoting Advisory Committee's note). Thus, the cases have generally defined the "listing of cases" requirement to include the name of the court, the name of the parties, the case number, and whether the testimony was given at deposition or trial. *Id.* Accord *Zollinger v. Owens-Brockway Glass Container, Inc.*, 233 F.Supp.2d 349, 356 (N.D.N.Y. 2002); *Coleman v. Dydula*, 190 F.R.D. 316, 318 (W.D.N.Y. 1999); *Hilt v. SFC Inc.*, 170 F.R.D. 182, 185 (D.Kan. 1997); *Giladi v. Strauch*, 2001 U.S. Dist. LEXIS 4645, No. 94 Civ. 3976, 2001 WL 388052, at \*3 (S.D.N.Y. Apr. 16, 2001).<sup>21</sup>

[\*\*69] In nearly every instance, Mr. Dohmeyer's description of the cases in which he previously had been involved was uninformative. Here are 2 examples: "Breach of Contract -- Analysis of Economic Loss to an Oil & Gas Concern," and "Economic Loss -- Injury -- Jay Gueck, Esq. (August, 2002)." As to the 33 entries that topically were relevant to Mr. Dohmeyer's testimony, involving as they did, "economic loss," the only case name listed was *Ellis v. Walker*. (Qualifications of Principal Appraisers, at 1-6). The others are listed as "Analysis of Economic Loss" or "Economic Loss," followed by the kind of business involved: a restaurant franchise, a weekly newspaper, a mobile home park, an aircraft maintenance facility, medical industry, residential building company, real estate agent, law firm, printing company, software developer, retail dress shop, real estate developer, and so on. As to these entries, their format made impossible, any [\*820] meaningful investigation of Mr. Dohmeyer's background as an expert witness.<sup>22</sup>

[\*\*70] Significantly, Mr. Dohmeyer did not list *In Matter of Dunham*, 110 F.3d 286 (5th Cir. 1997).<sup>23</sup> There, Mr. Dohmeyer was engaged to testify regarding the value of an insurance agency's book of business. He concluded that the value was \$ 26,000; his opposite number in the case, Mr. Phillips, concluded the figure was closer to \$ 200,000. The district court held that Mr. Dohmeyer was not only inexperienced in the insurance industry, but his computations rested on the "erroneous assumption" that no non-competition agreements had been executed. *110 F.3d at 288*. The district court did not find Mr. Dohmeyer's assessment credible. The Fifth Circuit agreed that the district court was right in attributing little or no probative value to the Mr. Dohmeyer's appraisal. *Id. at 289*.

[\*\*71] I need not decide why the *curriculum vitae* failed, with but two exceptions, to list the names of the 116 cases. Whatever the reason, given Mr. Dohmeyer's extensive experience and the defendants' lawyer's sophistication, the skeletal format employed was indefensible and severely compromised Loeffel's ability to investigate Mr. Dohmeyer's involvement in any but a handful of the 116 matters he listed.

But this omission is insignificant compared to Mr. Dohmeyer's failure to disclose that the Analysis of Economic Loss was based entirely upon a theory given to him by the defendants, namely that the claimed deficiencies with the Line could be cured by the simple expedient of adding two additional workers and running the Line longer. While the theory, itself, might be deducible from the content of the arithmetic schedules that comprise the Analysis of Economic Loss Report, the source of the theory was not. Nothing in the "Limiting Conditions," which purported to state the "general assumptions and general limiting conditions" on which the "value opinion report has been prepared," hinted that the core assumptions on which all of Mr. Dohmeyer's endeavors were predicated came from [\*\*72] his employers. Indeed, Mr. Dohmeyer's report conveyed precisely the opposite impression.

<sup>21</sup> The Rule requires the qualifications of the witness, including a list of all publications authored by the witness within the preceding ten years; the compensation to be paid for the study and testimony; and a listing of any other cases in which the witness has testified as an expert at trial or by deposition within the preceding four years.

<sup>22</sup> Only a handful of the entries contain the designation "trial" or "deposition." Even as to those that did, it was impossible to tell anything about the engagement or Mr. Dohmeyer's testimony since the entry did not contain sufficient information to enable Loeffel to conduct an appropriate inquiry.

<sup>23</sup> The only conceivable reference to the *Dunham* case in the *curriculum vitae* is the terse entry, "Bankruptcy -- Valuation of an insurance agency," which was buried in the middle of the 116 entries.

In the "Appraisal Certification" attached to his report, Mr. Dohmeyer "certified that, to the best of our knowledge and belief," the "reported analyses, opinions, and conclusions are limited *only* by the *reported assumptions* and limiting conditions, and are *our personal*, unbiased professional analyses, opinions, and conclusions." He went on to say that "*no one* provided significant professional assistance to the person signing this report." (Emphasis supplied). This was untrue: the defendants' employees had provided the salient "assumption" on which the Analysis Of Economic Loss was based, and nothing played a more "significant" role in that analysis.

Mr. Dohmeyer attempted at his deposition to distance himself from the "Statement of Limiting Conditions" by claiming that the attachment was "boilerplate that we use in . . . all of our assignments," and that the Appraisal Certification wasn't particularly meaningful since his report was not a business appraisal, but an economic loss analysis. (Dohmeyer deposition at 21, [\*821] 15-17). In his belatedly filed Declaration, he said that the [\*\*73] appraisal certification was attached in error to the Analysis. *Id.* at 2.

Some six months after the deposition, Loeffel filed the instant motion and raised the issue of the non-compliance with Rule 26(a)(2)(B). In response, the defendants filed a nine-page declaration from Mr. Dohmeyer and a paragraph from a book on valuation by Sharron Pratt. The breezy squib cites no authority, either scholarly or legal for its conclusion. Ms. Pratt, according to her internet site, is the owner of Business Valuation Resources, a company dedicated to "high-quality valuation related resources" for all manner of professionals.<sup>24</sup>

The Declaration echoed much of Mr. Dohmeyer's deposition testimony. But it went substantially beyond [\*\*74] that and attempted to make the case against Mr. Wiersema that the February 27th "critique" did not. Not surprisingly, Loeffel objects to the Declaration and to the squib from Ms. Pratt's book.

The Declaration contended that, as a certified public accountant, Mr. Wiersema lacked "valuation expertise" and thus, wrongly concluded that Loeffel's economic loss exceeded the pre-damaged value of the company. (Declaration, P 9). This opinion appeared nowhere in the February 27, 2004 letter. Ms. Pratt apparently agrees, but the one paragraph excerpt relied on by Mr. Dohmeyer, contains no citation of authority and nothing beyond her *ipse dixit* that "it is axiomatic that the present value of lost future profits can be equal to but not greater than, the total value of the enterprise had the damaging event not occurred." However, there immediately follows this sentence, which supports Mr. Wiersema's position: "however, I have seen 'experts' testify to damage sums many times any reasonable value for the entire entity." Apparently some judges have admitted as proper expert opinion the conclusion denounced by Mr. Dohmeyer.

He again repeated in his Declaration that there was no authoritative [\*\*75] test for assessing damages when a machine operated at a level below specifications. (Declaration, P 19). This opinion seems at odds with the defendants' Response, which insists that the measure of damages is properly set forth in *Moorman*. More importantly, Mr. Dohmeyer contradicted his deposition testimony by claiming that the Analysis of Economic Loss relied upon a "benefit of the bargain" theory and took into account the production rates provided by the contract specifications. (Declaration, P 23). To say this contradicts his previous position is an understatement; he testified that the specifications were "inherently not relevant" and that he "didn't consider them one way or another." (Dohmeyer Dep., at 35, 83).

The defendants do not attempt to justify the omissions and deficiencies in the February 27th critique or in Mr. Dohmeyer's curriculum vitae; nor do they attempt to argue that the omissions are harmless. Instead, they say that Mr. Dohmeyer has "satisfied all the requirements of Rule 26," and that Loeffel's only objection relates to the "format" of the February 27th letter. (Response at 17). Any argument of harmlessness is therefore forfeited. See *Hammel v. Eau Galle Cheese Factory*, 407 F.3d 852, 869 (7th Cir. 2005); [\*\*76] *Musser v. Gentiva Health Servs.*, 356 F.3d 751, 758 (7th Cir. 2004); Rule 37(c)(1). Federal [\*822] Rules of Civil Procedure. To the extent the Declaration repeats Mr. Dohmeyer's deposition testimony, it is irrelevant. To the extent it seeks to explain the basis for his

<sup>24</sup> The defendants' Response calls Ms. Pratt a "highly regarded economist," but does not identify the basis for the representation. (Response at 7). An internet search reveals that she writes on valuation of businesses. [www.bvresources.com](http://www.bvresources.com). Ms. Pratt is apparently in the same field as Mr. Dohmeyer.

opinions either in his deposition or in his reports, it is improper and untimely and will not be considered. [Bailey v. Allgas, 148 F.Supp.2d at 1236.](#) Cf. *Dura Automotive*.

## IV

### CONCLUSION

The plaintiff's motion to bar the testimony of Mr. Dohmeyer [77] is GRANTED, and the plaintiff's motion to strike exhibits A and C to the Response [93] is also GRANTED. The defendants' unamplified request for a "full *Daubert* hearing to determine the admissibility of Mr. Dohmeyer's testimony," made in the last sentence of their Response brief, is denied. I have before me the deposition of Mr. Dohmeyer and his reports. No more is needed to determine reliability. [Kumho Tire, 526 U.S. at 152;](#) [Group Health Plan, Inc. v. Philip Morris USA, Inc., 344 F.3d 753, 761 n.3](#) (8th Cir. 2003); [Oddi v. Ford Motor Co., 234 F.3d 136, 153-154 \(3rd Cir.\),](#) [\*\*77] cert. denied 532 U.S. 921, 149 L. Ed. 2d 287, 121 S. Ct. 1357 (2000); [Jaros v. DuPont \(In re Hanford Nuclear Reservation Litig.\), 292 F.3d 1124, 1138-39 \(9th Cir. 2002\);](#) [Kirstein v. Parks Corp., 159 F.3d 1065, 1067 \(7th Cir. 1998\).](#) They will not be permitted to "return to the drawing board" to restructure Mr. Dohmeyer's testimony. [Gregory, 2002 U.S. Dist. LEXIS 24730, 2002 WL 31972165 at \\*3.](#)

**DATE:** July 22, 2005

**ENTERED:**

Jeffery Cole

**UNITED STATES MAGISTRATE JUDGE**

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## Polygram Holding, Inc. v. FTC

United States Court of Appeals for the District of Columbia Circuit

September 16, 2004, Argued ; July 22, 2005, Decided

No. 03-1293

**Reporter**

416 F.3d 29 \*; 367 U.S. App. D.C. 367 \*\*; 2005 U.S. App. LEXIS 14931 \*\*\*; 2005-1 Trade Cas. (CCH) P74,870

Polygram Holding, Inc., et al., Petitioners v. Federal Trade Commission, Respondent

**Prior History:** [\*\*\*1] On Petition for Review of an Order of the Federal Trade Commission.

*[In re Polygram Holding, 2003 FTC LEXIS 155 \(F.T.C., Oct. 14, 2003\)](#)*

**Disposition:** Petition for review denied.

## **Core Terms**

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album, concert, advertising, FTC, moratorium, consumers, rule of reason, procompetitive, condemned, output, anticompetitive, discounting, products, competitors, promoted, prices, joint venture, distribute, antitrust, courts, anti trust law, learning, restrain, reasons

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Public Enforcement > US Federal Trade Commission Actions > Judicial Review

### **[HN1](#)[] US Federal Trade Commission Actions, Judicial Review**

The Federal Trade Commission's findings of fact are conclusive if supported by substantial evidence. [15 U.S.C.S. § 45\(c\)](#). The legal issues are for the courts to resolve, although even in considering such issues the courts are to give some deference to the Commission's informed judgment that a particular commercial practice is to be condemned as unfair.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Per Se Rule & Rule of Reason > Per Se Rule Tests > Manifestly Anticompetitive Effects

### **[HN2](#)[] Antitrust & Trade Law, Sherman Act**

There are two complimentary categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality; they are illegal per se. In the second category are agreements whose competitive effect can only be evaluated by analyzing the facts particular to the business, the history of the restraint, and the reasons why it was imposed.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

### **HN3** Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

Per se analysis, which requires courts to generalize about the utility of a challenged practice, reduces the cost of decisionmaking but correspondingly raises the total cost of error by making it more likely some practices will be held unlawful in circumstances where they are harmless or even procompetitive. The converse, increased litigation cost but reduced cost of error, obtains under the rule of reason, which requires an exhaustive inquiry into all the myriad factors bearing on whether the conduct is on balance anticompetitive or procompetitive.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

### **HN4** Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

Rather than focusing upon the category to which a particular restraint should be assigned, judicial precedent emphasizes the basic point that under [15 U.S.C.S. § 1](#) the essential inquiry is whether the challenged restraint enhances competition. In order to make that determination, a court must make an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint, which in some cases may not require a full-blown market analysis. The object is to see whether the experience of the market has been so clear, or necessarily will be, that a confident conclusion about the principle tendency of a restriction will follow from a quick (or at least quicker) look, in place of a more sedulous one. And of course what the court sees may vary over time, if rule-of-reason analyses in case after case reach identical conclusions.

Antitrust & Trade Law > Sherman Act > General Overview

### **HN5** Antitrust & Trade Law, Sherman Act

At bottom, the Sherman Act requires the court to ascertain whether the challenged restraint hinders competition.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

### **HN6** Price Fixing & Restraints of Trade, Cartels & Horizontal Restraints

If, based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition, then the restraint is presumed unlawful and, in order to avoid liability, the defendant must either

identify some reason the restraint is unlikely to harm consumers or identify some competitive benefit that plausibly offsets the apparent or anticipated harm.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Joint Contracts

Business & Corporate Law > Joint Ventures > Formation

Mergers & Acquisitions Law > Antitrust > Joint Ventures

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Business & Corporate Law > Joint Ventures > General Overview

### **HN7** Types of Contracts, Joint Contracts

A restraint on trade cannot be justified solely on the ground that it increases the profitability of the enterprise that introduces the new product, regardless whether that enterprise is a joint venture or a solo undertaking.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

### **HN8** Price Fixing & Restraints of Trade, Cartels & Horizontal Restraints

In any case in which competitors are able to increase the price level or to curtail production by agreement, it could be argued that the agreement has the effect of making the market more attractive to potential new entrants. If that potential justifies horizontal agreements among competitors imposing one kind of voluntary restraint or another on their competitive freedom, it would seem to follow that the more successful an agreement is in raising the price level, the safer it is from antitrust attack.

**Counsel:** Bradley S. Phillips argued the cause for petitioners. With him on the briefs were Glenn D. Pomerantz and Stephen E. Morrissey.

John F. Daly, Deputy Special Counsel for Litigation, Federal Trade Commission, argued the cause for respondent. With him on the brief were Michele Arington, Attorney, Susan A. Creighton, Director, and Richard B. Dagen, Assistant Director.

**Judges:** Before: GINSBURG, Chief Judge, and EDWARDS and ROGERS, Circuit Judges. Opinion for the Court filed by Chief Judge GINSBURG.

**Opinion by:** Ginsburg

## **Opinion**

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[\*\*369] [\*31] *Ginsburg*, CHIEF JUDGE: PolyGram Holding, Inc. and several of its affiliates petition for review of an order of the Federal Trade Commission holding PolyGram violated § 5 of the Federal Trade Commission Act, [15 U.S.C. § 45](#). As detailed below, PolyGram entered into an agreement with Warner Communications, Inc. to distribute the recording of a concert to be given by "The Three Tenors" in 1998. The two companies later entered into a separate agreement to suspend, for ten weeks, advertising and discounting of two earlier Three Tenors concert albums, one distributed by PolyGram [\*\*\*2] and the other by Warner. The Commission held the latter

agreement unlawful and prohibited PolyGram from entering into any similar agreement in the future. We agree with the Commission that, although not a *per se* violation of **antitrust law**, the agreement was presumptively unlawful and PolyGram failed to rebut that presumption. We therefore deny PolyGram's petition for review.

## I. Background

Here are the facts as found by the Commission in its order and opinion of July 28, 2003. See [In re PolyGram Holding, Inc., 2003 FTC LEXIS 120, Docket No. 9298 \(FTC\), 2003 WL 21770765 \(2003\)](#), available at <http://www.ftc.gov/os/2003/07/polygramopinion.pdf> (hereinafter, FTC Op.). The Three Tenors -- Jose Carreras, Placido Domingo, and Luciano Pavarotti -- put on spectacular concerts coinciding with the World Cup soccer finals in 1990, 1994, and 1998. PolyGram distributed the recording of the 1990 concert, which became one of the best-selling classical albums of all time. FTC Op. at 5-6. Warner distributed the 1994 concert album, which also met with great success. Both albums remained on the top-ten classical list throughout 1994, 1995, and 1996. *Id.* at 6.

In late 1997 PolyGram and Warner agreed jointly [\*\*\*3] to distribute the recording of The Three Tenors' July 1998 concert. Warner, which had the worldwide rights, retained the United States rights but licensed to PolyGram the exclusive right to distribute the 1998 album outside the United States, and the companies agreed to share equally the worldwide profit or loss on the project. FTC Op. at 8. The agreement also obligated PolyGram and Warner to consult with one another on all "marketing and promotional activities" for the 1998 concert album, but each company was free ultimately to pursue its own marketing strategy and to continue exploiting its earlier Three Tenors concert album without limitation. The agreement also provided that PolyGram and Warner would collaborate on the distribution of any future Three Tenors album released through August 2002. *Id.*

[\*32] [\*\*370] Representatives of PolyGram and Warner first met in January 1998 to discuss "marketing and operational issues." One of PolyGram's representatives voiced concern about the effect of marketing the earlier Three Tenors albums upon the prospects for the 1998 concert album and suggested the two companies impose an "advertising moratorium" surrounding the 1998 release, which was scheduled [\*\*\*4] for August 1. According to notes of their next meeting (in March) PolyGram and Warner representatives agreed that "a big push" on the earlier albums "shouldn't take place before November 15." After that meeting, each company instructed its affiliates to cease all promotion of the 1990 and 1994 Three Tenors albums for approximately six weeks, beginning in late July or early August. FTC Op. at 8.

Apparently Warner's overseas division did not get the message because in May it announced an aggressive marketing campaign, scheduled to run through December, to discount and to promote the 1994 album throughout Europe. When PolyGram learned of this, it threatened to "retaliate" by cutting the price of its 1990 album. Accusations then flew between the two companies about which had started the imminent price war. Meanwhile, in June the promoter of The Three Tenors concert informed PolyGram and Warner that the repertoire for the 1998 concert would substantially overlap those of the 1990 and 1994 concerts, which in the view of both PolyGram and Warner executives jeopardized the commercial viability of the forthcoming concert album. FTC Op. at 8-9.

By the time The Three Tenors performed in Paris [\*\*\*5] on July 10, PolyGram and Warner had exchanged letters reaffirming their commitment to suspend advertising and discounting the 1990 and 1994 concert albums and agreeing the moratorium would run from August 1 through October 15. About a week later, however, PolyGram's Senior Marketing Director, who had passed on the details of the agreement to PolyGram's General Counsel, sent a memorandum around the company stating, "Contrary to any previous suggestion, there has been no agreement with [Warner] in relation to the pricing and marketing of the previous Three Tenors albums." Warner followed suit on August 10, sending a letter to PolyGram repudiating any pricing or advertising restrictions relative to its 1994 album. At the same time, however, PolyGram and Warner executives privately assured one another their respective companies intended to honor the agreement, and in fact the companies did substantially comply with the agreement through October 15, 1998. FTC Op. at 9.

In 2001 the Commission issued complaints against PolyGram and Warner charging that, by entering into the moratorium agreement, the companies had engaged in an unfair method of competition in violation of [§ 5 of the FTC Act](#). [\*\*\*6] Warner soon consented to an order barring it from making any similar agreement in the future.

FTC Op. at 3 n.3. PolyGram contested the charge and, after a trial, an Administrative Law Judge ruled that PolyGram had violated [§ 5](#) and ordered PolyGram, like Warner, to refrain from making any similar agreement in the future.

The Commission affirmed the order of the ALJ. After first observing (correctly) that the analysis under [§ 5 of the FTC Act](#) is the same in this case as it would be under § 1 of the Sherman Act, [15 U.S.C. § 1](#), FTC Op. at 13 n.11, the Commission revived the analytic framework it had first announced *In re Massachusetts Board of Optometry*, 110 F.T.C. 549 (1988), which begins with the proposition that conduct "inherently suspect" as a restraint of competition -- that is, conduct that "appears [\[\\*33\]](#) [\[\\*\\*371\]](#) likely, absent an efficiency justification, to restrict competition and decrease output" -- is to be presumed unreasonable. FTC Op. at 22-24. Only if the competitive harm wrought by the restraint is not readily apparent from the nature of the restraint itself, or the charged party offers a plausible competitive justification for the restraint, [\[\\*\\*\\*7\]](#) must the Commission, under this approach, engage in a more searching analysis of the market circumstances surrounding the restraint. *Id.* at 29.

Here the Commission determined the agreement between PolyGram and Warner to prohibit discounts and advertising for a time was indeed "inherently suspect" because such restraints by their nature tend to raise prices and to reduce output. FTC Op. at 35-40. The Commission then looked to PolyGram to identify some competitive justification for the restraint. *Id.* at 40. PolyGram objected that the Commission must first offer some evidence the agreement actually harmed competition. In any event, PolyGram argued, the agreement was justified because it prevented PolyGram and Warner, as distributors of the 1990 and 1994 albums, respectively, from free-riding upon -- and thereby diminishing -- each other's efforts to promote the 1998 album; hence the restraints created an incentive for each company vigorously to promote the 1998 album and thereby increased output. The Commission rejected that purported efficiency justification as legally insufficient. In the Commission's view, the moratorium agreement could not have had any such procompetitive [\[\\*\\*\\*8\]](#) effect but instead simply shielded the 1998 concert album from the competition of the two earlier albums. *Id.* at 41-48.

Observing that under the analytic framework of *Mass. Board* it could have stopped there, the Commission nonetheless went on to rule that, even if PolyGram's efficiency justification were cognizable, the facts simply did not support it, FTC Op. at 50; indeed, the Commission found the moratorium had no effect upon the degree to which the companies promoted the 1998 album and did not make the joint venturers any more likely to release a future Three Tenors album. *Id.* at 56-57. Thus, upon closer inspection, the Commission confirmed its initial conclusion that the moratorium agreement was an unreasonable restraint of trade in violation of [§ 1 of the Sherman Act](#) and, hence, an unfair method of competition in violation of [§ 5](#) of the FTC Act. *Id.* at 58.

## II. Analysis

PolyGram raises four objections to the decision of the Commission: First, the Commission should not have rejected the free-rider justification as legally insufficient because the moratorium agreement had a legitimate, procompetitive purpose reasonably related to the joint venture. Second, [\[\\*\\*\\*9\]](#) the Commission was required to show the restraints actually harmed competition before it could require PolyGram to proffer a competitive justification. Third, the Commission's findings concerning the competitive impact of the restraint were not supported by substantial evidence. Finally, there is no danger the same conduct will recur, so the Commission's prohibitory remedy is unreasonable.

**HN1**  The Commission's findings of fact are conclusive if supported by substantial evidence. See [15 U.S.C. § 45\(c\)](#). The legal issues are "for the courts to resolve, although even in considering such issues the courts are to give some deference to the Commission's informed judgment that a particular commercial practice is to be condemned as 'unfair.'" [FTC v. Ind. Fed'n of Dentists](#), 476 U.S. 447, 454, 90 L. Ed. 2d 445, 106 S. Ct. 2009 (1987) (*IFD*).

The Supreme Court's approach to evaluating a [§ 1](#) claim has gone through a transition over the last twenty-five years, from [\[\\*34\]](#) [\[\\*\\*372\]](#) a dichotomous categorical approach to a more nuanced and case-specific inquiry. In 1978, just before the transition began, the Court summarized its doctrine as follows:

**HN2**[<sup>10</sup>] There are ... two complimentary [\*\*\*10] categories of antitrust analysis. In the first category are agreements whose nature and necessary effect are so plainly anticompetitive that no elaborate study of the industry is needed to establish their illegality -- they are "illegal per se." In the second category are agreements whose competitive effect can only be evaluated by analyzing the facts particular to the business, the history of the restraint, and the reasons why it was imposed.

Nat'l Soc'y of Prof'l Eng'rs v. United States, 435 U.S. 679, 692, 55 L. Ed. 2d 637, 98 S. Ct. 1355 (1978).

Courts and commentators have recognized the trade-offs inherent in each category. **HN3**[<sup>11</sup>] Per se analysis, which requires courts to generalize about the utility of a challenged practice, reduces the cost of decision-making but correspondingly raises the total cost of error by making it more likely some practices will be held unlawful in circumstances where they are harmless or even procompetitive. See, e.g., Arizona v. Maricopa County Med. Soc., 457 U.S. 332, 344, 73 L. Ed. 2d 48, 102 S. Ct. 2466 (1982) ("For the sake of business certainty and litigation efficiency, we have tolerated the invalidation of some agreements that a fullblown inquiry [\*\*\*11] might have proved to be reasonable"); Phillip E. Areeda & Herbert Hovenkamp, Antitrust Law, P1509c (2d ed. 2003) (observing that per se analysis "dispenses with costly proof requirements, such as proof of market power," but consequently "produces a certain number of false positives"). The converse -- increased litigation cost but reduced cost of error -- obtains under the rule of reason, which requires an exhaustive inquiry into all the myriad factors "bearing on whether the conduct is on balance anticompetitive or procompetitive." Donald F. Turner, The Durability, Relevance, and Future of American Antitrust Policy, 75 CAL. L. REV. 797, 800 (1987); see Frank H. Easterbrook, The Limits of Antitrust, 63 Tex. L. Rev. 1, 12-13 (1984) ("When everything is relevant, nothing is dispositive .... Litigation costs are the product of vague rules combined with high stakes, and nowhere is that combination more deadly than in antitrust litigation under the Rule of Reason").

Since *Professional Engineers* the Supreme Court has steadily moved away from the dichotomous approach -- under which every restraint of trade is either unlawful *per se*, and [\*\*\*12] hence not susceptible to a procompetitive justification, or subject to full-blown rule-of-reason analysis -- toward one in which the extent of the inquiry is tailored to the suspect conduct in each particular case. For instance, the Court did not hold unlawful *per se* an agreement limiting the number of football games each participating college could sell to television, which agreement was challenged in NCAA v. Board of Regents, 468 U.S. 85, 100, 82 L. Ed. 2d 70, 104 S. Ct. 2948 (1984) (recognizing but declining to apply doctrine that "horizontal price-fixing and output limitation are ordinarily condemned as a matter of law under an 'illegal per se' approach"); or the refusal of an organization of dentists to provide x-rays to dental insurers, which was at issue in IFD, 476 U.S. at 458 ("Although this Court has in the past stated that group boycotts are unlawful *per se*, we decline to resolve this case by forcing the Federation's policy into the 'boycott' pigeonhole and invoking the *per se* rule") (citations omitted). Compare, e.g., United States v. Socony-Vacuum Oil Co., 310 U.S. 150, 84 L. Ed. 1129, 60 S. Ct. 811 (1940) (price-fixing *per* [\*\*\*13] *se* unlawful); and Klor's, Inc. v. Broadway-Hale Stores, Inc., 359 U.S. 207, 3 L. Ed. 2d 741, [\*35] [\*373] 79 S. Ct. 705 (1959) (group boycott *per se* unlawful).

At the same time, however, in *NCAA* and *IFD* the Court did not insist upon the elaborate market analysis ordinarily required under the rule of reason to prove the defendant had market power and the restraint it imposed had an anticompetitive effect. See NCAA, 468 U.S. at 109-10 (rule of reason analysis unnecessary in light of district court's finding price and output not responsive to demand); IFD, 476 U.S. at 459 ("While this is not price fixing as such, no elaborate industry analysis is required to demonstrate the anticompetitive character of such an agreement"). The Court instead adopted an intermediate inquiry, since dubbed the "quick look," to evaluate horizontal restraints of trade. See, e.g., Areeda & Hovenkamp, Antitrust Law, P1911a.

It would be somewhat misleading, however, to say the "quick look" is just a new category of analysis intermediate in complexity between "*per se*" condemnation and full-blown "rule of reason" treatment, for that would suggest the Court has [\*\*\*14] moved from a dichotomy to a trichotomy, when in fact it has backed away from any reliance upon fixed categories and toward a continuum. The Court said as much in *California Dental Association v. FTC*:

The truth is that our categories of analysis of anticompetitive effect are less fixed than terms like "*per se*," "quick look," and "rule of reason" tend to make them appear. We have recognized, for example, that there is

often no bright line separating *per se* from Rule of Reason analysis, since considerable inquiry into market conditions may be required before the application of any so-called "*per-se*" condemnation is justified.

[526 U.S. 756, 779, 143 L. Ed. 2d 935, 119 S. Ct. 1604 \(1999\).](#)

**HN4**[] Rather than focusing upon the category to which a particular restraint should be assigned, therefore, the Court emphasized the basic point that under [§ 1](#) the essential inquiry is "whether ... the challenged restraint enhances competition." *Id. at 779-80* (quoting [NCAA, 468 U.S. at 104](#)). In order to make that determination, a court must make "an enquiry meet for the case, looking to the circumstances, details, and logic of a restraint," *id. at 781*, which in [\*\*\*15] some cases may not require a full-blown market analysis. The Court continued:

The object is to see whether the experience of the market has been so clear, or necessarily will be, that a confident conclusion about the principle tendency of a restriction will follow from a quick (or at least quicker) look, in place of a more sedulous one. And of course what we see may vary over time, if rule-of-reason analyses in case after case reach identical conclusions.

*Id.*; cf. [United States v. Microsoft, 346 U.S. App. D.C. 330, 253 F.3d 34, 84 \(D.C. Cir. 2001\)](#) (declining to condemn *per se* tying arrangements involving platform software products because there was "no close parallel in prior antitrust cases" and "simplistic application of *per se* tying rules carries a serious risk of harm").

In this case, as we have said, the Commission analyzed PolyGram's conduct under the legal framework it had devised in *Mass. Board* (1988), which it maintains is consistent with the Supreme Court's teaching of more than a decade later in *California Dental* (1999). FTC Op. at 28-29. The *Mass. Board* analysis proceeds in several distinct steps: First, the Commission [\*\*\*16] must determine whether it is obvious from the nature of the challenged conduct that it will likely harm consumers. If so, then the restraint is deemed "inherently [<sup>\*</sup>36] [\*\*374] suspect" and, unless the defendant comes forward with some plausible (and legally cognizable) competitive justification for the restraint, summarily condemned. "Such justifications," the Commission explained, "may consist of plausible reasons why practices that are competitively suspect as a general matter may not be expected to have adverse consequences in the context of the particular market in question, or they may consist of reasons why the practices are likely to have beneficial effects for consumers." *Id. at 29*.

If the defendant does offer such an explanation, then the Commission "must address the justification" in one of two ways. First, the Commission may explain why it can confidently conclude, without adducing evidence, that the restraint very likely harmed consumers. *Id. at 33-34*. Alternatively, the Commission may provide the tribunal with sufficient evidence to show that anticompetitive effects are in fact likely. *Id. at 33*. If the Commission succeeds in either way, then the evidentiary burden shifts [\*\*\*17] to the defendant to show the restraint in fact does not harm consumers or has "procompetitive virtues" that outweigh its burden upon consumers. *Id. at 34 n.45*.

PolyGram argues the Commission's framework conflicts with Supreme Court precedent by condemning a restraint that is not *per se* illegal without the Commission having to prove the restraint actually harms competition. According to PolyGram, "proof of actual anticompetitive effect (or market power as its surrogate) is required in *any* Rule of Reason case."

For reasons we have already explained, we reject PolyGram's attempt to locate the appropriate analysis, and the concomitant burden of proof, by reference to the vestigial line separating *per se* analysis from the rule of reason. See Areeda & Hovenkamp, [Antitrust Law](#), P1511a ("judges and litigants too often assume erroneously that the classification, *per se* or rule of reason, necessarily determines what must or may be alleged and proved, made the subject of detailed findings, or submitted to the jury"). **HN5**[] At bottom, the [Sherman Act](#) requires the court to ascertain whether the challenged restraint hinders competition; the Commission's framework, at least as [\*\*\*18] the Commission applied it in this case, does just that.

We therefore accept the Commission's analytical framework. **HN6**[] If, based upon economic learning and the experience of the market, it is obvious that a restraint of trade likely impairs competition, then the restraint is presumed unlawful and, in order to avoid liability, the defendant must either identify some reason the restraint is unlikely to harm consumers or identify some competitive benefit that plausibly offsets the apparent or anticipated

harm. That much follows from the caselaw; for instance, in *NCAA* the Court held that a "naked restraint on price and output requires some competitive justification even in the absence of a detailed market analysis." [468 U.S. at 110](#). Similarly, in *IFD*, the Supreme Court ruled a horizontal agreement to withhold services could not be sustained because the dentists failed to advance any "credible argument" that "some countervailing procompetitive virtue ... [redeemed] an agreement limiting consumer choice by impeding the 'ordinary give and take of the market place.'" [476 U.S. at 459](#); see also [California Dental, 526 U.S. at 771](#) (remanding for [\*\*\*19] closer look at challenged advertising restrictions after concluding they "might plausibly be thought to have a net procompetitive effect, or possibly no effect at all on competition").

Although the Commission uses the term "inherently suspect" to describe those restraints that judicial experience and economic [\*37] [\*\*375] learning have shown to be likely to harm consumers, see FTC Op. at 29, we note that, under the Commission's own framework, the rebuttable presumption of illegality arises not necessarily from anything "inherent" in a business practice but from the close family resemblance between the suspect practice and another practice that already stands convicted in the court of consumer welfare. The Commission appears to acknowledge, as it must, that as economic learning and market experience evolve, so too will the class of restraints subject to summary adjudication. See [California Dental, 526 U.S. at 781](#) (the ability of a court to draw "a confident conclusion about the principal tendency of a restraint ... may vary over time, if rule-of-reason analyses in case after case reach identical conclusions); see also [Broad. Music, Inc. v. CBS, 441 U.S. 1, 9, 60 L. Ed. 2d 1, 99 S. Ct. 1551 \(1979\)](#) [\*\*\*20] ("it is only after considerable experience with certain business relationships that courts classify them as *per se* violations"). See generally INDUSTRIAL CONCENTRATION: THE NEW LEARNING (Harvey J. Goldschmid, H. Michael Mann, J. Fred Weston, eds., 1974).

That said, we have no difficulty with the Commission's conclusion that PolyGram's agreement with Warner in all likelihood had a deleterious effect upon consumers -- unless, that is, PolyGram comes forward with some plausible explanation to the contrary. An agreement between joint venturers to restrain price cutting and advertising with respect to products not part of the joint venture looks suspiciously like a naked price fixing agreement between competitors, which would ordinarily be condemned as *per se* unlawful. The Supreme Court has recognized time and again that agreements restraining autonomy in pricing and advertising impede the "ordinary give and take of the market place." [IFD, 476 U.S. at 459](#); see also [NCAA, 468 U.S. at 107](#) ("restrictions on price and output are the paradigmatic examples of restraints of trade that the Sherman Act was intended to prohibit"); [Bates v. State Bar of Ariz., 433 U.S. 350, 364, 53 L. Ed. 2d 810, 97 S. Ct. 2691 \(1977\)](#) [\*\*\*21] (advertising "serves to inform the public of the availability, nature, and prices of products and services, and thus performs an indispensable role in the allocation of resources in a free enterprise system").

PolyGram's fate in this case therefore rests upon the plausibility of the sole competitive justification it proffered for the moratorium agreement, namely, that the restrictions on discounting and advertising enhanced the long-term profitability of all three concert albums and promoted the "Three Tenors" brand. According to PolyGram, each company was concerned the other would "free ride" on the promotional activities of the joint venture by promoting its own earlier concert album; as a result fewer Three Tenors albums would be sold overall and the joint venture would be less likely to create future products, such as a "greatest hits" album or a boxed set. Thus, PolyGram likens the moratorium agreement here to the restraint at issue in [Polk Brothers, Inc. v. Forest City Enterprises, 776 F.2d 185 \(7th Cir. 1985\)](#), where two potential retail competitors collaborated to build a store offering some of each company's products but agreed not to sell competing products [\*\*\*22] at the new store. Because the restraint arguably promoted productivity and output by controlling each participant's ability to free-ride on the other's promotional efforts, the court, rather than condemning the restraint summarily, went on to evaluate it under the rule of reason. [Id. at 190](#).

At first glance PolyGram's contention has some force; the moratorium appears likely to have mitigated the "spillover" effects that could be expected to follow an [\*38] [\*\*376] aggressive launch of the 1998 album. Absent the moratorium, that is, a consumer, after learning of the new album through the joint venture's advertising, might decide that he would be just as happy with an older concert album, especially if the older album were then available at a discount. The "free-riding" to be eliminated by the moratorium agreement, however, was nothing more than the competition of products that were not part of the joint undertaking. Why not an agreement by which PolyGram and

Warner would eliminate advertising and price competition on all their records for a time while they focused exclusively upon promoting the new Three Tenors album? The "procompetitive" justification PolyGram offers is "nothing [\*\*\*23] less than a frontal assault on the basic policy of the Sherman Act." *Nat'l Soc'y of Prof'l Engineers, 435 U.S. at 695.*

To take the Commission's example, if General Motors were vigorously to advertise the release of a new model SUV, other SUV manufacturers would no doubt reap some of the benefit of GM's efforts. FTC Op. at 43. But that would not mean General Motors and its competitors could lawfully agree to restrict prices and advertising on existing SUV models in return for General Motors giving its rivals a share of its profit on the new model. Nor would an agreement to restrain prices and advertising on existing SUVs be lawful if General Motors were to release the new model SUV as a joint venture with one of its competitors. *Id.* at 45. **HN7**<sup>↑</sup> A restraint cannot be justified solely on the ground that it increases the profitability of the enterprise that introduces the new product, regardless whether that enterprise is a joint venture or a solo undertaking. And it simply does not matter whether the new SUV would have been profitable absent the restraint; if the only way a new product can profitably be introduced is to restrain the legitimate competition of older products, [\*\*\*24] then one must seriously wonder whether consumers are genuinely benefitted by the new product. As the Supreme Court said in *Catalano, Inc. v. Target Sales, Inc., 446 U.S. 643, 649, 64 L. Ed. 2d 580, 100 S. Ct. 1925 (1980),*

**HN8**<sup>↑</sup> in any case in which competitors are able to increase the price level or to curtail production by agreement, it could be argued that the agreement has the effect of making the market more attractive to potential new entrants. If that potential justifies horizontal agreements among competitors imposing one kind of voluntary restraint or another on their competitive freedom, it would seem to follow that the more successful an agreement is in raising the price level, the safer it is from antitrust attack. Nothing could be more inconsistent with our cases.

See also *Law v. NCAA, 134 F.3d 1010, 1023 (10th Cir. 1998)* ("While increasing output, creating operating efficiencies, making a new product available, enhancing service or quality, and widening consumer choice have been accepted by courts as justifications for otherwise anticompetitive agreements, mere profitability or cost savings have not qualified as a defense under the antitrust [\*\*\*25] laws").

In sum, because PolyGram has failed to identify any competitive justification for its agreement with Warner to refrain from advertising or discounting their competitive Three Tenors products, we hold it violated § 5 of the FTC Act. Hence, we need not go on to determine whether the Commission's findings of fact concerning actual competitive harm are supported by substantial evidence.

Finally, we hold the remedy ordered by the Commission was reasonable. The Commission found there was a significant risk that, if not prohibited from doing so, PolyGram would enter into similar arrangements [\*39] [\*\*377] in the future. That determination is supported by substantial evidence. The record shows the condition that gave rise to the moratorium agreement -- namely, the company "feared that a new release by one of [its] recording artists may lose sales to the artist's older albums owned by a competitor," FTC Op. at 59 -- is a recurrent one in the record industry; therefore, PolyGram would have the same incentive in the future to enter into other agreements to restrain advertising and price discounting.

### III. Conclusion

For the foregoing reasons, PolyGram's petition for review [\*\*\*26] is

*Denied.*

## Kendall v. Visa U.S.A. Inc.

United States District Court for the Northern District of California

July 25, 2005, Decided

No. C 04-04276 JSW

**Reporter**

2005 U.S. Dist. LEXIS 21449 \*; 2005 WL 2216941

SHERI L. KENDALL, et al., Plaintiffs, v. VISA U.S.A. INC., et al., Defendants.

**Subsequent History:** Claim dismissed by, Motion to strike granted by [Kendall v. Visa U.S.A., Inc., 2005 U.S. Dist. LEXIS 21450 \(N.D. Cal., July 25, 2005\)](#)

**Prior History:** [Kendall v. Visa U.S.A., Inc., 2005 U.S. Dist. LEXIS 53690 \(N.D. Cal., Mar. 29, 2005\)](#)

## Core Terms

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allegations, Sherman Act, merchant, banks, discount, motion to dismiss, Consortiums, interchange, antitrust, acquiring, leave to amend, card

## LexisNexis® Headnotes

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Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### [HN1](#) [] Motions to Dismiss, Failure to State Claim

A motion to dismiss for failure to state a claim will be denied unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him or her to relief.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### [HN2](#) [] Motions to Dismiss, Failure to State Claim

On a motion to dismiss for failure to state a claim, all allegations of material fact are taken as true and construed in the light most favorable to the nonmoving party.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN3** Motions to Dismiss, Failure to State Claim

Dismissal is proper only where there is no cognizable legal theory or an absence of sufficient facts alleged to support a cognizable legal theory.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN4** Motions to Dismiss, Failure to State Claim

On a motion to dismiss for failure to state a claim, the court is not bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation.

Antitrust & Trade Law > Regulated Practices > Private Actions > General Overview

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Antitrust & Trade Law > Sherman Act > General Overview

### **HN5** Regulated Practices, Private Actions

For private antitrust claims, if the facts do not at least outline or adumbrate a violation of the Sherman Antitrust Act, [15 U.S.C.S. § 1](#), the plaintiffs will get nowhere merely by dressing them up in the language of antitrust.

Antitrust & Trade Law > Sherman Act > General Overview

### **HN6** Antitrust & Trade Law, Sherman Act

To state a claim under [§ 1](#) of the Sherman Antitrust Act, [15 U.S.C.S. § 1](#), plaintiffs must allege: (1) an agreement or conspiracy among two or more persons or distinct business entities; (2) by which the persons or entities intended to harm or restrain competition; and (3) which actually injures competition.

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > Sherman Act > General Overview

### **HN7** Sherman Act, Claims

To prevail on a [§ 1](#) Sherman Antitrust Act, [15 U.S.C.S. § 1](#), claim, a plaintiff must establish a conscious commitment to a common scheme designed to achieve an unlawful result.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN8** Motions to Dismiss, Failure to State Claim

Plaintiffs may not simply recite legal conclusions in an effort to state a claim.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

#### [HN9](#) [↓] Motions to Dismiss, Failure to State Claim

A court is not bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegations.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

#### [HN10](#) [↓] Antitrust & Trade Law, Sherman Act

A claimant must, at a minimum, sketch the outline of the antitrust violation with allegations of supporting factual detail.

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

#### [HN11](#) [↓] Price Discrimination, Defenses

No general principle of antitrust law forbids charging different prices to different customers.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > General Overview

#### [HN12](#) [↓] Private Actions, Remedies

Threatened antitrust injury is a prerequisite to equitable relief.

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**Judges:** JEFFREY S. WHITE, UNITED STATES DISTRICT JUDGE.

**Opinion by:** JEFFREY S. WHITE

## Opinion

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### ORDER GRANTING BANK DEFENDANTS' SECOND MOTION TO DISMISS WITHOUT LEAVE TO AMEND

Now before the Court is the second motion of defendants Bank of America, N.A., Wells Fargo Bank, N.A., and U.S. Bank, N.A. (the "Bank Defendants") to dismiss each of Plaintiffs' claims against them pursuant to [Rule 12\(b\)\(6\) of the Federal Rules of Civil Procedure](#). Having carefully read the parties' papers and considered the arguments and the relevant legal authority, the Court hereby GRANTS the Bank Defendants' motion to dismiss Plaintiffs' claims against them without leave to amend.

### BACKGROUND

Plaintiffs are various merchant, retail and service businesses [\*3] who bring this action against Mastercard International, Inc. ("MASTERCARD"), VISA U.S.A., Inc. ("VISA"), and the Bank Defendants, who are credit card issuing and/or acquiring banks (collectively "Defendants"). Through their member banks, VISA and MASTERCARD issue various forms of payment cards. Member banks can issue VISA or MASTERCARD payment cards to consumers and set interest rates, fees, and other terms for cardholders. (First Amended Complaint ("FAC"), PP 8-11.) Member banks also individually contract with retailers on behalf of VISA or MASTERCARD to purchase payment card transactions. *Id.* Member banks may function as either "issuing" banks or "acquiring" banks, or both. *Id.*

Plaintiffs' claims are directed at payment card transaction fees, which include a "merchant discount fee," which is the transaction fee between the merchant and the acquiring bank, and an "interchange fee," which is the transaction fee between the acquiring bank and the issuing bank. (*Id.*, PP 16-18.) In their first amended complaint, Plaintiffs allege that Defendants' act of setting merchant discount and interchange fees amounts to horizontal price fixing under Section 1 of the Sherman Antitrust [\*4] Act ("Sherman Act"), [15 U.S.C. § 1](#). Plaintiffs again allege that Defendants' conduct violates Section 16 of the Clayton Act, [15 U.S.C. § 26](#).

The Bank Defendants moved to dismiss the original complaint, challenging the sufficiency of Plaintiffs' allegations against them on the ground that Plaintiffs failed to allege the requisite anti-competitive conduct necessary to state a claim under [Section 1](#) of the Sherman Act. In its order granting the Bank Defendants' first motion to dismiss, the Court found that the allegations in the original complaint were insufficient to state a claim under [Section 1](#) because they did not allege an agreement, combination, or conspiracy by the Bank Defendants to fix prices. See Order dated March 29, 2005 ("Order") at 3, citing [Les Shockley Racing, Inc. v. National Hot Rod Ass'n, 884 F.2d 504, 507 \(9th Cir. 1989\)](#).

On April 25, 2005, Plaintiffs filed an amended complaint. On June 3, 2005, the Bank Defendants moved to dismiss. The Court heard oral argument on the motion on July 8, 2005.

## DISCUSSION

### A. Legal Standard on Motion to Dismiss.

**HN1**[<sup>1</sup>] A motion to dismiss for failure to [\*5] state a claim will be denied unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him or her to relief. *Conley v. Gibson*, 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957). **HN2**[<sup>1</sup>] All allegations of material fact are taken as true and construed in the light most favorable to the nonmoving party. *Cahill v. Liberty Mut. Ins. Co.*, 80 F.3d 336, 337-38 (9th Cir. 1996). **HN3**[<sup>1</sup>] Dismissal is proper only where there is no cognizable legal theory or an absence of sufficient facts alleged to support a cognizable legal theory. *Navarro v. Block*, 250 F.3d 729, 732 (9th Cir. 2001). **HN4**[<sup>1</sup>] The Court is not, however, bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation. *Papasan v. Allain*, 478 U.S. 265, 286, 92 L. Ed. 2d 209, 106 S. Ct. 2932 (1986); *Arpin v. Santa Clara Transp. Agency*, 261 F.3d 912, 923 (9th Cir. 2001) (internal quotation omitted). **HN5**[<sup>1</sup>] For private antitrust claims, if the facts "do not at least outline or adumbrate a violation of the Sherman Act, the plaintiffs will get nowhere merely by dressing them up in the language of antitrust." *Rutman Wine Co. v. E&J Gallo Winery*, 829 F.2d 729, 736 (9th Cir. 1987). [\*6]

### B. Section 1 Sherman Act Claim.

**HN6**[<sup>1</sup>] To state a claim under *Section 1* of the Sherman Act, Plaintiffs must allege: (1) an agreement or conspiracy among two or more persons or distinct business entities; (2) by which the persons or entities intended to harm or restrain competition; and (3) which actually injures competition. *Les Shockley Racing*, 884 F.2d at 507 (citations omitted); see also *Monsanto Co. v. Spray-Rite Serv. Corp.*, 465 U.S. 752, 764, 79 L. Ed. 2d 775, 104 S. Ct. 1464 (1984). **HN7**[<sup>1</sup>] (to prevail on a *Section 1* Sherman Act claim, a plaintiff must establish a "conscious commitment to a common scheme designed to achieve an unlawful result").

Plaintiffs have failed to remedy the deficiencies identified by the Court in its prior order. The Court stated clearly that the original complaint failed to allege that the Bank Defendants conspired or agreed to fix merchant discount or interchange fees, and explicitly stated that the allegations concerning the setting of a floor for the merchant discount fee did not, standing alone, constitute unlawful conduct on the part of the Bank Defendants. See Order at 4. In their amended complaint, Plaintiffs now allege that: [\*7] (1) the Defendant Banks charge to Plaintiffs and other merchants "the amount of the interchange rate fixed by the Consortiums [VISA and MASTERCARD] as the merchant discount fee"; (2) the Defendant Banks adopt the interchange fees set by the Consortiums; (3) the acquiring banks "knowingly, intentionally and actively participated in an individual capacity with the Consortiums in following these fees"; and (4) there is an agreement among all financial institutions to charge a minimum merchant discount set by the Consortiums. (See FAC,-PP 8, 14, 11, 13(a).)

Plaintiffs contend that they have adequately alleged that the Bank Defendants "individually participated in setting the interchange fees with the Consortiums and then individually as an acquirer applied the particular category of fee to each of the merchants as a minimum discount fee." See Opp. Br. at 7. However, Plaintiffs have failed to allege that the Bank Defendants "knowingly, intentionally, and actively participated in an individual capacity" in setting those fees, as is required to state a claim under *Section 1*. See *Kline v. Coldwell, Banker & Co.*, 508 F.2d 226, 232 (9th Cir. 1974). **HN8**[<sup>1</sup>] Plaintiffs may [\*8] not simply recite legal conclusions in an effort to state a claim. See *Papasan*, 478 U.S. at 286; *Arpin*, 261 F.3d at 923 **HN9**[<sup>1</sup>] (a court is not bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegations). **HN10**[<sup>1</sup>] A claimant must, at a minimum, sketch the outline of the antitrust violation with allegations of supporting factual detail. See *Les Shockley*, 884 F.2d at 508; see also *Rutman Wine Co.*, 829 F.2d at 736.

Contrary to Plaintiffs' contentions, the foregoing revised allegations are insufficient to state a claim against the Bank Defendants under *Section 1* because they still fail to allege an agreement, combination, or conspiracy by the Bank

Defendants to fix prices. See [Les Shockley, 884 F.2d at 507](#). In other words, there are no allegations that, as part of the Bank Defendants' participation in the management of, or their proprietary interest in, VISA or MASTERCARD, the Bank Defendants "knowingly, intentionally and actively participated in an individual capacity in the alleged scheme" to fix the interchange fee or the merchant discount fee. Merely charging, adopting [\*9] or following the fees allegedly set by the Consortiums is insufficient as a matter of law to state a claim under [Section 1](#) of the Sherman Act.<sup>1</sup>

[\*10] To the extent Plaintiffs attempt to aver an independent third cause of action for violation of [Section 1](#) of the Sherman Act under a "consortium marketing" theory, this allegation fails for the same reasons stated herein. The allegations relating to price differentials between customers does not state a claim for an antitrust violation. See [Zoslaw v. MCA Distrib. Corp., 693 F.2d 870, 887 \(9th Cir. 1982\)](#); [USM Corp. v. SPS Technologies, Inc., 694 F.2d 505, 512 \(7th Cir. 1982\)](#) [HN11](#) [↑] ("No general principle of [antitrust law](#) forbids charging different prices to different customers").

Based on the foregoing, Plaintiffs' [Section 1](#) Sherman Act claims against the Bank Defendants are DISMISSED without leave to amend.

### C. Section 16 Clayton Act Claim.

Because Plaintiffs' have failed to state a claim under [Section 1](#) of Sherman Act against the Bank Defendants', Plaintiffs' fourth claim for relief, under [Section 16](#) of the Clayton Act, [15 U.S.C. § 26](#), predicated upon a violation [Section 1](#) of the Sherman Act, is also dismissed without leave to amend. [Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 109, 93 L. Ed. 2d 427, 107 S. Ct. 484 \(1986\)](#) [\*11] [HN12](#) [↑] (threatened antitrust injury is a prerequisite to equitable relief); see also [Lucas Auto. Eng'g, 140 F.3d 1228, 1234-35](#).

## CONCLUSION

For the foregoing reasons, the Bank Defendants' motion to dismiss is GRANTED without leave to amend.

## IT IS SO ORDERED.

Dated: July 25, 2005

/s/ Jeffrey S. White

UNITED STATES DISTRICT JUDGE

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<sup>1</sup> In this regard, Plaintiffs' somewhat premature motion for leave to file a motion for reconsideration of this Order indicates that a number of members of the Board of Directors of the Consortiums is comprised of bank members. (See Sheedy Deposition at 46-47; Jonas Deposition at 44-45). Plaintiffs, however, have still failed to allege that the bank members knowingly, intentionally or actively participated in the setting of the interchange fees and, after many opportunities to amend and to plead sufficient facts, Plaintiffs have again apparently conducted no discovery to demonstrate such necessary facts nor have they pled the requisite facts to establish a claim against the Bank Defendants. In addition, Plaintiffs were admonished by this Court upon granting the Bank Defendants' first motion to dismiss that Plaintiffs must conduct a reasonable inquiry of the underlying factual and legal grounds supporting their claims before amending. See Order at 4. Because the first amended complaint represents the fifth attempt to allege sufficient facts to support claims against the Defendant Banks (including the three complaints filed in Reyn's on the same basic theories and two attempts in this matter), the Court, in its discretion, finds that amendment under these particular circumstances would be futile and grants the present motion without leave to amend.

## Kendall v. Visa U.S.A., Inc.

United States District Court for the Northern District of California

July 25, 2005, Decided

No. C 04-04276 JSW

**Reporter**

2005 U.S. Dist. LEXIS 21450 \*

SHERI L. KENDALL, et al., Plaintiffs, v. VISA U.S.A. INC., et al., Defendants.

**Subsequent History:** Affirmed by [Kendall v. Visa U.S.A., 2008 U.S. App. LEXIS 5032 \(9th Cir. Cal., Mar. 7, 2008\)](#)

**Prior History:** [Kendall v. Visa U.S.A. Inc., 2005 U.S. Dist. LEXIS 21449 \(N.D. Cal., July 25, 2005\)](#)

## Core Terms

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merchant, discount, acquirers, Consortiums, antitrust, interchange, purchasers, allegations, card, discount rate, amended complaint, motion to dismiss, cause of action, Sherman Act, indirect, banks, indirectly, estoppel, conclusory allegation, prior litigation, leave to amend, collateral, overcharge, network, member bank

## LexisNexis® Headnotes

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Banking Law > Bank Activities > General Overview

Immigration Law > Admission of Immigrants & Nonimmigrants > Visa Eligibility & Issuance > Issuance of Visas

### [HN1](#) Banking Law, Bank Activities

In a credit card system, the issuing bank rather than the merchant bears the risk of nonpayment by the cardholder.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### [HN2](#) Motions to Dismiss, Failure to State Claim

A motion to dismiss for failure to state a claim will be denied unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him or her to relief. All allegations of material fact are taken as true and construed in the light most favorable to the nonmoving party. Dismissal is proper only where there is no cognizable legal theory or an absence of sufficient facts alleged to support a cognizable legal theory. The court is not, however, bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation.

Antitrust & Trade Law > Regulated Practices > Private Actions > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

### **HN3** **Regulated Practices, Private Actions**

For private antitrust claims, if the facts do not at least outline or adumbrate a violation of the Sherman Antitrust Act, [15 U.S.C.S. § 1 et seq.](#), the plaintiffs will get nowhere merely by dressing them up in the language of antitrust.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Strike > Immaterial Matters

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > General Overview

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Strike > General Overview

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Strike > Redundant Matters

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Strike > Scandalous Matters

### **HN4** **Motions to Strike, Immaterial Matters**

[Fed. R. Civ. P. 12\(f\)](#) provides that a court may order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent, or scandalous matter. Immaterial matter is that which has no essential or important relationship to the claim for relief or the defenses being pleaded. Impertinent material consists of statements that do not pertain, or are not necessary to the issues in question. Motions to strike are regarded with disfavor because they are often used as delaying tactics and because of the limited importance of pleadings in federal practice. The possibility that issues will be unnecessarily complicated or that superfluous pleadings will cause the trier of fact to draw unwarranted inferences at trial is the type of prejudice that is sufficient to support the granting of a motion to strike.

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

### **HN5** **Private Actions, Standing**

The United States Supreme Court in Illinois Brick, in an effort to increase effectiveness and deterrent power of private treble damages suits which are vital to the enforcement of the antitrust laws, has held that recovery for damage incurred by indirect purchasers is barred. The Court has held that permitting the use of pass-on theories essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge from direct purchasers to middlemen to ultimate consumers. However appealing that attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness. Courts are not permitted to determine what portion of an illegal overcharge was passed on and what part was absorbed by the middlemen because such an analysis would involve all the evidentiary and economic complexities that Illinois Brick clearly forbade.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## **HN6** Motions to Dismiss, Failure to State Claim

Dismissal of claims is proper where there is an absence of facts alleged sufficient to support a cognizable legal theory. The court is not bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation. For purposes of deciding a motion to dismiss, the court does not have to accept every allegation in the complaint as true in considering the sufficiency of the allegations; rather, the court should examine whether conclusory allegations follow from the description of facts as alleged by the plaintiff.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN7** Estoppel, Collateral Estoppel

Collateral estoppel bars the relitigation of an issue that is: (1) identical to an issue; (2) actually litigated and decided in prior litigation; when (3) the determination of the issue in the prior litigation was critical and necessary to support the judgment rendered in the prior litigation. The burden to demonstrate the presence of those elements is on the party seeking to establish collateral estoppel effect. Further, the factors are applied strictly. It is not sufficient that an issue is factually similar to the one in an earlier case; to satisfy the collateral estoppel factors, the issues must be identical and involve the same facts and surrounding context.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

## **HN8** Purchasers, Direct Purchasers

Indirect purchasers can sue for damages if there is no realistic possibility that the direct purchaser will sue over the antitrust violation.

Antitrust & Trade Law > Sherman Act > General Overview

## **HN9** Antitrust & Trade Law, Sherman Act

The allegation of price differentials between customers does not state a claim for an antitrust violation.

**Counsel:** [\*1] For Sheri L. Kendall, doing business as Bala Hair Salon, James Maser, Maiz Holding Company, on Behalf of Themselves & All Others Similarly Situated doing business as Picante Cocina Restaurant, Plaintiffs:

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For Mastercard International, Inc., Defendant: Gianluca Morello, Jay Neil Fastow, Debra J. Pearlstein, Weil, Gotshal & Manges LLP, New York, NY; Nancy Karen Raber, Clifford Chance US LLP, Palo Alto, CA; Wesley Railey Powell, Hunton & Williams LLP, New York, NY; Keila Doris Ravelo, Clifford Chance US LLP, New York, NY.

For Bank of America, N.A., a subsidiary of Bank of America Corporation, Defendant: Sonya D. Winner, Tara M. Steeley, Covington & Burling, San Francisco, CA.

For Wells Fargo Bank, N.A., a subsidiary of Wells Fargo & Company, Defendant: J. Thomas Rosch, Joshua N. Holian, Latham & Watkins, San Francisco, CA.

For U.S. Bank, N.A., a subsidiary of U.S. Bancorp, Defendant: Michael C. Lueder, Maurice J. McSweeney, Foley & Lardner [\*2] LLP, Milwaukee, WI; Eileen R. Ridley, Foley & Lardner, San Francisco, CA.

For Jasa, Inc., Jasperson Sod Service, Randall Jasperson, Rookies, Inc., Miscellaneous: Kevin K. Eng, Markun Zusman & Compton LLP, San Francisco, CA.

**Judges:** JEFFREY S. WHITE, UNITED STATES DISTRICT JUDGE.

**Opinion by:** JEFFREY S. WHITE

## **Opinion**

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### **ORDER GRANTING VISA U.S.A. INC.'S AND MASTERCARD'S MOTIONS TO DISMISS WITHOUT LEAVE TO AMEND**

Now before the Court are the motions of defendant VISA U.S.A. Inc. ("VISA") and defendant MasterCard International Incorporated ("MASTERCARD") to dismiss and/or to strike each of Plaintiffs' claims against them pursuant to [Rule 12\(b\)\(6\)](#) and [12\(f\)](#) of the Federal Rules of Civil Procedure. Having carefully read the parties' papers and considered the arguments and the relevant legal authority, the Court hereby GRANTS VISA's and MASTERCARD's motions to dismiss Plaintiffs' claims without leave to amend.

### **BACKGROUND**

Plaintiffs are various merchant, retail and service businesses who bring this action against VISA, MASTERCARD, and the Bank Defendants, who are credit card issuing and/or acquiring banks (collectively, "Defendants"). Through their member banks, VISA and MASTERCARD [\*3] (for ease of reference, the network defendants are referred to herein as "the Consortiums") issue various forms of payment cards. Member banks can issue VISA or MASTERCARD payment cards to consumers and set interest rates, fees, and other terms for cardholders. (First Amended Complaint ("FAC"), 118-11.) Member banks also individually contract with retailers on behalf of VISA or MASTERCARD to purchase payment card transactions. *Id.* Member banks may function as either "issuing" banks or "acquiring" banks, or both. *Id.*

When a customer pays with a payment card, the "acquiring" bank purchases the payment card receipt (or electronic equivalent) from the retailer for the amount of payment less a "merchant discount fee." Through the VISA or MASTERCARD system, the acquiring bank then receives reimbursement from the cardholder's "issuing" bank for the purchase price less an "interchange fee" - a preset fee consented to by all issuing and acquiring banks on the VISA or MASTERCARD network. The issuing bank then profits by the amount of the interchange fee, while the acquiring bank profits by the amount of the merchant discount fee less the interchange fee. [HN1](#)[ In a credit card

system, the [\*4] issuing bank rather than the merchant bears the risk of nonpayment by the cardholder. See [National Bancard Corp. \(NaBanco\) v. Visa U.S.A., Inc.](#), 779 F.2d 592, 595 (11th Cir. 1986).

Plaintiffs' claims are directed at payment card transaction fees. In their first amended complaint, Plaintiffs allege that Defendants' conduct in setting merchant discount and interchange fees amounts to horizontal price fixing under Section 1 of the Sherman Antitrust Act ("Sherman Act"), [15 U.S.C. § 1](#). Plaintiffs again allege that Defendants' conduct violates [Section 16](#) of the Clayton Act, [15 U.S.C. § 26](#).

VISA moves to dismiss the amended complaint and/or to strike certain allegations pursuant to [Federal Rules of Civil Procedure 12\(b\)\(6\)](#) and [12\(f\)](#). VISA contends that the first and second causes of action are barred by [Illinois Brick v. Illinois](#), 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977), the third cause of action fails to state a claim, and the fourth cause of action does not provide an independent ground for relief.

MASTERCARD moves to dismiss the amended complaint on the basis that Plaintiffs lack standing to [\*5] assert the first and second causes of action for violations of [Section 1](#) of the Sherman Act based on the alleged fixing of the interchange fee and the "Citigroup allegation," that the third cause of action fails to state an independent antitrust claim, and that the fourth cause of action fails to provide a basis for injunctive relief for a violation of another [antitrust law](#).

Because the issues raised in both VISA and MASTERCARD's motions to dismiss overlap significantly, the Court will address the substance of the two motions together, and delineate the differences where appropriate.

## DISCUSSION

### A. Legal Standard on Motion to Dismiss and Motion to Strike.

[HN2](#) A motion to dismiss for failure to state a claim will be denied unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him or her to relief. [Conley v. Gibson](#), 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957). All allegations of material fact are taken as true and construed in the light most favorable to the nonmoving party. [Cahill v. Liberty Mut. Ins. Co.](#), 80 F.3d 336, 337-38 (9th Cir. 1996). Dismissal is proper only where there is no cognizable legal [\*6] theory or an absence of sufficient facts alleged to support a cognizable legal theory. [Navarro v. Block](#), 250 F.3d 729, 732 (9th Cir. 2001). The Court is not, however, bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation.

[Papasan v. Allain](#), 478 U.S. 265, 286, 92 L. Ed. 2d 209, 106 S. Ct. 2932 (1986); [Arpin v. Santa Clara Transp. Agency](#), 261 F.3d 912, 923 (9th Cir. 2001) (internal quotation omitted). [HN3](#) For private antitrust claims, if the facts "do not at least outline or adumbrate a violation of the Sherman Act, the plaintiffs will get nowhere merely by dressing them up in the language of antitrust." [Rutman Wine Co. v. E&J Gallo Winery](#), 829 F.2d 729, 736 (9th Cir. 1987).

[Federal Rule of Civil Procedure 12\(f\)](#) provides that [HN4](#) a court may "order stricken from any pleading any insufficient defense or any redundant, immaterial, impertinent, or scandalous matter." Immaterial matter "is that which has no essential or important relationship to the claim for relief or the defenses being pleaded." [Cal. Dep't of Toxic Substances Control v. Alco Pac., Inc.](#), 217 F. Supp. 2d 1028, 1032 (C.D. Cal. 2002) [\*7] (internal citations and quotations omitted). Impertinent material "consists of statements that do not pertain, or are not necessary to the issues in question." *Id.* Motions to strike are regarded with disfavor because they are often used as delaying tactics and because of the limited importance of pleadings in federal practice. [Colaprico v. Sun Microsystems Inc.](#), 758 F. Supp. 1335, 1339 (N.D. Cal. 1991). The possibility that issues will be unnecessarily complicated or that superfluous pleadings will cause the trier of fact to draw unwarranted inferences at trial is the type of prejudice that is sufficient to support the granting of a motion to strike. [Cal. Dept. of Toxic Substances Control](#), 217 F. Supp. at 1028.

## B. Standing Under Section 1 of the Sherman Act.

**[HN5]** The Supreme Court in *Illinois Brick*, in an effort to "increase effectiveness and deterrent power [of] private treble damages suits [which are] vital to the enforcement of the antitrust laws," held that recovery for damage incurred by "indirect purchasers" is barred. *Illinois Brick*, 431 U.S. at 736; see also *Royal Printing Co. v. Kimberly-Clark Corp.*, 621 F.2d 323, 325-26 (9th Cir. 1980). [\*8] The Court held that permitting the use of pass-on theories "essentially would transform treble-damages actions into massive efforts to apportion the recovery among all potential plaintiffs that could have absorbed part of the overcharge from direct purchasers to middlemen to ultimate consumers. However appealing this attempt to allocate the overcharge might seem in theory, it would add whole new dimensions of complexity to treble-damages suits and seriously undermine their effectiveness." *Illinois Brick*, 431 U.S. at 737. Courts are not permitted to determine "what portion of [an] illegal overcharge was 'passed on' . . . and what part was absorbed by the middlemen" because such an analysis would "involve all the evidentiary and economic complexities that *Illinois Brick* clearly forbade." *Royal Printing*, 621 F.2d at 327; see also *Lucas Auto. Eng'g, Inc. v. Bridgestone/Firestone, Inc.*, 140 F.3d 1228, 1233 (9th Cir. 1998) ("The indirect purchaser rules serves to avoid the complications of apportioning overcharges between direct and indirect purchasers and to eliminate multiple recoveries.")<sup>1</sup>

### [\*9] 1. Allegations That the Consortiums Indirectly Set Merchant Discount Fees.

In their amended complaint, Plaintiffs attempt to aver that VISA and MASTERCARD somehow, indirectly, set the merchant discount fees. However, viewed in context, each allegation is constructed on the premise that VISA's and MASTERCARD's interchange fee sets the minimum, or floor, for the merchant discount fee. (See, e.g., FAC P8 ("a minimum merchant discount fee . . . is established, both directly and indirectly, by the Consortiums"); P9 (merchants are charged by the acquiring banks "the amount of the interchange rate fixed by the Consortiums as the minimum merchant discount fee"); P11 ("a merchant discount fee . . . is established, both directly and indirectly, by the Consortiums. Most of the merchant discount fee is the interchange rate which is established by the Consortiums.") (citation omitted).)

Plaintiffs' damages theory is based therefore on the allegation that the Consortiums set the interchange fee to acquirers who then pass it along to merchants as a component of what Plaintiffs allege to be inflated merchant discount rates. To the extent Plaintiffs contend that therefore the Consortiums [\*10] "indirectly" set the merchant discount rates, those claims are precluded by operation of the *Illinois Brick* bar on recovery for indirect purchasers. See *Illinois Brick*, 431 U.S. at 746; see also *Kansas v. Utilicorp United Inc.*, 497 U.S. 199, 216, 111 L. Ed. 2d 169, 110 S. Ct. 2807 (1990) (holding that there was no exception to *Illinois Brick* even where the direct purchaser almost certainly passed on the entire cost of alleged overcharge to the indirect purchaser); see also *In re Coordinated Pretrial Proceedings in Petroleum Prods. Antitrust Litig.*, 691 F.2d 1335, 1342 (9th Cir. 1982) ("indirect purchasers

<sup>1</sup> In their original complaint in this matter, Plaintiffs alleged that VISA and MASTERCARD set only the interchange fee, which then "established" the basis or floor for the merchant discount rates. (See Complaint, P21(a).) Plaintiffs lack standing to assert such claims because they have not suffered the requisite antitrust injury from the Consortiums' setting of the interchange rate. See, e.g., *Associated General Contractors of Cal., Inc. v. State Council of Carpenters*, 459 U.S. 519, 539, 74 L. Ed. 2d 723, 103 S. Ct. 897 (1983) (plaintiff failed to demonstrate requisite antitrust injury because it was "neither a consumer nor a competitor in the market in which the trade was restrained."); see also *Cargill, Inc. v. Monfort of Colorado, Inc.*, 479 U.S. 104, 113, 93 L. Ed. 2d 427, 107 S. Ct. 484 (1986) ("a private plaintiff must allege threatened loss or damage 'of the type the antitrust laws were designed to prevent and that flows from that which makes defendants' acts unlawful.'") (citing *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977)).

This contention is the independent basis for much of MASTERCARD's current motion to dismiss. To the extent Plaintiffs' claims are premised upon the setting only of the interchange fee, MASTERCARD's argument is well-taken. However, the First Amended Complaint alleges that the Consortiums set, either directly or indirectly, the merchant discount rate, which, for the purpose of resolving the pending motions, is the more troubling of the allegations now before the Court.

of price-fixed goods may not maintain an antitrust damage action for overcharges passed on to them by direct purchasers from the defendant.")

## **2. Allegations That the Consortiums Directly Set Merchant Discount Fees.**

In addition to the claims of indirect control over the merchant discount rates which are expressly precluded by the holding in *Illinois Brick*, Plaintiffs attempt to aver that VISA and MASTERCARD directly set the merchant discount rates. (See, e.g., FAC PP8-11, 16 ("minimum merchant discount fee ... is established [\*11] . . . directly . . . by the Consortiums").)

First, in order to avoid the bar of *Illinois Brick*, Plaintiffs cannot allege that VISA and MASTERCARD directly negotiate with certain merchants to promote the Consortiums' acceptance in the marketplace. Plaintiffs have expressly excluded from the class all "merchants who negotiate merchant discounts directly with VISA and/or MASTERCARD or receive payments directly from them." (FAC, P16.) Those merchants that directly negotiate with the networks are explicitly excluded from the class of Plaintiffs and therefore, are not currently before the Court alleging an antitrust injury for the direct setting of the merchant discount rates by VISA or MASTERCARD.

Second, to the extent that Plaintiffs aver that the Consortiums directly set the merchant discount rates for those merchants in the plaintiff class, those allegations are conclusory. [HN6](#) Dismissal of claims is proper where there is an absence of facts alleged sufficient to support a cognizable legal theory. [Navarro](#), 250 F.3d at 732. The Court is not bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation. See, e.g., [Papasan](#), 478 U.S. at 286; [\*12] [Arpin](#), 261 F.3d at 923. For purposes of deciding a motion to dismiss, the Court does not have to accept every allegation in the complaint as true in considering the sufficiency of the allegations; rather, the Court should examine whether conclusory allegations follow from the description of facts as alleged by the plaintiff. See [Holden v. Hagopian](#), 978 F.2d 1115, 1121 (9th Cir. 1992).

In context, each time Plaintiffs aver that the Consortiums set the merchant discount fees directly, Plaintiffs quote *United States v. VISA U.S.A., Inc.* ("VISA I") in which the Southern District of New York court stated "merchant acceptance of a card brand is also defined and controlled at the system level and the merchant discount rate is established, directly and indirectly, by the networks." [163 F. Supp. 2d 322, 338 \(S.D. N.Y. 2001\)](#) (citing the trial and deposition transcripts before that court); see FAC, PP8-11.

### **a. Estoppel Effect of Statement in *VISA I*.**

Plaintiffs cite the decision by the New York court as evidence that the merchant discount fee is established, directly or indirectly, by the Consortiums. Plaintiffs, however, [\*13] cannot rely on the collateral estoppel effect of the statement in that matter. [HN7](#) Collateral estoppel bars the relitigation of an issue that is (1) identical to an issue (2) actually litigated and decided in prior litigation, when (3) the determination of the issue in the prior litigation was critical and necessary to support the judgment rendered in the prior litigation. [Pool Water Prods. v. Olin Corp.](#), 258 F.3d 1024, 1031 (9th Cir. 2001). The burden to demonstrate the presence of these elements is on the party seeking to establish collateral estoppel effect. [Id. at 1033](#). Further, the factors are applied strictly. It is not sufficient that an issue is "factually similar" to the one in an earlier case; to satisfy the collateral estoppel factors, the issues must be "identical" and involve the same facts and surrounding context. [Western Oil & Gas Ass'n v. United States EPA](#), 633 F.2d 803, 809 (9th Cir. 1980).

Having failed to come forward with any showing to establish that the elements of the collateral estoppel doctrine are satisfied, the Court cannot rely on the brief statement made in *VISA I* on the factually complex record before [\*14] it in order to determine the veracity of the conclusory allegations presented here. It is not clear from the opinion of the New York court that the issue was even contested by the parties or that it was actually litigated. See, e.g., *Gospel Missions v. City of Los Angeles*, 328 F.3d 548, 553 (9th Cir. 2003) (rejecting collateral estoppel argument where prior issue was "neither framed in the pleadings nor contested by the parties" in the earlier litigation). The context of the court's determination and the record before that court are completely different from the context and record presented to this Court. There has been no showing that the issues are identical, that they were actually litigated

and decided in the prior litigation, or that the determination of the issue in the prior litigation was critical and necessary to support the judgment rendered in the prior litigation. See [Pool Water Prods., 258 F.3d at 1031](#). Therefore, the statement in the VISA / opinion has no preclusive effect on this Court. See [id. at 1030-31](#).<sup>2</sup>

**[\*15] b. The Factual Record Does Not Support Plaintiffs' Theory.**

Lastly, the Court was urged by both parties to examine closely the record before the Court as presented in conjunction with the motions for summary judgment, to determine whether the Court should grant leave to amend with regard to the conclusory allegations in the amended complaint. Having reviewed the evidence submitted with the pending summary judgment motions, the Court is satisfied that the factual record does not support Plaintiffs' claims that the Consortiums directly set the merchant discount fees. The uncontested evidence demonstrates that neither VISA nor MASTERCARD are directly involved in the setting of the merchant discount rates. (See Declaration of William Sheedy in Support of VISA's Motion for Summary Judgment ("Sheedy Decl."), P17 ("the merchant discount fee is the fee set by Visa acquirers and/or their designated third-parties, in their sole discretion based on agreement with their merchants, and in competition with other Visa acquirers"), P18 ("Merchant discount fees are negotiated only between merchants and acquirers, and not with Visa."), P19 ("It is certainly the case that IRF [interchange [\*16] reimbursement fee] is a cost that acquirers typically seek to recover in the overall fees they charge merchants and thus IRF generally has an impact on merchant discount rates. But it is only one of a number of costs acquirers face, including costs for terminal deployment, risk management, customer service, marketing and sales - to name a few."), P20 ("Visa does not set these merchant discount fees. My understanding is that the extent to which acquirers can generate an appropriate revenue stream while recovering these various costs, including IRF, varies greatly and depends upon the particular acquirer and the particular merchant. The way in which acquirers recover their costs and generate revenue is entirely within their discretion."). See also Declaration of Steven Jonas in Support of MASTERCARD's Motion for Summary Judgment ("Jonas Decl."), P15 ("MasterCard does not set any acquirer's merchant discount fee; the acquirers set the merchant discount fees, which are agreed to by merchants in contracts between merchants and their acquirers. Further, MasterCard has no input into whether or how an acquirer factors any interchange fee amount into its merchant discount fee level."). [\*17] )

Because the essential facts demonstrating that neither VISA nor MASTERCARD set the merchant discount fee are uncontested, and having given Plaintiffs adequate opportunity to contest those facts in conjunction with the pending motions for summary judgment, the Court is satisfied that the factual record fails to support Plaintiffs' conclusory allegations in the First Amended Complaint that the Consortiums directly set the merchant discount fee.<sup>3</sup>

**[\*18] 4. Exceptions to *Illinois Brick* Do Not Apply.**

Arguing only that Plaintiffs have averred in the amended complaint that the Consortiums set the merchant discount rates directly, Plaintiffs fail to address whether an exception to the rule set out in *Illinois Brick* applies in this matter. [HN8](#) Indirect purchasers can sue for damages if there is no "realistic possibility that the direct purchaser will sue" over the antitrust violation. [Freeman v. San Diego Ass'n of Realtors, 322 F.3d 1133, 1145 \(9th Cir. 2003\)](#) (citing [Royal Printing Co. v. Kimberly-Clark Corp., 621 F.2d 323, 326 \(9th Cir. 1980\)](#)). During oral argument on

<sup>2</sup> In this regard, without converting the current motion before the Court to a motion for summary judgment, the Court has reviewed the full evidentiary record presented by the parties in their motions for summary judgment. Although the motions for summary judgment filed by VISA and MASTERCARD, which are fully briefed and set for hearing on August 19, 2005, will not be necessary as the Court by this order will dismiss the case, the Court has substantively reviewed those motions and the evidence submitted in conjunction therein for purposes of resolving the current motions.

<sup>3</sup> The failure of Plaintiffs to come forward with any evidence to the contrary also dictates that this Court grant the pending motions to dismiss without leave to amend. It is clear from the record before this Court that Plaintiffs have failed to demonstrate that they have standing to sue and have failed to garner evidence which would enable them to generate a sufficient basis for the Court to find standing should leave be granted. Because the first amended complaint represents the fifth attempt to allege sufficient claims (three complaints filed in Reyn's and two attempts in this matter), and because, after development of the factual record, Plaintiffs are still unable to marshal sufficient facts to confer standing, the Court finds in its discretion that amendment in this particular context would be futile and grants the present motions without leave to amend.

these motions, the parties were specifically asked to address the issue of what entity would have standing to make an antitrust claim against the Consortiums should the Court find that Plaintiffs lack standing. Plaintiffs failed to address the question directly, and merely reiterated the holding in *Freeman*. The Consortiums contended that the acquiring banks would have standing to sue on an antitrust theory regarding the incorporation of the set interchange fee in the passed on merchant discount fees. Although the record reflects [\*19] that a number of the members of the Board of Directors of the Consortiums is comprised of bank members,<sup>4</sup> there are apparently on the order of 8,000 acquirers in the VISA network and 9,000 members in the MASTERCARD network, a large portion of which are acquiring banks. (Sheedy Decl., P3; Jonas Decl., P4.) Certainly, any number of those banks could sue and would be granted standing to do so.

In addition, the Court notes that processing agents for the member banks have standing to sue and could make, in essence, the claims alleged herein. In this regard, the Court takes judicial notice of claims against VISA by First Data Corporation, currently pending before the undersigned, a lawsuit which contains, *inter alia*, allegations of antitrust violations with regard to the setting of interchange rates.<sup>5</sup>

#### **[\*20] C. Third Cause of Action Fails to State a Claim Upon Which Relief May Be Granted.**

To the extent Plaintiffs attempt to aver an independent third cause of action for violation of [Section 1](#) of the Sherman Act under a "consortium marketing" theory, this allegation fails for the same reasons stated herein. [HN9](#)[  
↑] The allegation of price differentials between customers does not state a claim for an antitrust violation. See [Zoslaw v. MCA Distrib. Corp.](#), 693 F.2d 870, 887 (9th Cir. 1982); [USM Corp. v. SPS Technologies, Inc.](#), 694 F.2d 505, 512 (7th Cir. 1982) ("No general principle of antitrust law forbids charging different prices to different customers").

Based on the foregoing, Plaintiffs' [Section 1](#) Sherman Act claims against VISA and MASTERCARD are DISMISSED without leave to amend.

#### **D. CitiGroup Allegations Are Stricken.**

MASTERCARD moves against paragraph 15 of the amended complaint, which concerns the allegations that the 1997 proposal by the CEO of CitiGroup to merge the processes of clearing and settlement of payment cards with the clearing and settlement of checks was rejected.

Although MASTERCARD's motion, properly a motion to strike, [\*21] is rendered moot by this Court's determination that the claims against the Consortiums must be dismissed, the motion is also GRANTED on the merits on the basis that, having no essential or important relationship to the claim for relief, such allegations are immaterial. See [California Dept. of Toxic Substance Control](#), 217 F. Supp. 2d at 1032. In addition, there is no indication that Plaintiffs have standing to make such a claim as the allegation concerns card issuers, not interchange, merchant acquirers or merchant discount fees. Accordingly, Plaintiffs cannot make a claim for antitrust injury for allegedly anticompetitive effects on issuers. See, e.g., [Associated General Contractors](#), 459 U.S. at 539 (plaintiff failed to demonstrate requisite antitrust injury because it was "neither a consumer nor a competitor in the market in which the trade was restrained."); see also [Cargill](#), 479 U.S. at 113. Such immaterial and baseless allegations are independently stricken.

#### **E. Section 16 Clayton Act Claim.**

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<sup>4</sup> See Sheedy Deposition at 46-47; Jonas Deposition at 44-45.

<sup>5</sup> See [VISA U.S.A., Inc. v. First Data Corporation, et al.](#), C02-1786 JSW; see also [National Bancard Corp. \(NaBanco\) v. VISA U.S.A., Inc.](#), 596 F. Supp. 1231 (S.D. Fla. 1984), aff'd, 779 F.2d 592 (11th Cir. 1986).

Because Plaintiffs' have failed to state a claim under Section 1 of Sherman Act against VISA, Plaintiffs' fourth claim for relief, [\*22] under Section 16 of the Clayton Act, 15 U.S.C. § 26, predicated upon a violation Section 1 of the Sherman Act, is also dismissed without leave to amend. See Cargill, Inc. v. Monfort of Colo., Inc., 479 U.S. 104, 109, 93 L. Ed. 2d 427, 107 S. Ct. 484 (1986) (threatened antitrust injury is a prerequisite to equitable relief); see also Lucas Auto. Eng'g, 140 F.3d at 1234-35.

## **CONCLUSION**

For the foregoing reasons, VISA's and MASTERCARD's motions to dismiss and/or to strike are GRANTED without leave to amend.

## **IT IS SO ORDERED.**

Dated: July 25, 2005

/s/ JEFFREY S. WHITE

UNITED STATES DISTRICT JUDGE

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## People's Choice Wireless, Inc. v. Verizon Wireless

Court of Appeal of California, Second Appellate District, Division Two

July 28, 2005, Filed

B175179

### **Reporter**

131 Cal. App. 4th 656 \*; 31 Cal. Rptr. 3d 819 \*\*; 2005 Cal. App. LEXIS 1183 \*\*\*; 2005 Cal. Daily Op. Service 6701

PEOPLE'S CHOICE WIRELESS, INC., et al., Plaintiffs and Appellants, v. VERIZON WIRELESS, Defendant and Respondent.

**Prior History:** [\*\*\*1] Superior Court of Los Angeles County, No. BC291811, Charles W. McCoy, Jr., Judge.

## **Core Terms**

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independent dealer, cellular telephone, customers, dealers, machines, holdback, anti trust law, consumer, brand, manufacturers, new model, price competition, antitrust, fulfilled, sales, service contract, relevant market, territorial, discount, warranty, allegations, selling, models, prices, competitors, intrabrand, demurrer, monopoly, service provider, monopoly power

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### **HN1** **Regulated Practices, Trade Practices & Unfair Competition**

See [Cal. Bus. & Prof. Code § 17203.](#)

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Responses > Defenses, Demurrs & Objections > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrs & Objections > Demurrs

### **HN2** **Standards of Review, De Novo Review**

When a complaint has been disposed of via demurrer, appellate review is de novo. The appellate court treats a demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law. The court also considers matters which may be judicially noticed. Further, the court gives the complaint a reasonable interpretation, reading it as a whole and its parts in their context. When a demurrer is sustained, the court determines whether the complaint states facts sufficient to constitute a cause of action.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

### **HN3** [down] **Private Actions, Remedies**

Injury to a competitor is not equivalent to injury to competition; only the latter is the proper focus of antitrust laws.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview

Business & Corporate Law > Distributorships & Franchises > Causes of Action > Restraints of Trade

Antitrust & Trade Law > Sherman Act > General Overview

### **HN4** [down] **Price Fixing & Restraints of Trade, Horizontal Refusals to Deal**

Subject to antitrust laws such as the Sherman Act, there is a long recognized right of a trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal. Refusal to deal is not an unqualified right. Still, the United States Supreme Court has been very cautious in recognizing exceptions, because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single company.

Antitrust & Trade Law > Sherman Act > General Overview

Criminal Law & Procedure > Sentencing > Fines

### **HN5** [down] **Antitrust & Trade Law, Sherman Act**

See [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > Sherman Act > Defenses

Tax Law > ... > Sales & Exchanges > Related Party Transactions > Fifty Percent Ownership

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Tax Law > ... > Sales & Exchanges > Related Party Transactions > General Overview

### **HN6** [down] **Sherman Act, Defenses**

The offense of monopoly under [15 U.S.C.S. § 2](#) of the Sherman Act has two elements: (1) the possession of monopoly power in the relevant market; and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident. One brand does not necessarily constitute a relevant market if substitutes are available. The second element requires the use of monopoly power to foreclose competition, to gain a competitive advantage, or to destroy a competitor. [Section 2](#) prohibits a monopolist's unilateral action if that conduct harms the competitive process in the absence of a legitimate business justification.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

#### [HN7](#) Price Fixing & Restraints of Trade, Horizontal Refusals to Deal

The mere refusal to deal does not violate the spirit or policy of [antitrust law](#). Antitrust policy attempts to balance the benefits of protecting and fostering economic incentives for entrepreneurs to pursue business with the benefits procured for consumers when courts manage markets.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

#### [HN8](#) Antitrust & Trade Law, Sherman Act

[15 U.S.C.S. § 1](#) of the Sherman Act reaches unreasonable restraints of trade effected by a contract, combination or conspiracy between separate entities. It does not reach conduct that is wholly unilateral. A parent and its wholly-owned subsidiaries are considered a single economic entity for purposes of the Sherman Act.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

#### [HN9](#) Antitrust & Trade Law, Sherman Act

See [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

#### [HN10](#) Price Fixing & Restraints of Trade, Vertical Restraints

Vertically imposed territorial restrictions normally have the potential for creating, simultaneously, benefits and detriments to competition. Such restraints typically inhibit the dealers in a given brand of product from competing against other dealers in the same brand; hence intrabrand competition is reduced. But these restraints may also

achieve efficiencies that stimulate competition between brands. In assessing whether a violation had occurred, a court has to weigh any enhancement of interbrand competition against the restrictive effect on intrabrand competition, determine whether the restraints were, in all the circumstances, reasonable, and look to the history of the restraint itself, to the problem perceived by the manufacturer and the goal sought to be achieved, and to the actual effect of the restraint.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

### **HN11**[ **Monopolies & Monopolization, Actual Monopolization**

Concerted activity subject to [15 U.S.C.S. § 1](#) is judged more sternly than unilateral activity under [15 U.S.C.S. § 2](#). This is largely because there are countervailing policies involved with [§ 2](#). The Sherman Act contains a basic distinction between concerted and independent action. The conduct of a single firm is governed by [§ 2](#) alone and is unlawful only when it threatens actual monopolization. It is not enough that a single firm appears to restrain trade unreasonably, for even a vigorous competitor may leave that impression. For instance, an efficient firm may capture unsatisfied customers from an inefficient rival, whose own ability to compete may suffer as a result. This is the rule of the marketplace and is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster. In part because it is sometimes difficult to distinguish robust competition from conduct with long-run anticompetitive effects, Congress has authorized Sherman Act scrutiny of single firms only when they pose a danger of monopolization. Judging unilateral conduct in this manner reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Law > ... > Duties & Liabilities > Causes of Action & Remedies > Compensatory Damages

### **HN12**[ **Regulated Practices, Trade Practices & Unfair Competition**

[Cal. Bus. & Prof. Code § 17203](#) can apply even if a defendant has not violated the antitrust laws.

## **Headnotes/Summary**

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### **Summary**

#### CALIFORNIA OFFICIAL REPORTS SUMMARY

The trial court sustained a cellular telephone company's demurrer without leave to amend in an action by independent dealers of cellular telephones that alleged that the company engaged in unfair competition under [Bus. & Prof. Code, § 17203](#). The independent dealers claimed that the company engaged in unfair competition by refusing to sell popular, new cellular telephone models to them during an extended holdback period and by selling cellular telephones to customers below cost in certain circumstances when the independent dealers could not afford to compete. (Superior Court of Los Angeles County, No. BC291811, Charles W. McCoy, Jr., Judge.)

The Court of Appeal affirmed, holding that the allegations failed to demonstrate that the effect of the company's conduct was comparable to or the same as a violation of the antitrust laws. Unless there was an exception, the right to refuse to deal remained sacrosanct. Accordingly, the mere refusal to deal did not violate the spirit or policy of

**antitrust law.** The allegations also failed to demonstrate that the company's conduct otherwise significantly threatened or harmed competition. Although there might have been a reduction in intrabrand competition regarding some of the company's cellular telephones for short periods of time, there was no reduction in interbrand competition. Furthermore, although the company's conduct had injured the independent dealers, injury to competitors was not the same thing as injury to competition, and the court could only consider the latter. The company's conduct did not pose an evil because it and its stores were viewed as a single entity, and because it did not possess a monopoly and was not threatening a monopoly. The court was aware of no case or statute, state or federal, which contained a policy that would force a company to either let its competitors have all of a particular category of sales, or force it to prop up its competitors financially. (Opinion by Ashmann-Gerst, J., with Doi Todd, Acting P. J., and Nott, J., \* concurring.)

[\*657]

## Headnotes

### CA(1) [1] (1)

#### **Appellate Review § 128—Scope of Review—De Novo—Function of Appellate Court—Rulings on Demurrers.**

When a complaint has been disposed of via demurrer, appellate review is de novo. The appellate court treats a demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law. The court also considers matters which may be judicially noticed. Further, the court gives the complaint a reasonable interpretation, reading it as a whole and its parts in their context. When a demurrer is sustained, the court determines whether the complaint states facts sufficient to constitute a cause of action.

### CA(2) [2] (2)

#### **Unfair Competition § 1—Violation of Antitrust Laws or Harm to Competition.**

A cellular phone company's demurrer to independent dealers' unfair competition action under Bus. & Prof. Code, § 17203, was properly sustained because the dealers' allegations that the company engaged in unfair competition by refusing to sell popular new cellular phone models to them during an extended holdback period and by selling cellular phones to customers below cost in certain circumstances when the dealers could not afford to compete, failed to demonstrate that the company's conduct violated the policy or spirit of the antitrust laws or that its conduct otherwise significantly threatened or harmed competition. Injury to a competitor was not equivalent to injury to competition; only the latter was the proper focus of antitrust laws.[b].]

[13 Witkin, Summary of Cal. Law (10th ed. 2005) Equity, § 123; 1 Witkin, Summary of Cal. Law (9th ed. 1987) Contracts, §§ 560, 575; Simon et al., Matthew Bender Practice Guide: Cal. Unfair Competition and Business Torts (2005) § 2.11[3]

### CA(3) [3] (3)

#### **Monopolies and Restraints of Trade § 4—Refusal to Deal—Particular Agreements and Combinations—Sherman Act.**

Subject to antitrust laws such as the Sherman Act, there is a long-recognized right of a trader or manufacturer engaged in an entirely private business, freely to exercise its own independent discretion as to parties with whom it

\* Retired Associate Justice of the Court of Appeal, Second Appellate District, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.

will deal. Refusal to deal is not an unqualified right. Still, the United States Supreme Court has been very cautious in recognizing exceptions, because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single company.

#### CA(4) (4)

##### **Monopolies and Restraints of Trade § 4—Monopoly Elements—Particular Agreements and Combinations—Sherman Act.**

The offense of monopoly under [15 U.S.C. § 2](#), section 2 of the Sherman Act [**\*658**] has two elements: (1) the possession of monopoly power in the relevant market; and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident. One brand does not necessarily constitute a relevant market if substitutes are available. The second element requires the use of monopoly power to foreclose competition, to gain a competitive advantage, or to destroy a competitor. [Section 2](#) prohibits a monopolist's unilateral action if that conduct harms the competitive process in the absence of a legitimate business justification.

#### CA(5) (5)

##### **Monopolies and Restraints of Trade § 1—Refusal to Deal—No Violation of *Antitrust Law*.**

The mere refusal to deal does not violate the spirit or policy of *antitrust law*. Antitrust policy attempts to balance the benefits of protecting and fostering economic incentives for entrepreneurs to pursue business with the benefits procured for consumers when courts manage markets.

#### CA(6) (6)

##### **Monopolies and Restraints of Trade § 4—Parent and Wholly Owned Subsidiaries—Particular Agreements and Combinations—Sherman Act.**

[15 U.S.C. § 1](#), the Sherman Act, reaches unreasonable restraints of trade effected by a contract, combination or conspiracy between separate entities. It does not reach conduct that is wholly unilateral. A parent and its wholly owned subsidiaries are considered a single economic entity for purposes of the Sherman Act.

#### CA(7) (7)

##### **Monopolies and Restraints of Trade § 1—Vertically Imposed Territorial Restrictions—Intrabrand and Interbrand Competition.**

Vertically imposed territorial restrictions normally have the potential for creating, simultaneously, benefits and detriments to competition. Such restraints typically inhibit the dealers in a given brand of product from competing against other dealers in the same brand; hence intrabrand competition is reduced. But these restraints may also achieve efficiencies that stimulate competition between brands. In assessing whether a violation had occurred, a court has to weigh any enhancement of interbrand competition against the restrictive effect on intrabrand competition, determine whether the restraints were, in all the circumstances, reasonable, and look to the history of the restraint itself, to the problem perceived by the manufacturer and the goal sought to be achieved, and to the actual effect of the restraint.

#### CA(8) (8)

**Monopolies and Restraints of Trade § 4—Concerted and Unilateral Activity—Particular Agreements and Combinations—Sherman Act.**

Concerted activity subject to [15 U.S.C. § 1](#) is judged more sternly [[\\*659](#)] than unilateral activity under [15 U.S.C. § 2](#). This is largely because there are countervailing policies involved with [§ 2](#). The Sherman Act contains a basic distinction between concerted and independent action. The conduct of a single firm is governed by [§ 2](#) alone and is unlawful only when it threatens actual monopolization. It is not enough that a single firm appears to restrain trade unreasonably, for even a vigorous competitor may leave that impression. For instance, an efficient firm may capture unsatisfied customers from an inefficient rival, whose own ability to compete may suffer as a result. This is the rule of the marketplace and is precisely the sort of competition that promotes the consumer interests that the Sherman Act aims to foster. In part because it is sometimes difficult to distinguish robust competition from conduct with long-run anticompetitive effects, Congress has authorized Sherman Act scrutiny of single firms only when they pose a danger of monopolization. Judging unilateral conduct in this manner reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur.

[CA\(9\)A](#) [9] (9)

**Unfair Competition § 1—Application.**

[Bus. & Prof. Code, § 17203](#), can apply even if a defendant has not violated the antitrust laws.

**Counsel:** Blecher & Collins, Maxwell M. Blecher and Matthew E. Hess for Plaintiffs and Appellants.

Overland Borenstein Scheper & Kim, Diann H. Kim and Wendy O. Clendening for Defendant and Respondent.

**Judges:** Ashmann-Gerst, J., with Doi Todd, Acting P.J., and Nott, J., concurring.

**Opinion by:** ASHMANN-GERST

## Opinion

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[\*\*820] **ASHMANN-GERST, J.**—Appellants People's Choice Wireless, Inc., and Cellular Depot, Inc., sued respondent Verizon Wireless (Verizon) for unfair competition pursuant to [Business and Professions Code section 17203](#)<sup>1</sup> on behalf of themselves and similarly situated independent dealers of cellular telephones (collectively, the Independent Dealers). In their first amended complaint (the complaint), the Independent Dealers alleged that Verizon engaged in unfair competition by: (1) refusing to sell popular new cellular [[\\*660](#)] telephone models to the Independent [\[\\*\\*821\]](#) Dealers during an extended holdback period; and (2) selling cellular [\[\\*\\*2\]](#) telephones to customers below cost in certain circumstances when the Independent Dealers could not afford to compete. According to the Independent Dealers, the trial court erred when it sustained Verizon's demurrer without leave to amend. We have reviewed the complaint and the law and find no error.

We affirm.

## FACTS

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<sup>1</sup> All further statutory references are to the Business and Professions Code unless otherwise indicated. [Section 17203](#) provides, in relevant part: “[HN1A](#) Any person who engages, has engaged, or proposes to engage in unfair competition may be enjoined in any court of competent jurisdiction.”

*The Complaint*

The Independent Dealers alleged: Because cellular telephones are expensive, service providers such as Verizon sell them below cost if a consumer agrees to purchase telephone service for a set period of time, usually one to three years. Similarly, service providers often subsidize the cost if a customer wishes to upgrade to a new cellular telephone. Verizon sells cellular telephones through [\*\*\*3] its wholly owned retail stores and retail stores operated by the Independent Dealers.

At Verizon's request, companies such as Motorola, Nokia and Sony manufacture cellular telephone models that are solely compatible with Verizon's telephone network. The manufacturers agree to sell new models to Verizon on an exclusive basis for a specified period of time, normally three to six months (the exclusive period). During the exclusive period, the Independent Dealers cannot purchase new models from the manufacturers, but they can purchase new models directly from Verizon. Most consumer sales occur within the exclusive period during the first one to two months of when a new model is released.

The Independent Dealers match the prices being charged for cellular telephones in the Verizon stores. Above and beyond that, the Independent Dealers provide customers who purchase a cellular telephone with several useful accessories, such as headsets or carrying cases, at no additional cost. If a customer wanted to purchase these same accessories at a Verizon store, the customer would have to pay extra. By providing free accessories to their customers, the Independent Dealers undercut Verizon's prices [\*\*\*4] and create price competition.

*Count I*

In the past, within the exclusive period, Verizon imposed a two-week holdback period on its most popular new cellular telephones models. During [\*661] this holdback period, Verizon released its most popular new models to Verizon's retail stores but not to the Independent Dealers. As a result, the Independent Dealers could not sell the most popular new models of Verizon's cellular telephones for the first two weeks of their release. Then, when the Motorola T720 was released for sale, Verizon extended the holdback period to two months. For the Blackberry 6750, Verizon extended the holdback for a period of time that exceeded four months and was continuing as of the date the complaint was filed. Verizon claims that the holdback period is necessary for quality control. The true purpose is to ensure that Verizon's retail stores obtain the majority of sales for popular new models. Verizon heavily advertises the availability of popular new models during the holdback period. Once the holdback period ends, Verizon's advertising ceases almost entirely. The Independent Dealers depend on new model sales for a majority of their income and are adversely impacted [\*\*\*5] by the holdback period. Moreover, if they were given access to the models subject to the holdback period on the same terms as the Verizon stores, they would match Verizon's prices, offer free accessories and undercut [\*\*822] Verizon's prices. As a practical matter, the holdback period prevents price competition and is therefore violative of [section 17200 et seq.](#)

*Count II*

Until recently, Verizon's commission structure placed the Independent Dealers on an equal footing with Verizon's wholly owned retail stores. Verizon subsidized the cost of new cellular telephones only for those customers who had fulfilled at least one year of their service contract. On a parallel basis, Verizon's authorized wholesale distributors paid a commission to the Independent Dealers whenever they obtained service contract renewals from customers who had fulfilled at least one year of their existing service contract. The Independent Dealers were able to use their service contract renewal commissions to partially offset the cost of new cellular telephones and then price those new models to match the prices being charged for the same models in Verizon's stores. In December 2002, Verizon began subsidizing all [\*\*\*6] new cellular telephone sales, even sales to customers who had not fulfilled a least one year of their service contract. Verizon did not, however, change its commission structure for the Independent Dealers. Without commissions on sales to customers who fulfilled less than one year of their service contracts, the Independent Dealers cannot subsidize the cost of new cellular telephones to those customers.

Verizon's commission structure reduces intrabrand competition, discriminates against the Independent Dealers, and amounts to unfair competition.

### [\*662] The Demurrer and This Appeal

Verizon demurred to the complaint on the grounds, *inter alia*, that the allegations did not satisfy the test set forth by [Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co. \(1999\) 20 Cal.4th 163 \[83 Cal.Rptr.2d 548, 973 P.2d 527\]](#) (*Cel-Tech*). The trial court sustained the demurrer without leave to amend and the Independent Dealers noticed this appeal. Because there was no judgment, the clerk of the Court of Appeal informed the Independent Dealers that the Court of Appeal lacked jurisdiction. Thereafter, in order to perfect appellate jurisdiction, the parties stipulated that the action was dismissed [\*\*\*7] and judgment entered in favor of Verizon. The stipulation was filed and the trial court ordered that it be given legal effect.

## STANDARD OF REVIEW

**CA(1)** [1] (1) [HN2](#) When a complaint has been disposed of via demurrer, our review is *de novo*. In other words, “ ‘[w]e treat [a] demurrer as admitting all material facts properly pleaded, but not contentions, deductions or conclusions of fact or law. [Citation.] We also consider matters which may be judicially noticed.’ [Citation.] Further, we give the complaint a reasonable interpretation, reading it as a whole and its parts in their context. [Citation.] When a demurrer is sustained, we determine whether the complaint states facts sufficient to constitute a cause of action. [Citation.]” ([Zelig v. County of Los Angeles \(2002\) 27 Cal.4th 1112, 1126 \[119 Cal.Rptr.2d 709, 45 P.3d 1171\]](#).)

## DISCUSSION

### 1. The holdback period.

**CA(2)** [2] (2) According to the Independent Dealers, the allegations in count I of the complaint satisfy two of the three possible grounds for finding conduct between competitors to be considered unfair pursuant to our Supreme Court's opinion in *Cel-Tech*. We are unable to concur with this assessment. As we shall discuss below, the [\*\*\*8] allegations fail to demonstrate either [\*\*\*823] that Verizon's conduct (1) violates the policy or spirit of the antitrust laws because the effect of the conduct is comparable to or the same as a violation of the antitrust laws, or (2) it otherwise significantly threatens or harms competition. ([Cel-Tech, supra, 20 Cal.4th at p. 187](#))<sup>2</sup> While expediting our duties, we have kept the following principle uppermost in our reasoning. [HN3](#) “Injury to a competitor is not [\*663] equivalent to injury to competition; only the latter is the proper focus of antitrust laws. [Citations.]” ([Cel-Tech, supra, 20 Cal.4th at p. 186](#).)

#### a. Violation of antitrust policies.

To kick off their argument, the Independent Dealers solicit [\*\*\*9] a comparison of this case to a refusal-to-deal case, [Eastman Kodak Co. v. Image Technical Services, Inc. \(1992\) 504 U.S. 451 \[119 L.Ed.2d 265, 112 S.Ct. 2072\]](#) (*Eastman Kodak*). Verizon parries with the contention that, with few exceptions, a company owes no duty to help anyone and is free to deal or not deal with a competitive rival.

<sup>2</sup> The third *Cel-Tech* ground is that the conduct threatens an incipient violation of the antitrust laws. We need not analyze this ground. The Independent Dealers freely admit that this is not an antitrust case under federal law or [section 16720 et seq.](#) (the Cartwright Act).

**CA(3) [↑]** (3) Indeed, Verizon is on target with the general rule. Nearly a century ago, the Supreme Court recognized that, **HN4 [↑]** subject to antitrust laws such as the Sherman Act,<sup>3</sup> there is a “long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal.” (*United States v. Colgate & Company* (1919) 250 U.S. 300, 307 [63 L.Ed. 992, 39 S.Ct. 465, 1919 Dec. Comm'r Pat. 460] (*Colgate*).) That theme has continued life. (See *Dimidowich v. Bell & Howell* (9th Cir. 1986) 803 F.2d 1473, 1478 [stating that a “manufacturer may choose those with whom it wishes to deal and unilaterally may refuse to deal with a distributor or customer for business reasons without running afoul of the antitrust laws”].)

[\*\*\*10] Recently, we were treated to the Supreme Court’s scholarship on the matter when it revisited *Colgate* and the *Sherman Act* to once again place its intellectual brackets on our land’s **antitrust law**. (See *Verizon Communications Inc. v. Law Offices of Curtis V. Trinko, LLP* (2004) 540 U.S. 398, 408 [157 L.Ed.2d 823, 124 S.Ct. 872] (*Verizon Communications*).) The Supreme Court explained that the “opportunity to charge monopoly prices—at least for a short period—is what attracts ‘business acumen’ in the first place; it induces risk taking that produces innovation and economic growth.” (*Id. at p. 407*.) Diligent companies, of course, are in a position to gain monopoly power by building an infrastructure that allows them to excel in business. Upon noting this market reality, the court segued into the following observation: “Compelling such [companies] to share the source of their advantage is in some tension with the underlying purpose of **antitrust law**, since it may lessen the incentive for the monopolist, the rival, or both to invest in those economically beneficial facilities. Enforced sharing also requires antitrust courts to act as central planners, identifying [\*\*\*11] the proper price, quantity, and other terms of dealing—a role for which they are ill-suited.” (*Id. at pp. 407–408*.) For this reason, the general rule expressed in *Colgate* remains a major policy point.

[\*\*824] [\*664] By the same token, the *Verizon Communications* court explained that refusal to deal is not an unqualified right. (*Verizon Communications, supra*, 540 U.S. at p. 408.) Still, the court has “been very cautious in recognizing … exceptions [to *Colgate*], because of the uncertain virtue of forced sharing and the difficulty of identifying and remedying anticompetitive conduct by a single [company].” (*Ibid.*) In the view of the Supreme Court, the leading case for liability based on refusal to deal is *Aspen Skiing Co. v. Aspen Highlands Skiing Corp.* (1985) 472 U.S. 585 [86 L.Ed.2d 467, 105 S.Ct. 2847] (*Aspen Skiing*), a cased cited in the Independent Dealers’ briefs. In *Aspen Skiing*, there was a ski locale comprised of four mountain areas. The defendant owned three of those areas, and the plaintiff owned one. For years, they cooperated by issuing joint, multiple-day, all-area ski tickets. When the plaintiff refused to give [\*\*\*12] the defendant a greater share of the proceeds, the defendant canceled the joint tickets. The plaintiff tried unsuccessfully to recreate the joint tickets, even offering to buy the defendant’s tickets at retail price. The Supreme Court upheld the jury’s verdict in favor of the plaintiff, concluding that the jury may well have found that the defendant was more interested in reducing competition than obtaining the short-run benefits of the joint tickets. (*Verizon Communications, supra*, 540 U.S. at pp. 408–409.) But the *Verizon Communications* court highlighted the fact that *Aspen Skiing* “is at or near the outer boundary of [title 15 United States Code section] 2 liability.” (*Verizon Communications, supra*, 540 U.S. at p. 409.)

Now that we are done with our preliminaries, we bring *Eastman Kodak* to the fore. The book on that case goes like this. Kodak was in the business of providing service and parts for its office equipment to its customers. It produced some of the parts itself, and the rest were made to order by independent original-equipment manufacturers (OEM’s). In the early 1980’s, independent service organizations (ISO’s) started [\*\*\*13] repairing and servicing Kodak equipment. As well, they sold parts and reconditioned Kodak machines. Soon thereafter, Kodak adopted a policy of limiting the availability of parts to the ISO’s. It sold replacement parts for micrographic and copying machines only to buyers of Kodak equipment who also purchased service from Kodak for any repair of those machines. There were a variety of corollaries. Kodak and the OEM’s agreed that the OEM’s would not sell parts to anyone but Kodak. Through pressure, Kodak convinced Kodak equipment owners and independent parts distributors to stop selling Kodak parts to the ISO’s. Last, Kodak implemented a plan to prevent others from

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<sup>3</sup> Title 15 United States Code section 1 et seq.

obtaining used Kodak machines. The intent behind Kodak's machinations regarding parts was to inhibit the ISO's ability to sell service for Kodak machines. (*Eastman Kodak, supra, 504 U.S. at pp. 455–459.*)

The ISO's sued under the *Sherman Act*, claiming that Kodak had unlawfully tied the sale of service for Kodak machines to the sale of parts, in [\*665] violation of title [15 United States Code section 1](#), and had unlawfully monopolized and attempted to monopolize the sale of service for Kodak machines, [\*\*\*14] in violation of title [15 United States Code section 2](#).<sup>4</sup> (*Eastman Kodak, \*\*8251 supra, 504 U.S. at p. 459.*) The district court granted summary judgment for Kodak, and the matter was reversed on appeal.

**CA(4)↑ (4)** Because the Independent Dealers do not allege a tying agreement, we focus on the portion of *Eastman Kodak* that discusses [section 2](#) of the *Sherman Act*. In affirming the reversal, the Supreme Court noted that [\*\*\*15] [HN6↑](#) the “ ‘offense of monopoly under [\[section\] 2](#) of the *Sherman Act* has two elements: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident.’ [Citation.]” (*Eastman Kodak, supra, 504 U.S. at p. 481.*) The fact that Kodak controlled nearly 100 percent of the parts market and 80 percent to 95 percent of the service market, with no readily available substitutes, was sufficient to suggest the existence of monopoly power. Kodak complained that, as a matter of law, a single brand of a product or service can never be a relevant market under the *Sherman Act*. The court disagreed. “The relevant market for antitrust purposes is determined by the choices available to Kodak equipment owners. [Citation.] Because service and parts for Kodak equipment are not interchangeable with other manufacturers' service and parts, the relevant market from the Kodak equipment owner's perspective is composed of only those companies that service Kodak machines. [Citation.] This Court's prior cases support [\*\*\*16] the proposition that in some instances one brand of a product can constitute a separate market. [Citations.] The proper market definition in this case can be determined only after a factual inquiry into the ‘commercial realities’ faced by consumers. [Citation.]” (*Eastman Kodak, supra, at pp. 481–482*, fn. omitted.) In a footnote, the court explained that *United States v. Du Pont & Co. (1956) 351 U.S. 377 [100 L.Ed. 1264, 76 S.Ct. 994]*, did not foreclose single brands from being a market. Rather, it merely held that “one brand does not necessarily constitute a relevant market if substitutes are available. [Citations.]” (*Eastman Kodak, supra, at p. 482, fn. 30.*)

With respect to the second element, which required “the use of monopoly power ‘to foreclose competition, to gain a competitive advantage, or to destroy a competitor,’ ” the court stated that there was a triable issue if [\*666] “Kodak adopted its parts and service policies as part of a scheme of willful acquisition or maintenance of monopoly power.” (*Eastman Kodak, supra, 504 U.S. at pp. 482–483.*) Though Kodak offered justifications for its exclusionary policy, the court [\*\*\*17] found triable issues as to whether the justifications were valid and sufficient. (*Id. at p. 483.*)

On remand, the jury found for the ISO's on the title [15 United States Code section 2](#) claim. The Ninth Circuit affirmed in *Image Tech. Services, Inc. v. Eastman Kodak Co. (9th Cir. 1997) 125 F.3d 1195 (Image Tech)*. In doing so, the court detailed the “substantial evidence” that supported the jury's finding that Kodak used its monopoly over parts in order to gain a monopoly over the service of Kodak equipment. (*Id. at p. 1208.*) The court elucidated the controlling law thusly: “[Section 2](#) of the *Sherman Act* prohibits a monopolist's unilateral action, like Kodak's refusal to deal, if that conduct harms the [\*\*826] competitive process in the absence of a legitimate business justification. [Citations.]” (*Image Tech, supra, at p. 1209.*)

Jumping into the appellate fray, the Independent Dealers aver that the facts alleged in the complaint are “strikingly similar” to those in *Eastman Kodak* and *Image Tech* because: (1) the ISO's were forced to purchase all of their replacement parts from Kodak, and the [\*\*\*18] Independent Dealers were forced to purchase new Verizon cellular

<sup>4</sup> Section 2 of the Sherman Act provides: [HN5↑](#) “Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$ 100,000,000 if a corporation, or, if any other person, \$ 1,000,000, or by imprisonment not exceeding 10 years, or by both said punishments, in the discretion of the court.” ([15 U.S.C. § 2.](#))

telephones from Verizon; and (2) like Kodak, which willingly sold replacement parts to the ISO's and then stopped, Verizon always had a two-week holdback period and then suddenly and unfairly lengthened that period.

To be frank, a skepticism was born with this forced analogy. The two cases are decidedly *dissimilar*. The relevant market in *Eastman Kodak* was defined by a single brand of service, i.e., it was composed of companies that serviced Kodak machines because there were no available substitutes. Kodak had a monopoly in the parts market and used it to monopolize the service market. In contrast, the relevant market here is comprised of *all* cellular telephones, and there is no allegation that Verizon has monopolized that market, or any related market. Customers change service providers, options, calling plans and cellular telephones on a regular basis. There are service providers other than Verizon, such as T-Mobile and Cingular, and there are manufacturers, such as Motorola, Nokia and Sony, which all sell cellular telephones. Moreover, the Independent Dealers do not claim that they, like the ISO's, have been [\*\*\*19] permanently cut off from a whole brand of products, or that consumers will be forced to purchase cellular telephones only from Verizon. Rather, they merely contend that they are denied the ability to sell the most popular new Verizon models, only two of which are identified by the complaint, for a finite period of time. It can be inferred from the complaint that their ability to sell other brands is unfettered, and consumers still have a wide variety of [\*667] choices of what and where to buy. Finally, whereas competition in the relevant market in *Eastman Kodak* was diminished, there is no equivalent allegation here. The Independent Dealers complain about the diminution of "intrabrand" price competition, rather than the diminution of market competition. In other words, all they can say is that there is less price competition for Verizon's cellular telephones, not that there is less price competition among all the different cellular telephone brands. Given this, it cannot be said that the effect of Verizon's conduct is comparable to or the same as a violation of the antitrust laws. In fact, a logical deduction from the complaint is that even though the Independent Dealers cannot undercut [\*\*\*20] Verizon's prices on popular new Verizon cellular telephone models during the holdback period, they can still undercut Verizon's prices with respect to the competing brand models acquired from manufacturers and other service providers.

**CA(5) [↑] (5)** In essence, the Independent Dealers want to force Verizon to immediately release its most popular new models and thereby "share the source of [its] advantage." (*Verizon Communications, supra, 540 U.S. at p. 407.*) But, unless there is an exception, the right to refuse to deal remains sacrosanct. Because that is true, **HNT[↑]** the mere refusal to deal does not violate the spirit or policy of *antitrust law*. In the absence of an abuse of monopoly power in a relevant market, this case involves nothing more than a permissible refusal to deal with the Independent Dealers.

Boiled down, the Independent Dealers' position is that the trial court failed to [\*\*827] properly balance *Colgate* against other antitrust policies. In their reply brief, the Independent Dealers advert to the following Supreme Court quote: "'Congress designed the *Sherman Act* as a "consumer welfare prescription." ' [Citation.] A restraint that has the effect of reducing the importance [\*\*\*21] of consumer preference in setting price and output is not consistent with this fundamental goal of anti-trust law. Restrictions on price and output are the paradigmatic examples of restraints of trade that the *Sherman Act* was intended to prohibit. [Citation.]'" (*NCAA v. Board of Regents of Univ. of Okla. (1984) 468 U.S. 85, 107–108 [82 L.Ed.2d 70, 104 S.Ct. 2948]*, fn. omitted.) Using this language as a springboard, the Independent Dealers declare that price competition is "the single most important public policy goal furthered by the antitrust laws." What the Independent Dealers fail to appreciate is that antitrust policy attempts to balance the benefits of protecting and fostering economic incentives for entrepreneurs to pursue business with the benefits procured for consumers when courts manage markets. In our view, the trial court found the right balance when it sustained Verizon's demurrer without leave to amend. Because we are dealing with a limited time restriction on *some* cellular telephones of *one* of many brands in a vibrant, volatile market with many consumer options, we take special heed of the warning in *Verizon Communications* that we should be cautious before creating exceptions [\*\*\*22] to the conduct allowed by *Colgate*.

[\*668] It is true, as the Independent Dealers take pains to stress, that *Cel-Tech* does not require an antitrust violation in order to state a *section 17203* claim. But we must still look at the alleged impact of the conduct, and we must consider any countervailing policies. The allegations here are simply too far removed from cognizable antitrust evils to warrant intervention by a California court.

b. *Significant threat or harm to competition.*

The Independent Dealers' argument regarding the threat or harm to competition is set forth in the following three sentences: "Here, Verizon's conduct indisputably reduces both consumer choice and price competition. It reduces consumer choice by choking off one of the avenues of distribution of Verizon's products. More significantly, it prevents [the Independent Dealers] from selling [cellular] telephones at a discount." After parsing this argument, we find it lacking.

We do not perceive a threat or harm to competition which can be characterized as significant. As explained in part 1.a., *ante*, there may be a reduction in intrabrand competition regarding some Verizon cellular telephones for [\*\*\*23] short periods of time, but there is no reduction in interbrand competition. The continuing interbrand competition from manufacturers and other service providers offers consumers a healthy array of choices and the benefit of price competition. What shines through most clearly in the complaint is that Verizon's conduct has injured the Independent Dealers. But, as *Cel-Tech* teaches, injury to competitors is not the same thing as injury to competition, and we may only consider the latter.

## 2. The commission structure.

Count II fails to state a claim under [section 17203](#).

In part, the problem is that the meaning of count II is murky. In their prayer for relief in the complaint, the Independent Dealers requested an "injunction prohibiting Verizon from permitting customers to upgrade their [cellular telephones] at Verizon owned stores if they have not fulfilled [\*\*828] at least one year of their service contract, which injunction shall continue in force unless and until Verizon adjusts its commission structure in such a manner as to permit [the] Independent Dealers to subsidize the [cellular telephone] purchases of those customers who have not fulfilled at least one year of [\*\*\*24] their service contract."

Essentially, the Independent Dealers paint the following picture. In the past, when a Verizon customer wanted a new cellular telephone, Verizon [\*669] would sell that cellular telephone below cost if the customer had fulfilled a year of his or her existing service contract. The only way the Independent Dealers could compete was to get a customer who had fulfilled a year of his or her existing service contract to renew that contract and then use the commission from that renewal to offset the cost of the new cellular telephone. When Verizon began selling all new cellular telephones below cost, the Independent Dealers were unable to compete in situations in which they did not receive a renewal commission. To remedy this situation, the Independent Dealers want a court to prohibit customers from upgrading their cellular telephones at Verizon stores until after they fulfill at least a year of their service contracts. Oddly, this would make it unlawful for Verizon to sell cellular telephones to some of their own customers. Also, it would mean that those customers could only get upgrades through the Independent Dealers or the manufacturers. According to the Independent Dealers, [\*\*\*25] this injunction should last until such time as Verizon devises a commission structure that allows the Independent Dealers to sell Verizon cellular telephones below cost to all customers, not just those who have fulfilled a year of their service contracts.

The bottom line is the Independent Dealers want to prevent Verizon from discounting in situations where they themselves cannot discount. This means that if the Independent Dealers cannot share in the wealth, they want a court to force certain Verizon customers to pay *higher* prices. What antitrust policy would be at play here? The Independent Dealers do not say, and it is difficult for us to conceive. A few things must be sorted out before we even try.

**CA(6) [6]** It is important to note that the policies behind section 1 of the Sherman Act are not implicated here.<sup>5</sup> ([15 U.S.C. § 1](#).) We have been instructed by the Supreme Court that **HN8** [8] [section 1](#) of the *Sherman Act*

<sup>5</sup> [Section 1](#) of the *Sherman Act* provides: **HN9** [9] "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any contract or engage in any combination or conspiracy hereby declared to be illegal shall be deemed guilty of a felony, and, on conviction thereof, shall be punished by fine not exceeding \$ 100,000,000 if a corporation, or, if any

"reaches unreasonable restraints of trade effected by a 'contract, combination ... or conspiracy' between separate entities. It does not reach conduct that is 'wholly unilateral.' [Citations.]" ([Copperweld Corp. v. Independence Tube Corp. \(1984\) 467 U.S. 752, 768 \[81 L.Ed.2d 628, 104 S.Ct. 2731\]](#) [\*\*\*26] (*Copperweld*.) A parent and its wholly owned subsidiaries, like Verizon and its stores, are considered a single economic entity for purposes of the *Sherman Act*. (*Copperweld, supra, at pp. 771?774.*)

Now to the bone of contention.

[\*670] To establish the validity of count II, the Independent Dealers contend that Verizon's commission structure produces [\*\*\*27] an [\*\*829] effect comparable to or the same as that in [Eiberger v. Sony Corp. of America \(2d Cir. 1980\) 622 F.2d 1068](#) (*Eiberger*), and therefore triggers *Cel-Tech*. We disagree.

In *Eiberger*, the question was whether Sony Corporation of America (Sony) had violated [section 1](#) of the *Sherman Act*. ([Eiberger, supra, 622 F.2d at p. 1070](#).) The background facts were these. Eiberger's company (ABP) was a nonexclusive dealer of Sony dictation machines in the Atlanta, Georgia territory. ABP eventually began to sell large quantities of dictation machines to discounters who undersold to authorized dealers in other territories. Subsequently, Sony revised its dealership agreements. Nonselling dealers were required to accept warranty responsibilities on dictation machines when requested and paid by Sony. Additionally, if the selling dealer did not render warranty service, then it had to pay a scheduled warranty fee to Sony. Nonselling dealers began finding machines sold by others in their territories and reporting the serial numbers of those machines to Sony. Sony credited the accounts of those dealers with warranty fees and debited a corresponding amount to [\*\*\*28] the accounts of the selling dealers. Sony did so whether or not warranty service had been rendered and regardless of whether the warranty period had begun. When Sony began docking ABP's account, ABP refused to pay. As a result, Sony elected not to renew ABP's franchise. ([Id. at pp. 1071–1074](#).)

**CA(7)↑ (7)** The district court found that Sony's warranty fee requirement amounted to a vertical territorial restriction on trade, and that it was unlawful. As the *Eiberger* court explained, the reality is that [HN10](#)↑ "vertically imposed territorial restrictions normally have the potential for creating, simultaneously, benefits and detriments to competition. Such restraints typically inhibit the dealers in a given brand of product from competing against other dealers in the same brand; hence intrabrand competition is reduced. But these restraints may also achieve efficiencies that stimulate competition between brands." ([Eiberger, supra, 622 F.2d at pp. 1075–1076](#).) In assessing whether a violation had occurred, the court had to "weigh any enhancement of interbrand competition against the restrictive effect on intrabrand competition," "determine whether the restraints [were], [\*\*\*29] in all the circumstances, reasonable," and "look to the history of the restraint itself, to the problem perceived by the manufacturer and the goal sought to be achieved, and to the actual effect of the restraint." ([Id. at p. 1076](#).) Given that formula and the facts, the district court did not err. (*Ibid.*)

[\*671] There were two main findings that dictated the outcome. "First, [the district court] found that the principal purpose of the 1975 warranty plan was not to assure that the users of Sony dictation equipment secured warranty service but was rather to enforce the territorial divisions reflected in the dealership agreements. Second, the [district court] found that the effect of the new system 'would be the elimination of intrabrand competition within each authorized dealer's territory.' [Citation.]" ([Eiberger, supra, 622 F.2d at pp. 1076–1077](#), fn. omitted.)

We now turn to the Independent Dealers' position. They contend: "In the instant case, the [complaint] alleges that Verizon refuses to pay commissions for sales made by [the] Independent Dealers but does pay commissions for identical sales made by its own stores . . . . The allegations [\*\*\*30] in the [complaint] do not reveal any procompetitive justification for this practice. On the contrary, they clearly suggest that the true motive behind Verizon's discriminatory commission structure [\*\*830] is to prevent the [Independent Dealers] from discounting." The Independent Dealers suggest that Verizon's conduct violates the policy and spirit of the antitrust laws and creates an effect similar to an antitrust violation.

Reflecting on this argument proves difficult. First, it assumes allegations that the Independent Dealers never made. The complaint does not allege, for example, that Verizon pays commissions to its own stores.<sup>6</sup> Nor does it allege that the Independent Dealers never receive commissions. Second, while *Eiberger* involved vertically imposed territorial restrictions on intrabrand sales by authorized dealers, the case at bar does not involve any such allegations. Third, there were separate entities and anti-competitive contracts in *Eiberger*, but not here. It is only in the reply brief that some light is finally shed on why Independent Dealers direct us to consider the *Eiberger* decision. There, they claim that though this case is by no means identical to *Eiberger*, [\*\*\*31] “both cases are based on exactly the same public policy concerns, namely the protection of discounters and the promotion of price competition.”

**CA(8)** [8] (8) The discrepancy about the true contents of the complaint aside, our initial hesitation with trying to compare the commission structure to the facts in *Eiberger* is that, legally, these two cases are apples and oranges. *Eiberger* was the result of [section 1](#) of the [Sherman Act](#). Count II, if anything, implicates the polices underlying [section 2](#) of the [Sherman Act](#). As explained [\*672] in *Copperweld*, [HN11](#) [“c]oncerted activity subject [\*\*\*32] to [title [15 United States Code section 1](#) is judged more sternly than unilateral activity under [title [15 United States Code section 2](#).” (*Copperweld, supra, 467 U.S. at p. 768.*) This is largely because there are countervailing policies involved with title [15 United States Code section 2](#). “The [Sherman Act](#) contains a ‘basic distinction between concerted and independent action.’ [Citation.] The conduct of a single firm is governed by [title [15 United States Codes section 2](#)] alone and is unlawful only when it threatens actual monopolization. It is not enough that a single firm appears to ‘restrain trade’ unreasonably, for even a vigorous competitor may leave that impression. For instance, an efficient firm may capture unsatisfied customers from an inefficient rival, whose own ability to compete may suffer as a result. This is the rule of the marketplace and is precisely the sort of competition that promotes the consumer interests that the [Sherman Act](#) aims to foster. In part because it is sometimes difficult to distinguish robust competition from conduct with long-run anticompetitive effects, Congress authorized [Sherman Act](#) scrutiny of [\*\*\*33] single firms only when they pose a danger of monopolization. Judging unilateral conduct in this manner reduces the risk that the antitrust laws will dampen the competitive zeal of a single aggressive entrepreneur.” (*Copperweld, supra, 467 U.S. at pp. 767–768*, fns. omitted.)

Thus, from a policy standpoint, Verizon's conduct does not pose an evil because it and its stores are viewed as a single entity, and because it does not possess a monopoly and it is not threatening a monopoly. Moreover, because we are dealing with a [\*\*831] single entity, we do not want to dampen its competitive zeal.

**CA(9)** [9] (9) To reiterate, we are aware that [HN12](#) [section 17203] can apply even if a defendant has not violated the antitrust laws. But, simply put, this case falls outside the policy and spirit of *Eiberger*. *Eiberger* protected discounters and price competition by awarding damages to an authorized agent who was damaged by dealership contracts that created a punishment greater than the profit when the authorized agent sold in other territories. Here, there is no allegation that Verizon imposed contracts with punitive provisions on the Independent Dealers. While ABP objected to Sony's interference [\*\*\*34] with discounting, the Independent Dealers make no such complaint. Rather, they complain that Verizon should be forced to cease selling cellular telephones to certain customers, or that it should be forced to assist the Independent Dealers financially so that they can discount and compete. We are aware of no case or statute, state or federal, which contains a policy that would force a company to either let its competitors have all of a particular category of sales, or force it to prop up its competitors financially. Having found no such law cited in the briefs, we can only conclude that *Cel-Tech* is not satisfied.

## [\*673] DISPOSITION

The judgment of dismissal is affirmed.

<sup>6</sup> We find the Independent Dealers' recapitulation of the complaint perplexing for two reasons. As we have indicated, the complaint never states that Verizon started paying commissions to its own stores. If that were not confusing enough, the trial court's statement of decision indicated that the “commission changes alleged involve Verizon and Verizon stores, not” the Independent Dealers. It is unclear why the trial court made this assumption.

Verizon shall recover its costs on appeal.

Doi Todd, Acting P. J., and Nott, J.,<sup>\*</sup> concurred.

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\* Retired Associate Justice of the Court of Appeal, Second Appellate District, assigned by the Chief Justice pursuant to [article VI, section 6 of the California Constitution](#).



## Banner Pharmacaps, Inc. v. Perrigo Co.

United States District Court for the Middle District of North Carolina

August 1, 2005, Decided ; August 1, 2005, Filed

1:04CV492

### **Reporter**

2005 U.S. Dist. LEXIS 37842 \*; 2005 WL 2136927

BANNER PHARMACAPS INC., Plaintiff, v. PERRIGO COMPANY; L. PERRIGO COMPANY; and PERRIGO COMPANY OF SOUTH CAROLINA, Defendants.

**Subsequent History:** Adopted by, Partial summary judgment granted by, in part [Banner Pharmacaps Inc. v. Perrigo Co., 2005 U.S. Dist. LEXIS 38034 \(M.D.N.C., Sept. 6, 2005\)](#)

**Prior History:** [\*1] Case 1:04-cv-00492-FWB.

[Banner Pharmacaps, Inc. v. Perrigo Co., 2005 U.S. Dist. LEXIS 56180 \(M.D.N.C., July 6, 2005\)](#)

## **Core Terms**

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patent, infringement, marking, inequitable conduct, anti-trust, summary judgment, products, counterclaim, argues, summary judgment motion, patentee, notice, literal, tablets, prior art, misrepresented, references, material fact, containers, disclose, damages, recommended, violations, gelatin, cases, partial summary judgment, genuine issue, matter of law, misrepresentation, unenforceable

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

### **HN1[] Summary Judgment, Entitlement as Matter of Law**

Under [Fed. R. Civ. P. 56\(c\)](#), summary judgment is proper if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. A party seeking summary judgment bears the initial responsibility of informing the district court of the basis for its motion, and identifying those portions of the record which it believes demonstrate the absence of a genuine issue of material fact. Once the moving party has met its burden, the nonmoving party must then set forth specific facts showing that there is a genuine issue for trial. [Fed. R. Civ. P. 56\(e\)](#).

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Patent Law > Infringement Actions > Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

## **HN2** [down arrow] **Burdens of Proof, Movant Persuasion & Proof**

In making a determination on a summary judgment motion, a federal district court views the evidence in the light most favorable to the nonmoving party, according that party the benefit of all reasonable inferences. Mere allegations and denials, however, are insufficient to establish a genuine issue of material fact. Judges are not required to submit a question to a jury merely because some evidence has been introduced by the party having the burden of proof, unless the evidence be of such a character that it would warrant the jury in finding a verdict in favor of that party. Thus, the moving party can bear its burden either by presenting affirmative evidence or by demonstrating that the nonmoving party's evidence is insufficient to establish its claim. A complete failure of proof concerning an essential element of a plaintiff's case necessarily renders all other facts immaterial. The United States Court of Appeals for the Federal Circuit has clearly determined that summary judgment is available in patent cases as it is in any other type of case.

Patent Law > Infringement Actions > Burdens of Proof

Patent Law > Infringement Actions > General Overview

Patent Law > ... > Defenses > Patent Invalidity > Presumption of Validity

## **HN3** [down arrow] **Infringement Actions, Burdens of Proof**

A patent is literally infringed if every element it recites in a given claim or claims is present in the accused product. 35 U.S.C.S. § 271. The patentee has the burden of proving infringement by a preponderance of the evidence. By contrast, a patent is presumed valid and an accused infringer has the burden of overcoming this presumption by clear and convincing evidence. 35 U.S.C.S. § 282. A court should employ a two-step analysis in making an infringement determination. First, the court must construe the asserted claims to ascertain their meaning and scope. Construction of the claims is a question of law subject to de novo review. The trier of fact must then compare the properly construed claims with the accused infringing product. This second step is a question of fact.

Patent Law > ... > Defenses > Patent Invalidity > General Overview

Patent Law > Infringement Actions > General Overview

## **HN4** [down arrow] **Defenses, Patent Invalidity**

It is well settled that the validity of a patent and patent infringement are separate questions that must be answered independently of each other.

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

## **HN5** [down arrow] **Defenses, Inequitable Conduct**

Every applicant for a patent has a duty of candor and good faith in its dealing with the U.S. Patent and Trademark Office and the examiner handling his application. This means that the applicant and his lawyer must not intentionally withhold or misrepresent material information concerning the invention, as defined by the asserted claim. A breach of this duty is inequitable conduct and renders the patent unenforceable. To find that a patent applicant engaged in inequitable conduct in the pursuit of a patent, a court must find by clear and convincing evidence that the applicant omitted or misrepresented material facts with the intention of misleading or deceiving the examiner. Inequitable conduct includes affirmative misrepresentation of a material fact, failure to disclose material information, or submission of false material information, coupled with an intent to deceive. Even if conduct is found to be misleading on a material point, however, an inference of intent is not required. Finally, the more material the information, the less amount of intent is required, and vice versa.

Patent Law > Infringement Actions > Summary Judgment > General Overview

Patent Law > ... > Inequitable Conduct > Effect, Materiality & Scienter > General Overview

#### **HN6** [down arrow] **Infringement Actions, Summary Judgment**

Even if materiality and intent to commit inequitable conduct in obtaining a patent are adequately demonstrated, a federal district court must balance the equities to determine whether a patentee committed inequitable conduct that warrants holding the patent unenforceable. The defense of inequitable conduct is entirely equitable in nature, and is thus not an issue for a jury to decide. A patentee, therefore, has no right to a jury trial respecting the factual element of culpable intent as part of the defense of inequitable conduct. Thus, a disputed finding of intent to mislead or to deceive is one for the judge to resolve, not the jury, albeit not on summary judgment if there is a genuine dispute.

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Fraudulent Procurement of Patent

#### **HN7** [down arrow] **Defenses, Fraudulent Procurement of Patent**

The legal standard for fraud on the U.S. Patent and Trademark Office (PTO) is similar to that of inequitable conduct in that it requires that a patentee make a material misrepresentation to the PTO or withhold information material to the prosecution of the patent. Fraud on the PTO, however, requires a higher threshold showing of both intent and materiality than does a finding of inequitable conduct. Indeed, there must be clear evidence of deceptive intent and a clear showing that the examiner would not have issued the patent but for the misrepresentation or omission.

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Fraudulent Procurement of Patent

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Patent Law > Infringement Actions > Summary Judgment > General Overview

#### **HN8** [down arrow] **Defenses, Fraudulent Procurement of Patent**

The United States Court of Appeals for the Fourth Circuit has held that summary judgment is seldom appropriate in cases in which particular states of mind are decisive as elements of a claim or defense. In *Morrison v. Nissan Motor Co., Ltd.*, the Fourth Circuit cautioned that cases which turn on a finding of intent are not appropriate for summary judgment since resolution of that issue depends on the credibility of witnesses as determined by the trier of fact after observation of the witnesses' demeanor during direct and cross-examination. The principles enunciated by the

Fourth Circuit in Charbonnages de France v. Smith and Morrison v. Nissan Motor Co., Ltd. apply with particular emphasis in patent cases involving issues of fraud or inequitable conduct. In holding that issues of fraud or inequitable conduct are usually not appropriate for resolution by way of a motion for summary judgment, the United States Court of Appeals for the Federal Circuit has stated that a summary judgment of fraud or inequitable conduct, reached while denying to the person accused of the fraud or inequitable conduct the opportunity to be heard on the issue, is a draconian result.

Patent Law > US Patent & Trademark Office Proceedings > General Overview

### [\*\*HN9\*\*](#) [blue download icon] Patent Law, US Patent & Trademark Office Proceedings

References to prior art play a significant role in the application process for a patent. Applicants for patents have a duty of candor and good faith in dealing with the U.S. Patent and Trademark Office (PTO), which includes a duty to disclose to the PTO all information known to that individual to be material to patentability. [37 C.F.R. § 1.56](#). However, the duty of candor and good faith requires more than the obligation merely to bring material prior art to the attention of the PTO, and the issue is whether the plaintiff's argument to the examiner on appeal was contrary to the actual state-of-art.

Antitrust & Trade Law > ... > Intellectual Property > Misuse of Rights > Patent Misuse Defense

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Fraudulent Procurement of Patent

### [\*\*HN10\*\*](#) [blue download icon] Misuse of Rights, Patent Misuse Defense

The holder of a patent is generally immune from antitrust liability. Nevertheless, the United States Supreme Court established in *Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp.* that the fraudulent procurement of a patent or the enforcement of a patent knowingly obtained by fraud on the U.S. Patent and Trademark Office (PTO) may be the basis of an action under § 2 of the Sherman Act, provided that the other elements of a Sherman Act claim are present. Thus, one who procures a patent by defrauding the PTO is stripped of antitrust immunity. In *Walker Process*, the Supreme Court provided the guiding principles that where a patentee obtains its patent by fraud, it cannot enjoy the limited exception to the prohibitions of § 2 of the Sherman Act, but must answer under that section and § 4 of the Clayton Act in treble damages to those injured by any monopolistic action taken under the fraudulent patent claim. Nor can the interest in protecting patentees from innumerable vexatious suits be used to frustrate the assertion of rights conferred by the antitrust laws.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

### [\*\*HN11\*\*](#) [blue download icon] Burdens of Proof, Movant Persuasion & Proof

Although the failure of a party to respond to a summary judgment motion may leave uncontested those facts established by the motion, the moving party must still show that the uncontested facts entitle the party to a judgment as a matter of law.

Antitrust & Trade Law > Sherman Act > Claims

### [\*\*HN12\*\*](#) [blue download icon] Sherman Act, Claims

To establish an antitrust violation under the Sherman Act, a party must show (i) a specific attempt by the another party to monopolize the relevant market, and (ii) a dangerous probability that the attempt would be successful in achieving a monopoly in the relevant market.

Patent Law > Infringement Actions > Defenses > Marking

#### [HN13](#) [ ] Defenses, Marking

Under [35 U.S.C.S. § 287\(a\)](#), a patentee or other party selling a patented product under the patent must mark that product as patented in order to give the public notice. In cases where a patent owner sells a product embodying the invention, a patent owner may seek damages for infringement occurring during a period in which the accused infringer had actual or constructive notice of the asserted patent. [35 U.S.C.S. § 287\(a\)](#). A patentee may provide constructive notice of a patent through marking the patented product with the word "patent" or the abbreviation "pat.", together with the number of the patent. [35 U.S.C.S. § 287\(a\)](#). If the product itself cannot feasibly be marked, then packaging containing the patented product may be marked instead. [35 U.S.C.S. § 287\(a\)](#). If the patentee fails to comply, he may only recover damages for the period after the infringer was actually notified of the infringement, and, under [35 U.S.C.S. § 287\(a\)](#), the filing of an action for infringement shall constitute such notice. [35 U.S.C.S. § 287\(a\)](#). A patentee's licensees also must mark products with the patent number, and when the failure to mark is caused by someone other than the patentee, the court may consider whether the patentee made reasonable efforts to ensure compliance with the marking requirements.

Evidence > Burdens of Proof > Allocation

Patent Law > Infringement Actions > Summary Judgment > General Overview

Patent Law > Infringement Actions > Defenses > Marking

#### [HN14](#) [ ] Burdens of Proof, Allocation

A patentee bears the burden to prove compliance with the marking statute, [35 U.S.C.S. § 287\(a\)](#). In addition, compliance with the marking statute is a question of fact. Nevertheless, this issue is properly decided upon summary judgment when no reasonable jury could find that the patentee either has or has not provided actual notice to the 'particular defendants by informing them of his patent and of their infringement of it.

Patent Law > Infringement Actions > Defenses > Marking

#### [HN15](#) [ ] Defenses, Marking

See [35 U.S.C.S. § 287\(a\)](#).

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**Judges:** Wallace W. Dixon, United States Magistrate Judge.

**Opinion by:** Wallace W. Dixon

## Opinion

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### RECOMMENDATION OF UNITED STATES MAGISTRATE JUDGE

This matter is before the court on Plaintiff's [\*2] motion for partial summary judgment (docket no. 34). Defendant L. Perrigo has responded in opposition (docket no. 47), and Plaintiff has replied (docket no. 51). In this posture, this matter is ripe for disposition. Furthermore, because the parties have not consented to the jurisdiction of a magistrate judge, the court must deal with the motion by way of recommendation.

#### I. Background

Plaintiff Banner designs, manufactures, and sells pharmaceutical products, including over-the-counter medications for the treatment of cold, cough, flu, allergy, and other ailments. App. 11, Francis Aff. P 3. Banner employees conceived of a form of medication wherein a tablet, or "core," is enrobed in a gelatin covering formed by two layers of elastic gelatin film on opposite sides of the tablet. App. 1, '516 Parent, Abstract; App. 11, Francis Aff. P 3. These products are commercially known as Banner's Softlet(R) products. In 2002, Banner obtained a patent on these products, Banner Patent 6,482,516 (the "516 patent"). Defendant L. Perrigo Company ("L. Perrigo") is a pharmaceutical company which manufactures and sells lower-priced, store-brand alternatives to comparable brand over-the-counter [\*3] pharmaceutical products. Banner is a vendor to pharmaceutical companies such as L. Perrigo and for some time supplied to L. Perrigo its gelatin film-enrobed tablets in bulk quantities. Plaintiff has now sued L. Perrigo, its parent and its sister company, accusing them of infringing on the '516 patent. L. Perrigo has counterclaimed, seeking a declaratory judgment that the '516 patent is invalid for several reasons and unenforceable due to Banner's inequitable conduct and fraud in obtaining the '516 patent. L. Perrigo has also counterclaimed that Banner has used the fraudulently obtained patent in violation of anti-trust laws. Finally, L. Perrigo argues that even if Banner wins on the patent invalidity and contested infringement issues, Banner may recover damages only from June 4, 2004, the date it filed its complaint. According to L. Perrigo, this is so because Banner failed to properly mark its Softlet(R) products with the '516 patent number in accordance with [35 U.S.C. § 287\(a\)](#) and, thus, failed to give constructive notice of the patent. Plaintiff now seeks partial summary judgment on the following questions: (1) whether L. Perrigo has literally infringed Claims [\*4] 8, 12, 13, and 14 of the '516 Patent; (2) whether summary judgment should be granted as to L. Perrigo's counterclaims for inequitable conduct, fraud, and anti-trust; and (3) whether Banner marked its Softlet(R) products in compliance with [35 U.S.C. § 287\(a\)](#), thereby giving constructive notice to the public that these products were patented.

#### II. Discussion

**HN1** [↑] Under [Rule 56\(c\)](#), summary judgment is proper "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." [FED. R. CIV. P. 56\(c\)](#). A party seeking summary judgment "bears the initial responsibility of informing the district court of the basis for its motion, and

identifying those portions of the [record] which it believes demonstrate the absence of a genuine issue of material fact." [Celotex Corp. v. Catrett, 477 U.S. 317, 323, 106 S. Ct. 2548, 91 L. Ed. 2d 265 \(1986\)](#). Once the moving party has met its burden, the non-moving party must then set forth "specific facts showing that there [\*5] is a genuine issue for trial." [Matsushita Elec. Indus. Co. Ltd. v. Zenith Radio Corp., 475 U.S. 574 586-87, 106 S. Ct. 1348, 89 L. Ed. 2d 538 \(1986\)](#) (quoting [FED. R. CIV. P. 56\(e\)](#)).

**HN2**[] In making a determination on a summary judgment motion, the court views the evidence in the light most favorable to the non-moving party, according that party the benefit of all reasonable inferences. [Bailey v. Blue Cross & Blue Shield, 67 F.3d 53, 56 \(4th Cir. 1995\)](#). Mere allegations and denials, however, are insufficient to establish a genuine issue of material fact. See [Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 \(1986\)](#). Judges are not "required to submit a question to a jury merely because some evidence has been introduced by the party having the burden of proof, unless the evidence be of such a character that it would warrant the jury in finding a verdict in favor of that party." [Id. at 251](#) (citations omitted). Thus, the moving party can bear its burden either by presenting affirmative evidence or by demonstrating that the non-moving party's evidence is insufficient to establish its claim. [Celotex, 477 U.S. at 331](#) [\*6] (Brennan, J., dissenting). "[A] complete failure of proof concerning an essential element of [a plaintiff's] case necessarily renders all other facts immaterial." [Celotex, 477 U.S. at 323](#). The Federal Circuit has clearly determined that summary judgment is available in patent cases as it is in any other type of case. [Barmag Barmer Maschinenfabrik AG v. Murata Mach., Ltd., 731 F.2d 831, 835 \(Fed. Cir. 1984\)](#).

### Plaintiff's Motion for Summary Judgment As to Whether Claims 8, 12, 13, and 14 of the '516 Patent Have Been Infringed

Here, the court first addresses whether partial summary judgment should be granted to Plaintiff on the issue of literal infringement of certain claims of the '516 patent. **HN3**[] A patent is literally infringed if every element it recites in a given claim or claims is present in the accused product. [35 U.S.C. § 271](#). The patentee has the burden of proving infringement by a preponderance of the evidence. [Deering Precision Instruments, L.L.C. v. Vector Distribution Sys., Inc., 347 F.3d 1314, 1324-27 \(Fed. Cir. 2003\)](#). By contrast, a patent is presumed valid and an accused infringer [\*7] has the burden of overcoming this presumption by clear and convincing evidence. [35 U.S.C. § 282; Iron Grip Barbell Co. v. USA Sports, Inc., 392 F.3d 1317, 1320 \(Fed. Cir. 2004\)](#). A court should employ a two-step analysis in making an infringement determination. [Markman v. Westview Instruments, Inc., 52 F.3d 967, 976 \(Fed. Cir. 1995\)](#). First, the court must construe the asserted claims to ascertain their meaning and scope. *Id.* Construction of the claims is a question of law subject to de novo review. [Cybor Corp. v. FAS Techs., Inc., 138 F.3d 1448, 1454 \(Fed. Cir. 1998\)](#). The trier of fact must then compare the properly construed claims with the accused infringing product. [Markman, 52 F.3d at 976](#). This second step is a question of fact. [Bai v. L & L Wings, Inc., 160 F.3d 1350, 1353 \(Fed. Cir. 1998\)](#).

Here, Plaintiff Banner alleges that Defendant L. Perrigo and the other defendants have literally infringed Claims 8 and 12-14 of the '516 patent by offering for sale and selling film-enrobed, unitary-core tablets that meet the limitations of those claims. More specifically, Plaintiff [\*8] argues that L. Perrigo's products with a gelatin to plasticizer ratio of 4.8:1 infringe Claims 8, 12, 13, and 14 of the '516 Patent. Plaintiff has offered affidavit and other testimony as to literal infringement of these claims. In response, Defendant has not offered any summary judgment evidence to rebut Plaintiff's contention of literal infringement of these claims. Indeed, Defendant concedes literal infringement of these particular claims if the patent is valid and enforceable, but Defendant argues that the patent is neither valid nor enforceable. Specifically, Defendant states in its brief:

L. Perrigo has countered that it does not infringe some of the claims of the '516 patent, but has agreed that some of the very broad claims would be infringed, if they were valid. Banner has moved for summary judgment on infringement of those claims, which L. Perrigo asks to be deferred or otherwise dealt with in such a way as to avoid prejudice in the trial of the remainder of the case.

D.'s Br. p. 2. This statement by Defendant L. Perrigo appears to be nothing less than a clear admission of literal infringement of Claims 8, 12, 13, and 14 of the '516 patent. The court should, [\*9] therefore, grant summary judgment to Plaintiff on the issue of whether Defendant's products with a gelatin to plasticizer ratio of 4.8:1 literally

infringe Claims 8, 12, 13, and 14 of the '516 patent. The remaining disputed issue, therefore, is whether summary judgment is appropriate as to Defendant's counterclaims, including that the patent is unenforceable because of inequitable conduct and fraud and that Plaintiff has committed anti-trust violations.<sup>1</sup>

**[\*10] Plaintiff's Motion for Summary Judgment As to Defendant's Counterclaims for Inequitable Conduct, Fraud, and Anti-trust Violations**

Plaintiff has moved for summary judgment on Defendant's counterclaims that the patent is unenforceable due to Plaintiff's inequitable conduct, fraud, and anti-trust violations. Defendant's allegations of inequitable conduct, fraud, and antitrust liability are based on the assertion that Plaintiff misrepresented the state-of-art during an appeal on the denial of a patent. Defendant specifically points to prior art references for United States Patent 4,154,636 to Motoyama (Motoyama), United States Patent 2,775,081 to Stirn et al. (Stirn), and United States Patent 2,155,444 to Pittenger et al. (Pittenger). In opposing summary judgment on this issue, Defendant does not argue that Plaintiff failed to disclose these references during the application process in general. Indeed, it is undisputed that Plaintiff did disclose these references. Instead, Defendant argues that Plaintiff failed to disclose these references while distinguishing other references upon which the examiner had relied. Answer and Countercl., PP 40-43. Specifically, Defendant argues [\*11] that Plaintiff (1) positively misrepresented the state-of-the-art of film-enrobed tablets; (2) misrepresented the state-of-the-art of gelatin formulations used to enrobe liquid core products, which included formulations in the range claimed in the '516 patent application and which were known to Plaintiff; and (3) allowed the U.S. Patent and Trademark Office Patent Office ("PTO") to make an obvious error in allowing the "tenacious adherence" claims, when it failed to point out that the Pittenger '444 patent claimed that the film on its film-enrobed tablets adhered "tenaciously" to the tablet cores. See Def.'s Br. in Opp'n, p. 15. Defendant further argues that Plaintiff "did these things to intentionally mislead and deceive" the PTO. *Id.*

**HN5** Every applicant for a patent has a duty of candor and good faith in its dealing with the PTO and the Examiner handling his application. This means that the applicant and his lawyer must not intentionally withhold or misrepresent material information concerning the invention, as defined by the asserted claim. A breach of this duty is inequitable conduct and renders the patent unenforceable. To find that a patent applicant engaged in inequitable [\*12] conduct in the pursuit of a patent, a court must find by clear and convincing evidence that the applicant omitted or misrepresented material facts with the intention of misleading or deceiving the examiner. *Monsanto Co. v. Bayer BioScience N.V.*, 363 F.3d 1235, 1239 (Fed. Cir. 2004) (citing *Glaxo Inc. v. Novopharm Ltd.*, 52 F.3d 1043, 1048 (Fed. Cir. 1995)). "Inequitable conduct includes affirmative misrepresentation of a material fact, failure to disclose material information, or submission of false material information, coupled with an intent to deceive." *Molins PLC v. Textron, Inc.*, 48 F.3d 1172, 1178 (Fed. Cir. 1995). Intent can, sometimes, be inferred from misleading conduct itself, *Monsanto*, 363 F.3d at 1241 (citing *Paragon Podiatry Lab., Inc. v. KLM Labs., Inc.*, 984 F.2d 1182, 1191 (Fed. Cir. 1993)). Even if conduct is found to be misleading on a material point, however, an inference of intent is not required. *Monsanto*, 363 F.3d at 1241. Finally, the more material the information, the less amount of intent is required, and vice versa.<sup>2</sup> *Critikon, Inc. v. Becton Dickinson Vascular Access, Inc.*, 120 F.3d 1253, 1256 (Fed. Cir. 1997). [\*13]

<sup>1</sup> **HN4** It is well settled that validity and infringement are separate questions that must be answered independently of each other. See, e.g., *Pandrol USA, LP v. Airboss Ry. Prods., Inc.*, 320 F.3d 1354, 1364 (Fed. Cir. 2003) (where the defendants "did not waive the right to a trial on the issue of invalidity by failing to raise it in opposition to the cross-motion for summary judgment as to the issue of infringement"); *Medtronic, Inc. v. Cardiac Pacemakers, Inc.*, 721 F.2d 1563, 1583 (Fed. Cir. 1983) (clarifying that "though an invalid claim cannot give rise to liability for infringement, whether it is infringed is an entirely separate question capable of determination without regard to its validity").

<sup>2</sup> **HN6** Even if materiality and intent have been adequately demonstrated, the district court must balance the equities to determine whether the patentee has committed inequitable conduct that warrants holding the patent unenforceable. *Monsanto Co.*, 363 F.3d at 1239 (citing *Hoffmann-La Roche, Inc. v. Promega Corp.*, 323 F.3d 1354, 1359 (Fed. Cir. 2003)). Furthermore, the "defense of inequitable conduct is entirely equitable in nature, and [is] thus not an issue for a jury to decide." *PerSeptive Biosystems, Inc. v. Pharmacia Biotech, Inc.*, 225 F.3d 1315, 1318 (Fed. Cir. 2000). A patentee, therefore, has no right to a jury trial respecting the factual element of culpable intent as part of the defense of inequitable conduct. *Id.* Thus, a disputed finding of

**HN7**[] The legal standard for fraud on the PTO is similar to that of inequitable [\*14] conduct in that it requires that a patentee make a material misrepresentation to the PTO or withhold information material to the prosecution of the patent. *Unitherm Food Sys., Inc. v. Swift-Eckrich, Inc.*, 375 F.3d 1341, 1358 (Fed. Cir. 2004); *Nobelpharma AB v. Implant Innovations, Inc.*, 141 F.3d 1059, 1069 (Fed. Cir. 1998). Fraud on the PTO, however, requires a "higher threshold showing of both intent and materiality than does a finding of inequitable conduct." *Nobelpharma*, 141 F.3d at 1070-71. Indeed, there must be clear evidence of deceptive intent and a clear showing that the examiner would not have issued the patent but for the misrepresentation or omission. *Id. at 1070*; see also *Bristol-Myers Squibb Co. v. Ben Venue Lab.*, 90 F. Supp. 2d 540, 542 (D.N.J. 2000).

**HN8**[] The Fourth Circuit has held that summary judgment is seldom appropriate in cases in which particular states of mind are decisive as elements of a claim or defense. *Charbonnages de France v. Smith*, 597 F.2d 406, 414 (4th Cir. 1979). In *Morrison v. Nissan Motor Co., Ltd.*, 601 F.2d 139, 141 (4th Cir. 1979), [\*15] the Fourth Circuit cautioned that cases which turn on a finding of intent are not appropriate for summary judgment since resolution of that issue depends on the credibility of witnesses as determined by the trier of fact after observation of the witnesses' demeanor during direct and cross-examination. The principles enunciated by the Fourth Circuit in the *Charbonnages* and *Morrison* cases apply with particular emphasis in patent cases involving issues of fraud or inequitable conduct. In holding that issues of fraud or inequitable conduct are usually not appropriate for resolution by way of a motion for summary judgment, the Federal Circuit has stated that:

[a] summary judgment of fraud or inequitable conduct, reached while denying to the person accused of the fraud or inequitable conduct the opportunity to be heard on the issue, is a draconian result.

*KangaROOS U.S.A., Inc. v. Caldor, Inc.*, 778 F.2d 1571, 1573-74 (Fed. Cir. 1985); see also *Paragon Podiatry*, 984 F.2d at 1190 (observing that "the intent element of fraud or inequitable conduct . . . requires the fact finder to evaluate all the facts and circumstances in each case" [\*16] and therefore "such an evaluation is rarely enabled in summary proceedings").

Here, having considered the alleged prior art patents cited by Defendant along with expert witness testimony, depositions, affidavits, and other evidence submitted by both parties, the court finds that genuine issues of fact exist regarding whether, in prosecuting the patent application, Plaintiff engaged in inequitable conduct and/or fraud. To grant summary judgment to Plaintiff on Defendant's counterclaim of inequitable conduct and/or fraud, this court must be able to conclude from the evidence in the summary judgment record that Defendant has been unable raise a genuine issue of fact as to whether (1) Plaintiff either omitted or misrepresented material prior art references; (2) that any of these omissions or misrepresentations were made without the requisite "knowing and willful" intent; or (3) that these omissions or misrepresentations could have been the but-for cause of the patent's issuance. Viewing the evidence in the light most favorable to Defendant as the non-movant, this court cannot summarily make such conclusions. Defendant has produced summary judgment evidence that sufficiently raises the [\*17] issues of whether Plaintiff intentionally misled and deceived the examiner by misrepresenting the "state of the art" during the appeal stage of the patent prosecution, used an inappropriate subjective double standard to assess the "state of the art," failed to disclose prior art teachings that directly contradicted its statements made to the examiner, and cited only those relevant documents that supported its arguments and not those which were contrary to its arguments.

The court notes that in its reply to Defendant's response to the summary judgment motion, Plaintiff does not adequately address Defendant's claims that Plaintiff violated its duty of candor by misrepresenting the state of the prior art to the examiner during the appeal stage. Plaintiff argues simply that because it is undisputed that it did disclose the Motoyama, Stirn, and Pittenger prior art references in the grandparent and parent applications of the '516 patent, it cannot be found to have engaged in fraud or inequitable conduct on the PTO as a matter of law. **HN9**[] References to prior art play a significant role in the application process for a patent. Applicants for patents have a "duty of candor and good faith in dealing [\*18] with the [PTO], which includes a duty to disclose to the [PTO] all information known to that individual to be material to patentability . . ." *37 C.F.R. § 1.56*. The court agrees with Defendant, however, that the duty of candor and good faith requires more than the obligation merely to bring

material prior art to the attention of the PTO, and the issue is whether Plaintiff's argument to the examiner on appeal was contrary to the actual state-of-art. Plaintiff, the movant, has failed to demonstrate to this court that these particular questions can be answered as a matter of law. Thus, it will be recommended that the court deny Plaintiff's motion for summary judgment as to Defendant's counterclaims alleging that the '516 patent is unenforceable due to inequitable conduct and fraud.

As for Defendant's counterclaim alleging that Plaintiff violated **antitrust law**, Defendant asserts that Plaintiff obtained the '516 patent by committing fraud upon the PTO and thereafter used the patent to exclude parties from the relevant market. Defendant argues that Plaintiff has therefore violated federal **antitrust law**, specifically the Sherman Act, 15 U.S.C. § 2 et seq., [\*19] "by attempting to acquire and/or maintain unlawful monopoly power in the American market for film enrobed tablets and caplets." Answer and Countercl., P 64. Plaintiff requests that this court grant summary judgment on Defendant's counterclaim for anti-trust violations, arguing that anti-trust liability can only attach after fraud on the PTO is established and that, as a matter of law, Plaintiff has not committed fraud on the PTO. For the following reasons, it will recommended that the court deny Plaintiff's motion for summary judgment as to this counterclaim.

**HN10**[<sup>1</sup>] The holder of a patent is generally immune from anti-trust liability. Nevertheless, the Supreme Court established in Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172, 86 S. Ct. 347, 15 L. Ed. 2d 247 (1965), that the fraudulent procurement of a patent or the enforcement of a patent knowingly obtained by fraud on the PTO may be the basis of an action under Section 2 of the Sherman Act, provided that the other elements of a Sherman Act claim are present.<sup>3</sup> 382 U.S. at 177, 177 n.5. Thus, one who procures a patent by defrauding the PTO is stripped of anti-trust immunity. Walker Process Equip., Inc., 382 U.S. at 174. [\*20] The *Walker Process* Court provides the guiding principles that:

since [the patentee] obtained its patent by fraud it cannot enjoy the limited exception to the prohibitions of § 2 of the Sherman Act, but must answer under that section and § 4 of the Clayton Act in treble damages to those injured by any monopolistic action taken under the fraudulent patent claim. Nor can the interest in protecting patentees from "innumerable vexatious suits" be used to frustrate the assertion of rights conferred by the antitrust laws. It must be remembered that we deal only with a special class of patents, i.e., those procured by intentional fraud.

*Id. at 176*. As previously discussed, the court has found that there is an issue of fact as to whether Plaintiff committed fraud in obtaining the '516 patent. Thus, summary judgment cannot not be granted to Plaintiff on Defendant's counterclaim for anti-trust violations. Plaintiff argues that because Defendant does not address the anti-trust claim in its reply to Plaintiff's motion for partial summary judgment it has, therefore, waived its anti-trust claim. The court does not agree. The court has already found that issues [\*21] of fact exist as to whether Plaintiff obtained the patent through fraud, and the anti-trust is necessarily based on a finding of fraud. Thus, summary judgment should not be granted to Plaintiff on Defendant's counterclaim alleging anti-trust violations. As the Fourth Circuit has made clear, **HN11**[<sup>1</sup>] "although the failure of a party to respond to a summary judgment motion *may* leave uncontested those facts established by the motion, the moving party must still show that the uncontested facts entitle the party to 'a judgment as a matter of law.'" Custer v. Pan Am. Life Ins. Co., 12 F.3d 410, 416 (4th Cir. 1993) (emphasis added). Here, this court finds that the material facts relevant to the anti-trust claim are in dispute because the anti-trust issue cannot be separated from the fraud issue. Therefore, the court should deny Plaintiff's motion for summary judgment as to this counterclaim.

#### **[\*22] Plaintiff's Motion for Summary Judgment on the Issue of Whether Banner Properly Marked its Products with the '516 Patent Number**

<sup>3</sup> **HN12**[<sup>1</sup>] To establish an anti-trust violation under the Sherman Act, Defendant must show (i) a specific attempt by Plaintiff to monopolize the relevant market, and (ii) a dangerous probability that the attempt would be successful in achieving a monopoly in the relevant market. See Loctite Corp. v. Ultraseal Ltd., 781 F.2d 861, 875 (Fed. Cir. 1985).

Before addressing the parties' arguments regarding marking, the court will first explain the general marking requirements for patent law. [HN13](#)<sup>4</sup> Under [35 U.S.C. § 287\(a\)](#), a patentee or other party selling a patented product under the patent must mark that product as patented in order to give the public notice.<sup>4</sup> In cases where a patent owner sells a product embodying the invention, a patent owner may seek damages for infringement occurring during a period in which the accused infringer had actual or constructive notice of the asserted patent. See [35 U.S.C. § 287\(a\)](#). A patentee may provide constructive notice of a patent through marking the patented product with "the word 'patent' or the abbreviation 'pat.', together with the number of the patent." [35 U.S.C. § 287\(a\)](#). If the product itself cannot feasibly be marked, then packaging containing the patented product may be marked instead. *Id.* If the patentee fails to comply, he may only recover damages for the period after the [\*23] infringer was actually notified of the infringement, and, under [§ 287\(a\)](#), the "filing of an action for infringement shall constitute such notice." [35 U.S.C. § 287\(a\)](#). A patentee's licensees also must mark products with the patent number, and "when the failure to mark is caused by someone other than the patentee, the court may consider whether the patentee made reasonable efforts to ensure compliance with the marking requirements." [Maxwell v. J. Baker, Inc., 86 F.3d 1098, 1111-12 \(Fed. Cir. 1996\)](#). [HN14](#)<sup>5</sup> The patentee bears the burden to prove compliance with the marking statute. *Id. at 1112-13*. Finally, compliance with the marking statute is a question of fact. [Gart v. Logitech, Inc., 254 F.3d 1334, 1339 \(Fed. Cir. 2001\)](#). Nevertheless, "this issue is properly decided upon summary judgment when no reasonable jury could find that the patentee either has or has not provided actual notice to the 'particular defendants by informing them of his patent and of their infringement of it.'" *Id.* (quoting [Amsted Indus. Inc. v. Buckeye Steel Castings Co., 24 F.3d 178, 187 \(Fed. Cir. 1994\)](#)).

[\*24] Here, Plaintiff has moved for summary judgment on the issue of marking, asking this court to conclude that Plaintiff marked its Softlet(R) products in compliance with [35 U.S.C. § 287\(a\)](#), thereby giving notice to the public, including Defendant L. Perrigo, that these articles are patented. The '516 patent issued on November 19, 2002, and Plaintiff asserts that less than two months later, on January 10, 2003, Plaintiff began marking the containers for all of its products covered by the '516 patent with that patent number and that it has consistently done so since that date.<sup>5</sup> Thus, according to Plaintiff, if the court ultimately finds that it is entitled to damages on Defendant's infringement, then it may recover damages from that date.

[\*25] Defendant counters that genuine issues of material fact exist as to whether (1) Plaintiff actually marked containers used to provide bulk product to Defendant and whether (2) "the tiny printed patent number on [Plaintiff]'s label provided notice to the public of [Plaintiff]'s patent." Br. in Opp'n, pp. 15-16. As evidence, Defendant offers an affidavit by Tim Adamczyk, the warehouse manager for L. Perrigo, stating that the containers were barrels, not boxes as Plaintiff has argued, and that the barrels were never marked with any patent number. *Id.* at 16 (citing Ex. F., Adamczyk Decl., PP 2-3, and 4, respectively). Attached to the Adamczyk affidavit is a sample label from September 1998, offered as an example of the manner in which Plaintiff labeled its products with the '516 patent. Adamczyk Decl. P 5. Defendant further claims that it and the other bulk purchasers of Plaintiff's gelatin-enrobed tablets were implied licensees and, therefore, should have been instructed to mark the finished products with the '516 patent. Defendant argues that the absence of this requirement between Plaintiff and its bulk customers resulted in a failure to provide notice to the public as required [\*26] by [§ 287](#). According to Defendant, because the

<sup>4</sup> [35 U.S.C. § 287\(a\)](#) provides, in pertinent part:

[HN15](#)<sup>5</sup> Patentees, and persons making, offering for sale, or selling within the United States any patented article for or under them, or importing any patented article into the United States, may give notice to the public that the same is patented, either by fixing thereon the word "patent" or the abbreviation "pat.", together with the number of the patent, or when, from the character of the article, this can not be done, by fixing to it, or to the package wherein one or more of them is contained, a label containing a like notice. In the event of failure so to mark, no damages shall be recovered by the patentee in any action for infringement, except on proof that the infringer was notified of the infringement and continued to infringe thereafter, in which event damages may be recovered only for infringement occurring after such notice. Filing of an action for infringement shall constitute such notice.

<sup>5</sup> Plaintiff states that since the individual tablets are far too small to display such a notice, Plaintiff "properly marked the container in which the tablets are shipped to its customers in accordance with [35 U.S.C. § 287\(a\)](#)." Pl.'s Br. Supp. Summ. J. at p. 19.

patented products sold to end users were never marked, Plaintiff is precluded from recovering damages prior to the date that it actually notified Defendant of the alleged infringement, which Defendant contends was June 4, 2004, the date when the original complaint was filed. In response, Plaintiff argues that the sample label from September 1998 that was attached to the Adamczyk affidavit is entirely irrelevant to a patent that was issued in November 2002. Plaintiff also argues that its markings comply with [35 U.S.C. § 287\(a\)](#) since that section has no requirement of "font size or the like." Finally, Plaintiff argues in reply that Defendant is a customer, and not an implied licensee, and was not, therefore, required to mark the finished products with Plaintiff's patent number.

Viewing the evidence in the light most favorable to Defendant as the nonmovant, this court cannot grant Plaintiff's motion for summary judgment on the issue of whether the products or product containers in question were marked in accordance with [35 U.S.C. § 287\(a\)](#). First, the distinction between customer and implied licensee, [\*27] and the question of how that distinction affects Plaintiff's responsibility regarding marking and noticing the public, simply cannot be decided on the pleadings thus far. Furthermore, there is a question of fact as to whether the containers were marked at all, as well as what type of containers were used, and the specific size of the markings. Although the sample label which Defendant provided in the Adamczyk deposition predates the issuance of the '516 patent, Adamczyk declares under oath that he never saw a container marked with the patent information. In sum, there are genuine issues of fact as to marking. It will, therefore, be recommended that the court deny Plaintiff's motion for summary judgment as to this issue.

### **III. Conclusion**

For the reasons discussed herein, it is recommended that Plaintiff's motion for partial summary judgment be **GRANTED** as to whether Defendant has literally infringed Claims 8, 12, 13, and 14 of the '516 patent, and **DENIED** as to the issues of inequitable conduct, fraud, anti-trust liability, and marking.

Wallace W. Dixon

United States Magistrate Judge

Durham, NC

August 1, 2005

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End of Document



## McBee v. Delica Co.

United States Court of Appeals for the First Circuit

August 2, 2005, Decided

No. 04-2733

### **Reporter**

417 F.3d 107 \*; 2005 U.S. App. LEXIS 15826 \*\*; 75 U.S.P.Q.2D (BNA) 1609 \*\*\*; 2005-2 Trade Cas. (CCH) P74,904

CECIL McBEE, Plaintiff, Appellant, v. DELICA CO., LTD., Defendant, Appellee.

**Prior History:** [\*\*1] APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF MAINE.  
[Hon. Gene Carter, Senior U.S. District Judge].

*[McBee v. Delica Co., 2004 U.S. Dist. LEXIS 23414 \(D. Me., Nov. 19, 2004\)](#)*

## **Core Terms**

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Lanham Act, sales, website, extraterritorial, commerce, subject matter jurisdiction, substantial effect, consumers, trademark, products, personal jurisdiction, district court, no evidence, infringing, injunction, clothing, shipped, investigators, domestic, touring, courts, McBee's Lanham Act, cases, magistrate judge, endorsement, import, claim for damages, reputation, questions, purposes

## **LexisNexis® Headnotes**

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Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

International Law > Authority to Regulate > General Overview

International Law > Dispute Resolution > Tribunals

### **HN1[] Lanham Act, Extraterritorial Jurisdiction**

In addressing questions of extraterritoriality, the United States Supreme Court considers Congressional intent, employing various presumptions designed to avoid unnecessary international conflict. Unless a contrary intent appears, legislation of Congress is meant to apply only within the territorial jurisdiction of the United States.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

International Law > Authority to Regulate > General Overview

Trademark Law > ... > Infringement Actions > Jurisdiction > Extraterritorial Jurisdiction

## **HN2** Lanham Act, Extraterritorial Jurisdiction

The Lanham Act can sometimes be used to reach extraterritorial conduct, but the United States Supreme Court has never laid down a precise test for when such reach would be appropriate. Circuit courts have established a variety of tests for determining when extraterritorial application of the Lanham Act is appropriate, treating different factual contexts as all subject to the same set of criteria.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

International Law > ... > Comity Doctrine > Areas of Law > Commercial Transactions

International Law > Authority to Regulate > General Overview

International Law > Dispute Resolution > Comity Doctrine > General Overview

Trademark Law > ... > Infringement Actions > Jurisdiction > Extraterritorial Jurisdiction

## **HN3** Lanham Act, Extraterritorial Jurisdiction

To demonstrate extraterritorial application, a Lanham Act (Act) plaintiff must show (1) some effect on United States commerce, (2) an effect that is sufficiently great to be a cognizable injury to plaintiff under the Act, and (3) the interests and links to American commerce that are sufficiently strong in relation to those of other nations to justify, in terms of comity, an extraterritorial application of the Act.

International Trade Law > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > Jurisdiction

## **HN4** International Trade Law

The Lanham Act (Act) confers broad jurisdiction, as its purpose is to regulate commerce within the control of Congress. [15 U.S.C.S. § 1127](#). The Act prohibits the use of certain infringing marks in commerce. [15 U.S.C.S. §§ 1114\(1\), 1125\(a\)](#). Commerce is defined, in [§ 1127](#) of the Act, as all commerce which may lawfully be regulated by Congress.

Governments > Federal Government > General Overview

International Law > Authority to Regulate > General Overview

International Trade Law > General Overview

## **HN5** Governments, Federal Government

The power of Congress to regulate the conduct of its own citizens may extend to extraterritorial conduct. That doctrine is based on the idea that Congressional power over American citizens is a matter of domestic law that raises no serious international concerns, even when the citizen is located abroad.

International Law > Authority to Regulate > General Overview

International Trade Law > General Overview

Transportation Law > Interstate Commerce > Federal Powers

#### **HN6** International Law, Authority to Regulate

An American citizen cannot evade the thrust of the laws of the United States by moving his or her operations to a privileged sanctuary beyond its borders.

Business & Corporate Law > Foreign Corporations > General Overview

International Law > Authority to Regulate > Anticompetitive Activities

Trademark Law > Causes of Action Involving Trademarks > Infringement Actions > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

Trademark Law > ... > Infringement Actions > Jurisdiction > Extraterritorial Jurisdiction

#### **HN7** Business & Corporate Law, Foreign Corporations

When a purported trademark infringer is not an American citizen, and the alleged illegal activities occur outside the United States, the analysis appears to rest solely on the foreign commerce power. However, the Lanham Act can be applied against foreign corporations or individuals in appropriate cases.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

International Trade Law > General Overview

Trademark Law > Foreign & International Protection > Enforcement of Foreign Trademark Rights

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Trademark Law > Conveyances > General Overview

Trademark Law > Foreign & International Protection > General Overview

#### **HN8** Lanham Act, Extraterritorial Jurisdiction

In both the antitrust and the Lanham Act areas, there is a risk that absent a certain degree of extraterritorial enforcement, violators will either take advantage of international coordination problems or hide in countries without efficacious antitrust or trademark laws, thereby avoiding legal authority.

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

417 F.3d 107, \*107LAW2005 U.S. App. LEXIS 15826, \*\*1LAW25 U.S.P.Q.2D (BNA) 1609, \*\*\*1609

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Sherman Act > Jurisdiction

International Law > Authority to Regulate > General Overview

### **HN9** [blue icon] International Aspects, International Application of US Law

American jurisdiction over foreign conduct exists under the antitrust laws if that conduct is meant to produce and does in fact produce some substantial effect in the United States.

Business & Corporate Compliance > ... > Dispute Resolution > Conflict of Law > Jurisdiction

Civil Procedure > ... > Jurisdiction > Jurisdictional Sources > General Overview

Governments > Courts > Judicial Comity

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

International Law > Dispute Resolution > Comity Doctrine > General Overview

### **HN10** [blue icon] Conflict of Law, Jurisdiction

Comity considerations, such as whether relief ordered by an American court would conflict with foreign law, are properly understood not as questions of whether a United States court possesses subject matter jurisdiction, but instead as issues of whether such a court should decline to exercise the jurisdiction that it possesses.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

International Law > Authority to Regulate > Anticompetitive Activities

International Trade Law > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

### **HN11** [blue icon] Lanham Act, Extraterritorial Jurisdiction

The United States Court of Appeals for the First Circuit holds that the Lanham Act grants subject matter jurisdiction over extraterritorial conduct by foreign defendants only where the conduct has a substantial effect on United States commerce. Absent a showing of such a substantial effect, at least as to foreign defendants, the court lacks jurisdiction over the Lanham Act claim. Congress has little reason to assert jurisdiction over foreign defendants who are engaging in activities that have no substantial effect on the United States, and courts, absent an express statement from Congress, have no good reason to go further in such situations. Where the government's interest in a transaction is remote, minor, tangential, or otherwise insignificant, the government would presumably not seek to control it.

Antitrust & Trade Law > Consumer Protection > General Overview

Trademark Law > ... > Infringement Actions > Jurisdiction > Extraterritorial Jurisdiction

## **HN12** [blue icon] Antitrust & Trade Law, Consumer Protection

The substantial effects test requires that there be evidence of impacts within the United States, and these impacts must be of a sufficient character and magnitude to give the United States a reasonably strong interest in the litigation. The "substantial effects" test must be applied in light of the core purposes of the Lanham Act, which are both to protect the ability of American consumers to avoid confusion and to help assure a trademark's owner that it will reap the financial and reputational rewards associated with having a desirable name or product. The goal of the jurisdictional test is to ensure that the United States has a sufficient interest in the litigation, as measured by the interests protected by the Lanham Act, to assert jurisdiction.

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

Governments > Courts > Judicial Comity

Trademark Law > ... > Infringement Actions > Jurisdiction > Extraterritorial Jurisdiction

## **HN13** [blue icon] Lanham Act, Extraterritorial Jurisdiction

Where the substantial effects test is met in a Lanham Act claim against a foreign defendant, the court should proceed, in appropriate cases, to consider the doctrine of comity.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

## **HN14** [blue icon] Standards of Review, De Novo Review

Where all the relevant facts are undisputed and a district court did not make any finding of fact, an appellate court's review of a challenge for lack of subject matter jurisdiction is de novo, and the burden is on the party asserting the claim to establish jurisdiction.

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

Trademark Law > ... > Infringement Actions > Jurisdiction > General Overview

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Civil Procedure > Remedies > Injunctions > Preliminary & Temporary Injunctions

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

Trademark Law > ... > Remedies > Equitable Relief > General Overview

#### **HN15** [blue icon] Contracts, Sales of Goods

Congress has the power to enjoin sales of infringing goods into the United States, and, as a matter of Congressional intent, Congress intended to reach such sales via the Lanham Act. Courts distinguish between domestic acts of a foreign infringer and foreign acts of that foreign infringer; the extraterritoriality analysis to determine jurisdiction attaches only to the latter.

Antitrust & Trade Law > Sherman Act > General Overview

International Trade Law > General Overview

#### **HN16** [blue icon] Antitrust & Trade Law, Sherman Act

See [15 U.S.C.S. § 6\(a\)\(1\)](#).

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction

Computer & Internet Law > Civil Actions > Jurisdiction > Constitutional Limitations

Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview

Civil Procedure > ... > Jurisdiction > In Rem & Personal Jurisdiction > General Overview

Computer & Internet Law > Internet Business > General Overview

Computer & Internet Law > ... > Trademark Protection > Civil Infringement Actions > General Overview

#### **HN17** [blue icon] Lanham Act, Extraterritorial Jurisdiction

The mere existence of a website that is visible in a forum and that gives information about a company and its products is not enough, by itself, to subject a defendant to personal jurisdiction in that forum. Something more is necessary, such as interactive features which allow the successful online ordering of the defendant's products. The mere existence of a website does not show that a defendant is directing its business activities towards every forum where the website is visible; as well, given the omnipresence of Internet websites today, allowing personal jurisdiction to be premised on such a contact alone would eviscerate the limits on a state's jurisdiction over out-of-state or foreign defendants.

Trademark Law > ... > Damages > Types of Damages > Compensatory Damages

Trademark Law > Conveyances > General Overview

Trademark Law > Causes of Action Involving Trademarks > Dilution of Famous Marks > General Overview

Trademark Law > Likelihood of Confusion > Consumer Confusion > General Overview

#### **HN18** [blue icon] Types of Damages, Compensatory Damages

Confusion and reputational harm in the eyes of American consumers can often, although not always, be inferred from the fact that American consumers have been exposed to an infringing mark. But no inference of dilution or other harm can be made where American citizens are not exposed to the infringing product.

[Business & Corporate Law > Foreign Corporations > General Overview](#)

[International Trade Law > General Overview](#)

[Trademark Law > Conveyances > General Overview](#)

[Antitrust & Trade Law > International Aspects > International Application of US Law > General Overview](#)

[Business & Corporate Compliance > ... > Federal Unfair Competition Law > Lanham Act > Extraterritorial Jurisdiction](#)

## **[HN19](#)[] Business & Corporate Law, Foreign Corporations**

Courts may consider sales diverted from American companies in foreign countries in their analyses of a Lanham Act claim against a foreign defendant.

[Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview](#)

[Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview](#)

[Civil Procedure > Sanctions > Baseless Filings > General Overview](#)

## **[HN20](#)[] Subject Matter Jurisdiction, Jurisdiction Over Actions**

A federal court lacks subject matter jurisdiction over claims that involve no real federal controversy, where the claims clearly appear to be immaterial and made solely for the purpose of obtaining jurisdiction or where such a claim is wholly insubstantial and frivolous. The test is whether, legally, there is any real federal interest involved in the case.

[Civil Procedure > ... > Jurisdiction > In Rem & Personal Jurisdiction > General Overview](#)

[Constitutional Law > ... > Fundamental Rights > Procedural Due Process > General Overview](#)

[Civil Procedure > ... > Justiciability > Case & Controversy Requirements > General Overview](#)

[Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > General Overview](#)

[Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview](#)

[Civil Procedure > ... > Federal & State Interrelationships > State Sovereign Immunity > State Immunity](#)

## **[HN21](#)[] Jurisdiction, In Rem & Personal Jurisdiction**

The requirements of personal jurisdiction are not rooted in U.S. Const. art. III, although they do have constitutional resonance through the Due Process clause. Unlike subject matter jurisdiction under Article III, which goes to the

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fundamental institutional competence of the court and can be raised *sua sponte* at any time, personal jurisdiction is an individual liberty right and is therefore waivable; a court cannot raise personal jurisdiction *sua sponte*.

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Personam Actions > General Overview

## **HN22**[ **In Rem & Personal Jurisdiction, In Personam Actions**

A court will not force a defendant to expend resources on difficult personal jurisdiction issues and will not reach more difficult issues where there is an exceptionally easy method on the merits for the defendant to prevail.

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

## **HN23**[ **Appellate Review, Standards of Review**

Where questions raised on appeal were decided on a summary judgment record, the reviewing court may affirm on any ground supported by that record.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > ... > Subject Matter Jurisdiction > Supplemental Jurisdiction > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Supplemental Jurisdiction > Pendent Claims

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

## **HN24**[ **Estoppel, Collateral Estoppel**

Absent any viable federal claim, a district court's dismissal of pendent state law claims without prejudice to their being refiled in state court is fully appropriate and not an abuse of discretion.

**Counsel:** Alfred C. Frawley, with whom Robert O. Newton and Preti, Flaherty, Beliveau, Pachios & Haley, LLP were on brief, for plaintiff, appellant.

Todd S. Holbrook, with whom John G. Osborn and Bernstein, Shur, Sawyer & Nelson were on brief, for defendant, appellee.

**Judges:** Before Selya, Lynch, and Howard, Circuit Judges.

**Opinion by:** LYNCH

## **Opinion**

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[\*\*\*1610] [\*110] **LYNCH, Circuit Judge.** It has long been settled that the *Lanham Act* can, in appropriate cases, be applied extraterritorially. See *Steele v. Bulova Watch Co.*, 344 U.S. 280, 97 L. Ed. 319, 73 S. Ct. 252, 1953 Dec.

Comm'r Pat. 424 (1952). This case, dismissed for lack of subject matter jurisdiction, requires us, as a matter of first impression for this circuit, to lay out a framework for determining when such extraterritorial use of the Lanham Act is proper.

In doing so, we choose not to adopt the formulations used by various other circuits. See, e.g., Reebok Int'l, Ltd. v. Marnatech Enters., 970 F.2d 552, 554-57 (9th Cir. 1992); Vanity Fair Mills v. T. Eaton Co., 234 F.2d 633, 642-43 (2d Cir. 1956). [\*\*2] The best-known test, the *Vanity Fair* test, asks (1) whether the defendant is an American citizen, (2) whether the defendant's [\*111] actions have a substantial effect on United States commerce, and (3) whether relief would create a conflict with foreign law. 234 F.2d at 642-43. These three prongs are given an uncertain weight. Based on *Steele* and subsequent Supreme Court case law, we disaggregate the three prongs of the *Vanity Fair* test, identify the different types of "extraterritorial" application questions, and isolate the factors pertinent to subject matter jurisdiction.

Our framework asks first whether the defendant is an American citizen; that inquiry is different because a separate constitutional basis for jurisdiction exists for control of activities, even foreign activities, of an American citizen. Further, when the Lanham Act plaintiff seeks to enjoin sales in the United States, there is no question of extraterritorial application; the court has subject matter jurisdiction. [\*\*\*1611]

In order for a plaintiff to reach foreign activities of foreign defendants in American courts, however, we adopt a separate test. We hold that subject matter jurisdiction under the [\*\*3] Lanham Act is proper only if the complained-of activities have a substantial effect on United States commerce, viewed in light of the purposes of the Lanham Act. If this "substantial effects" question is answered in the negative, then the court lacks jurisdiction over the defendant's extraterritorial acts; if it is answered in the affirmative, then the court possesses subject matter jurisdiction.

We reject the notion that a comity analysis is part of subject matter jurisdiction. Comity considerations, including potential conflicts with foreign trademark law, are properly treated as questions of whether a court should, in its discretion, decline to exercise subject matter jurisdiction that it already possesses. Our approach to each of these issues is in harmony with the analogous rules for extraterritorial application of the antitrust laws. See Hartford Fire Ins. Co. v. California, 509 U.S. 764, 795-99, 125 L. Ed. 2d 612, 113 S. Ct. 2891 (1993).

The plaintiff, Cecil McBee, an American citizen and resident, seeks to hold the defendant, Delica Co., Ltd. (Delica), responsible for its activities in Japan said to harm McBee's reputation in both Japan and the United States and for Delica's [\*4] purported activities in the United States. McBee is a well-known American jazz musician; Delica is a Japanese corporation that adopted the name "Cecil McBee" for its adolescent female clothing line. McBee sued for false endorsement and dilution under the Lanham Act. The district court dismissed all of McBee's Lanham Act claims, concluding that it lacked subject matter jurisdiction. See McBee v. Delica Co., 2004 U.S. Dist. LEXIS 23414, No. 02-198-P-C, 2004 WL 2674360 (D. Me. Nov. 19, 2004) (unpublished).

We affirm, albeit on different reasoning. We conclude that the court lacked jurisdiction over McBee's claims seeking (1) an injunction in the United States barring access to Delica's Internet website, which is written in Japanese, and (2) damages for harm to McBee due to Delica's sales in Japan. McBee has made no showing that Delica's activities had a substantial effect on United States commerce. As to McBee's claim for (3) an injunction barring Delica from selling its goods in the United States, we hold that the district court had jurisdiction but conclude that this claim is without merit because the only sales Delica has made into the United States were induced by McBee for purposes of [\*\*5] this litigation, and there is no showing that Delica plans on selling into the United States again.

## I.

The relevant facts are basically undisputed. McBee, who lives in both Maine [\*112] and New York, is a jazz bassist with a distinguished career spanning over forty-five years. He has performed in the United States and worldwide, has performed on over 200 albums, and has released six albums under his own name (including in Japan). He won a Grammy Award in 1989, was inducted into the Oklahoma Jazz Hall of Fame in 1991, and

teaches at the New England Conservatory of Music in Boston. McBee has toured Japan several times, beginning in the early 1980s, and has performed in many major Japanese cities, including Tokyo. He continues to tour in Japan. McBee has never licensed or authorized the use of his name to anyone, except of course in direct connection with his musical performances, as for example on an album. In his own words, he has sought to "have [his] name associated only with musical excellence."

Delica is a Japanese clothing retailer. In 1984, Delica adopted the trade name "Cecil McBee" for a line of clothing and accessories primarily marketed to teen-aged girls. Delica holds **[\*\*6]** a Japanese trademark for "Cecil McBee," in both Japanese and Roman or English characters, for a variety of product types. Delica owns and operates retail shops throughout Japan under the brand name "Cecil McBee"; these are the only stores where "Cecil McBee" products are sold. There are no "Cecil McBee" retail shops outside of Japan. Delica sold approximately \$ 23 million worth of "Cecil McBee" goods in 1996 and experienced steady growth in sales in subsequent years; in 2002, Delica sold \$ 112 million worth of "Cecil McBee" goods.

Delica puts out a "style book" or catalog that includes pictures and descriptions of the products in its "Cecil McBee" line; this style book is written in Japanese with some English words for effect. The style book is available in Japan at the retail stores and in certain other locations; sometimes it is included with shipped packages of "Cecil McBee" products. The style book contains telephone and fax numbers which allow a customer to order "Cecil McBee" merchandise from another **[\*\*\*1612]** company, Opus M. Co., Ltd., and have it shipped directly to the customer. Opus M. Co. buys the goods from Delica for this purpose, and then uses yet another company, Hamasho Co. **[\*\*7]**, Ltd., to do the shipping. It is undisputed that Hamasho Co. has never shipped any "Cecil McBee" goods outside of Japan. As described later, Delica's policy generally is to decline orders from the United States.

Delica operates a website, <http://www.cecilmcbee.net>, which contains pictures and descriptions of "Cecil McBee" products, as well as locations and telephone numbers of retail stores selling those products. The website is created and hosted in Japan, and is written almost entirely in Japanese, using Japanese characters (although, like the style book, it contains some English words). The website contains news about the "Cecil McBee" line, including promotions. Customers can log onto the site to access their balance of bonus "points" earned for making past "Cecil McBee" purchases, as well as information about how to redeem those points for additional merchandise. However, the site does not allow purchases of "Cecil McBee" products to be made online. The website can be viewed from anywhere in the Internet-accessible world.

McBee produced evidence that, when searches on Internet search engines (such as Google) are performed for the phrase "Cecil McBee," Delica's website ([www.cecilmcbee.net](http://www.cecilmcbee.net)) generally comes up as one of the first few results, and occasionally comes up first, ahead of any of the various websites that describe the musical accomplishments of the plaintiff. Certain other websites associated with Delica's "Cecil **[\*113]** McBee" product line also come up when such searches are performed; like [www.cecilmcbee.net](http://www.cecilmcbee.net), it is evident from the search results page that these websites are written primarily in Japanese characters.

In 1995, plaintiff McBee became aware that Delica was using his name, without his authorization, for a line of clothing in Japan. He contacted an American lawyer, who advised him that Delica was unlikely to be subject to personal jurisdiction in the United States. McBee retained a Japanese attorney, who sent a letter to Delica asking it to cease using the "Cecil McBee" name. When Delica declined, McBee petitioned the Japanese Patent Office to invalidate Delica's English-language trademark on "Cecil McBee."

On February 28, 2002, the Japanese Patent Office ruled Delica's trademark in Japan invalid. However, Delica appealed to the Tokyo High Court, which on December 26, 2002, vacated the decision of the Japanese Patent Office. On remand, **[\*\*9]** the Japanese Patent Office found for Delica and reinstated Delica's registration of the "Cecil McBee" trademark. McBee appealed that ruling to the Tokyo High Court and lost; the trademark reinstatement has become final.<sup>1</sup>

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<sup>1</sup> The Japanese courts' rationale for finding in favor of Delica was (1) while Japanese law protects a person's full name from exploitation, McBee's full name, including his middle name, was "Cecil Leroy McBee," and thus the "Cecil McBee" line of

In early 2002, Delica formulated a policy not to sell or ship "Cecil McBee" brand products to the United States and informed its managers throughout the company. Delica's admitted reason for this policy was to prevent McBee from being able to sue Delica in the United States.

McBee was beginning to consider just such a [\*\*10] strategy. From December 2001 through early 2003, McBee retained three Japanese-speaking investigators to attempt to purchase "Cecil McBee" products from Delica and have them shipped to Maine. They met with mixed success. One initially, in December 2001, contacted the webmaster of <http://www.cecilmcbee.net> by email, asking about certain jewelry displayed on the website; that webmaster referred the investigator to the "Cecil McBee" retail shops in Japan for further information, but noted that at that time only domestic shipping was available.

The investigators then used the telephone numbers on the <http://www.cecilmcbee.net> website to contact various "Cecil McBee" retail stores in Japan directly. The investigators made it clear that they were residents of the United States inquiring about purchasing "Cecil McBee" goods. When the investigators requested an opportunity to buy merchandise and have it shipped to them in Maine, some stores stated that this could not be done, some of the stores worked out an arrangement whereby they would ship to an address in Japan [\*\*\*1613] but the investigator would then arrange to have the products forwarded to Maine, and some of the stores, at various times, shipped [\*\*11] directly to the investigators in Maine. The total value of "Cecil McBee" merchandise purchased by these three investigators -- including both goods shipped directly to Maine by Delica and goods shipped via the indirect method -- was approximately \$ 2,500. As counsel for McBee has conceded, there is no evidence of any other "Cecil McBee" sales by Delica to the United States.

Further, there is virtually no evidence of "Cecil McBee" brand goods entering the [\*114] United States after being sold by Delica in Japan. McBee stated in affidavit that "friends, fellow musicians, fans, students, and others . . . have reported seeing [his] name on clothing, shopping bags [and] merchandise (whether worn or carried by a young girl walking on the street in Boston or New York or elsewhere) . . . ." But no further evidence or detail of these sightings in the United States was provided. McBee also provided evidence that Cecil McBee goods have occasionally been sold on eBay, an auction website that allows bids to be placed and items sold anywhere in the world. Most of the sellers were not located in the United States, and there is no evidence that any of the items were purchased by American buyers.

[\*\*12] McBee states that he finds the use of his name by Delica "undignified, highly offensive and repugnant." He feels that he has been harmed by Delica's use of his name because people have reported to him that they have seen his name on Delica's products, either in the United States or in Japan, or on Delica's website, and have asked him if he endorsed those products. Even when he denies having a relationship with Delica, some people do not believe him, and some have asked him, "both in jest and with some degree of seriousness," whether he is "into young girls," the target audience for Delica's "Cecil McBee" line.<sup>2</sup>

McBee produces little evidence relating to the frequency of such incidents, [\*\*13] nor does he give many specific examples. He testified in deposition that two of his American friends and fellow musicians, while touring Japan, had seen a "Cecil McBee" advertisement created by Delica and had become confused as to whether McBee had some relationship with a clothing line; they asked McBee about the relationship when they returned to the United States. McBee told some of his students at the New England Conservatory of Music about his lawsuit against Delica, in order to help them understand the value of intellectual property law to a musician; some of his students found the Delica website and started rumors of his having a relationship with a women's clothing company. He feels that some of his students may have lost their focus during his classes because they are thinking about his connection to

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products was not an exact copy of McBee's full name; and (2) McBee received no protection for the abbreviated version of his name, "Cecil McBee," because the name had not received sufficient recognition in general Japanese society.

<sup>2</sup> McBee's expert, Joseph McNulty, testified that Delica's use of the name "Cecil McBee" on its Internet website could decrease McBee's ability to receive compensation for lending his name to another company's brand. However, as McBee's own brief points out, McBee has never shown any interest in this kind of product marketing.

women's clothing. Further, his class enrollment has dropped "for one reason or another" and so his position as a professor at the Conservatory has been made more uncertain.

McBee has seen his own name on "Cecil McBee" merchandise in Japan while touring and has become angry. His Japanese touring partner during his recent tours of Japan (from 2002 onwards) has made announcements [\*\*14] before concerts that McBee had no relationship with the Delica clothing line. In McBee's view, his audience of Japanese fans at his concerts has become younger through time and therefore more in line with the core age group of consumers for Delica's brand. McBee also notes that a fan once came up to him while he was performing in Taiwan to speak with him about Delica's line; the fan apparently presumed a connection between McBee and the line. As of 2003, McBee only had one regular tour in Japan each year, lasting three weeks or so each time; in McBee's view "it is speculating, but it is . . . possible" that Delica's "Cecil McBee" brand had led to his failure to receive additional Japanese touring opportunities.

#### [\*115] II.

McBee's complaint, filed October 1, 2002, alleged trademark dilution and unfair competition claims under the Lanham Act, [15 U.S.C. § 1051 et seq.](#), as well as various pendent Maine state law claims. McBee requested injunctive relief, damages, and attorney's fees. The core of McBee's Lanham Act claims is false endorsement: that the unlicensed use of his name has "made a misleading and false inference" that McBee endorses, approves, or [\*\*\*1614] sponsors [\*\*15] Delica's product, and that inference has caused McBee harm. See [15 U.S.C. § 1125\(a\)](#); 4 J.T. McCarthy, *McCarthy on Trademarks and Unfair Competition* § 28.14, at 28-19 (4th ed. 2005); see also [Wendt v. Host Int'l, Inc., 125 F.3d 806, 812 \(9th Cir. 1997\)](#).

Delica first moved to dismiss the complaint, under [Fed. R. Civ. P. 12\(b\)\(2\)](#), on the ground that the Maine federal district court lacked personal jurisdiction over it. A magistrate judge recommended that the motion be denied, emphasizing the existence of Delica's website and the \$ 2,500 in sales to McBee's investigators in Maine, see [McBee v. Delica Co., 2003 U.S. Dist. LEXIS 6123, No. 02-198-P-C, 2003 WL 1872907 \(D. Me. April 14, 2003\)](#) (unpublished); the district court adopted the magistrate judge's recommendation on July 9, 2003. Discovery proceeded. Delica then moved to dismiss McBee's complaint under [Fed. R. Civ. P. 12\(b\)\(1\)](#), asserting that the court lacked subject matter jurisdiction over McBee's Lanham Act claims because Delica's actions constituted extraterritorial conduct outside the ambit of the Act. [\*\*16] Delica also moved for summary judgment under [Fed. R. Civ. P. 56](#) based on laches, collateral estoppel due to the Japanese court decision against McBee, and various merits issues, including McBee's alleged failure to make a sufficient showing of likelihood of confusion to sustain his Lanham Act claims. McBee opposed but not on grounds of insufficient discovery, nor did he file a [Rule 56\(f\)](#) affidavit.

The magistrate judge issued a recommended decision on these motions on August 19, 2004.<sup>3</sup> See [McBee v. Delica Co., 2004 U.S. Dist. LEXIS 23415, No. 02-198-P-C, 2004 WL 2634465 \(D. Me. Aug. 19, 2004\)](#) (unpublished). On the subject matter jurisdiction question, the magistrate judge first noted that the Supreme Court had held, in [Steele v. Bulova Watch Co., 344 U.S. 280, 97 L. Ed. 319, 73 S. Ct. 252, 1953 Dec. Comm'r Pat. 424 \(1952\)](#), that the Lanham Act could, in some circumstances, be applied to reach extraterritorial conduct. See [McBee, 2004 U.S. Dist. LEXIS 23415, 2004 WL 2634465, at \\*2](#). The magistrate judge also noted that this circuit has never laid out a test for when such extraterritorial application is appropriate. See [id. 2004 U.S. Dist. LEXIS 23415, at \[WL\] \\*2 n.3](#). The magistrate judge thus utilized the test stated [\*\*17] by the Second Circuit in [Vanity Fair Mills, Inc. v. T. Eaton Co., 234 F.2d 633, 642 \(2d Cir. 1956\)](#), described earlier. See [McBee, 2004 U.S. Dist. LEXIS 23415, 2004 WL 2634465, at \\*2](#). However, the magistrate judge accepted the Fifth Circuit's modification of the first prong in [Am. Rice, Inc. v. Arkansas Rice Growers Coop. Ass'n, 701 F.2d 408, 414 n.8 \(5th Cir. 1983\)](#), and required

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<sup>3</sup> Delica's laches claim was rejected in a separate, earlier recommended decision of the magistrate judge, see [McBee v. Delica Co., 2003 U.S. Dist. LEXIS 20132, No. 02-198-P-C, 2003 WL 22586387 \(D. Me. Nov. 10, 2003\)](#) (unpublished), which was adopted by the district court.

a showing of only "some" effect on United States commerce. See [McBee, 2004 U.S. Dist. LEXIS 23415, 2004 WL 2634465, at \\*4](#). The magistrate judge recommended that all of McBee's Lanham Act claims for injunctive relief be dismissed because they failed two of the three *Vanity Fair* factors, but that all of his Lanham Act damages claims be allowed to go forward because they met two prongs of the test.<sup>4</sup> See [id. 2004 U.S. Dist. LEXIS 23415, at \[WL\] \\*3-\\*4](#).

**[\*\*18] [\*116]** Delica filed an objection, arguing that all of McBee's Lanham Act claims -- and not just those claims requesting injunctive relief -- failed the *Vanity Fair* test for extraterritorial application. McBee moved that the recommended decision be modified. He conceded that American courts had no extraterritorial jurisdiction to enjoin sales that occurred in Japan, but argued that there was jurisdiction for his damages claim against those sales. McBee also stated that he sought an injunction against Delica's sales of "Cecil McBee" goods in the United States and against Delica's use of the "Cecil McBee" website to reach United States consumers; these forms of relief, he argued, did not constitute extraterritorial applications of the Lanham Act at all and therefore the court should assert subject matter jurisdiction over them.

The district court amended the magistrate judge's recommended decision by holding that it lacked subject matter jurisdiction over all of McBee's Lanham Act claims, including both those for injunctive relief and damages. See [McBee v. Delica Co., 2004 U.S. Dist. LEXIS 23414, No. 02-198-P-C, 2004 WL 2674360 \(D. Me. Nov. 19, 2004\)](#) (unpublished). The district court, like the **[\*\*19]** magistrate judge, applied essentially the test laid out by the Second Circuit in *Vanity Fair*. See [id. 2004 U.S. Dist. LEXIS 23414, at \[WL\] \\*1](#). But the district court disagreed with the magistrate judge's application of that **[\*\*1615]** test, finding that a claim for damages, like a claim for injunctive relief, would create a conflict with Japanese trademark law. See [id. 2004 U.S. Dist. LEXIS 23414, at \[WL\] \\*2](#). Finding two of the three factors unsatisfied, the court ordered McBee's Lanham Act claims dismissed for lack of subject matter jurisdiction without considering the effect of Delica's actions on United States commerce. See *id.* With respect to this factor, however, the court noted that Delica's only sales into the United States "appear to have been made for purposes of this lawsuit alone." [Id. 2004 U.S. Dist. LEXIS 23414, at \[WL\] \\*1 n.2](#). After dismissing McBee's Lanham Act claims, the court declined to exercise supplemental jurisdiction over his pendent state law claims. See [id. 2004 U.S. Dist. LEXIS 23414, at \[WL\] \\*2](#). This made it unnecessary for the court to consider Delica's summary judgment motion on other bases.

On appeal, McBee renews his argument that his claims for a domestic injunction, both against Delica's sales into the United States and against its broadcasting of its website in the United **[\*\*20]** States, do not constitute extraterritorial applications of the Lanham Act at all. Further, while McBee concedes that United States courts lack jurisdiction over his Lanham Act claim for an injunction against Delica's sales in Japan, he argues that the district court had extraterritorial jurisdiction over damages claims against those same sales. Delica responds by arguing that United States courts lack extraterritorial jurisdiction over all of McBee's Lanham Act claims, and further urges lack of personal jurisdiction, preclusion due to collateral estoppel based on the Japanese judgment, and laches as alternative grounds for affirmance.

### III.

#### A. Framework for Assessing Extraterritorial Use of the Lanham Act

By extraterritorial application of the Lanham Act, we mean application of the Act to activity (such as sales) of a defendant outside of the territorial boundaries of the United States. In addressing extraterritorial application of the Lanham Act, we face issues of Congressional intent to legislate extraterritorially, undergirded by issues of Congressional power to legislate extraterritorially. [HN1↑](#) Usually in addressing **[\*117]** questions of extraterritoriality, the Supreme Court **[\*\*21]** has discussed Congressional intent, doing so by employing various

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<sup>4</sup> The magistrate judge recommended that Delica's motion for summary judgment on the remaining Lanham Act damages claims and on the various pendent state law claims be denied. See [McBee, 2004 U.S. Dist. LEXIS 23415, 2004 WL 2634465, at \\*5-\\*15](#).

presumptions designed to avoid unnecessary international conflict. See, e.g., [Spector v. Norwegian Cruise Line Ltd.](#), 545 U.S. 119, 162 L. Ed. 2d 97, 125 S. Ct. 2169, 2177 (2005); [F. Hoffmann-La Roche Ltd. v. Empagran S.A.](#), 542 U.S. 155, 124 S. Ct. 2359, 2366-73, 159 L. Ed. 2d 226 (2004); see also [EEOC v. Arabian Am. Oil Co.](#), 499 U.S. 244, 248, 113 L. Ed. 2d 274, 111 S. Ct. 1227 (1991) ("It is a longstanding principle of American law that legislation of Congress, unless a contrary intent appears, is meant to apply only within the territorial jurisdiction of the United States." (internal quotation marks and citation omitted)).

The parties characterize the extraterritoriality issue as, at least in part, one of subject matter jurisdiction under the Act, and it is often viewed that way. See, e.g., [Levi Strauss & Co. v. Sunrise Int'l Trading Co.](#), 51 F.3d 982, 984 (11th Cir. 1995); [Ocean Garden, Inc. v. Marktrade Co., Inc.](#), 953 F.2d 500, 502 (9th Cir. 1991); see also [United Phosphorus, Ltd. v. Angus Chem. Co.](#), 322 F.3d 942, 945-51 (7th Cir. 2003) [\*\*22] (en banc) (question whether [Sherman Act](#) applied extraterritorially under the Foreign Trade Antitrust Improvements Act (FTAIA), [15 U.S.C. § 6a](#), went to subject matter jurisdiction of court).

The Supreme Court has long since made it clear that [HN2](#) [↑] the Lanham Act could sometimes be used to reach extraterritorial conduct, but it has never laid down a precise test for when such reach would be appropriate.<sup>5</sup> [Steele v. Bulova Watch Co.](#), 344 U.S. 280, 97 L. Ed. 319, 73 S. Ct. 252, 1953 Dec. Comm'r Pat. 424 (1952); see also [Arabian Am. Oil Co.](#), 499 U.S. at 252-53 (distinguishing Steele). The circuit courts have established a variety of tests for determining when extraterritorial application of the Lanham Act is appropriate, treating different factual contexts as all subject to the same set of criteria. See [Vanity Fair Mills v. T. Eaton Co.](#), 234 F.2d 633, 642 (2d Cir. 1956); see also [Int'l Cafe, S.A.L., v. Hard Rock Cafe Int'l \(U.S.A.\), Inc.](#), 252 F.3d 1274, 1278-79 (11th Cir. 2001) (applying [Vanity Fair](#)); [Nintendo of Am., Ltd., v. Aeropower Co.](#), 34 F.3d 246, 250-51 (4th Cir. 1994) (adopting the [Vanity Fair](#) [\*\*23] test, although [\*\*\*1616] requiring a "significant effect" rather than a "substantial effect" on United States commerce); [Reebok Int'l, Ltd. v. Marnatech Enters., Inc.](#), 970 F.2d 552, 554-57 (9th Cir. 1992) (applying the jurisdictional "rule of reason" from [Timberlane Lumber Co. v. Bank of Am.](#), 549 F.2d 597 (9th Cir. 1977)): [HN3](#) [↑] plaintiff must show (1) some effect on United States commerce, (2) an effect that is sufficiently great to be a cognizable injury to plaintiff under the Lanham Act, and (3) the interests and links to American commerce must be sufficiently strong in relation to those of other nations to justify, in terms of comity, an extraterritorial application of the act); [Am. Rice, Inc. v. Ark. Rice Growers Coop. Ass'n](#), 701 F.2d 408, 414 & n. 8 (5th Cir. 1983) (modifying [Vanity Fair](#)'s first prong to require only "some effect" on United States commerce). This court has not previously addressed the question.

[\*\*24] [Steele](#) found that there was Lanham Act jurisdiction over a defendant, selling watches in Mexico, who was a United States citizen and whose "operations and their effects were not confined within the [\*118] territorial limits of a foreign nation."<sup>6</sup> [344 U.S. at 286](#). Defendant made no sales within the United States. The Court held that [HN4](#) [↑] the Lanham Act conferred broad jurisdiction in that its purpose was to regulate "commerce within the control of Congress." [15 U.S.C. § 1127](#). The Act prohibits the use of certain infringing marks "in commerce." [15 U.S.C. § 1114\(1\)](#); *Id.* [§ 1125\(a\)](#). Importantly, commerce is defined in the Act as "all commerce which may lawfully be regulated by Congress." *Id.* [§ 1127](#).

[\*\*25] The [Steele](#) Court did not define the outer limits of Congressional power because it was clear that the facts presented a case within those limits. The [Steele](#) Court explicitly and implicitly relied on two different aspects of Congressional power to reach this conclusion. First, it explicitly relied on the [HN5](#) [↑] power of Congress to regulate "the conduct of its own citizens," even extraterritorial conduct. [Steele](#), 344 U.S. at 285-86. This doctrine is based on

<sup>5</sup> The Lanham Act was substantially amended in 1988, see [Trademark Law Revision Act of 1988](#), Pub. L. No. 100-667, 102 Stat. 3935, and was amended again in 1999, see [Trademark Amendments Act of 1999](#), Pub. L. No. 106-43, 113 Stat. 218, but the key jurisdictional language of the Lanham Act has remained unchanged since [Steele](#).

<sup>6</sup> The Court in a more recent case held that Title VII could not be applied extraterritorially at all, even to domestic employees working for domestic employers overseas. See [Arabian Am. Oil Co.](#), 499 U.S. at 250-54. The Court held that Title VII's jurisdictional language, in contrast to the language of the Lanham Act, did not evince a Congressional intent to apply Title VII abroad sufficient to overcome the presumption against such extraterritorial application. See *id.*

an idea that Congressional power over American citizens is a matter of domestic law that raises no serious international concerns, even when the citizen is located abroad. See [\*id. at 285-86\*](#) (citing [\*Skirioites v. Florida\*, 313 U.S. 69, 73, 85 L. Ed. 1193, 61 S. Ct. 924 \(1941\)](#)) (Florida state criminal law banning taking of sponges from high seas) and [\*Branch v. Federal Trade Comm'n\*, 141 F.2d 31, 35, 38 F.T.C. 857 \(7th Cir. 1944\)](#) (federal unfair competition law); see also [\*F. Hoffmann-La Roche Ltd.\*, 124 S. Ct. at 2367](#); [\*Cook v. Tait\*, 265 U.S. 47, 54-56, 68 L. Ed. 895, 44 S. Ct. 444, 1924-1 C.B. 73, T.D. 3594 \(1924\)](#) (income tax law); [\*Restatement \(Third\) of Foreign Relations Law of the United States\* § 402\(2\) \[\\*\\*26\]](#) (1986) ("[A] state has jurisdiction to prescribe law with respect to . . . the activities . . . of its nationals outside as well as within its territory.").<sup>7</sup> Second, Steele also implicitly appears to rely on Congressional power over foreign commerce, although the Foreign [\*Commerce clause\*](#) is not cited -- the Court noted that the defendant's actions had an impact on the plaintiff's reputation, and thus on commerce within the United States. See [\*344 U.S. at 286-87, 288\*](#). The Steele Court concluded that [\*HN6\*](#)<sup>↑</sup> an American citizen could not evade the thrust of the laws of the United States by moving his operations to a "privileged sanctuary" beyond our borders. [\*Id. at 287\*](#).

[\*\*27] For purposes of determining subject matter jurisdiction, we think certain distinctions are important at the outset. The reach of the Lanham Act depends on context; the nature of the analysis of the jurisdictional question may vary with that context. Steele addressed the pertinent Lanham Act jurisdictional analysis when an American citizen is the defendant. In such cases, the domestic effect of the international activities may be of lesser importance and a lesser showing of domestic effects may be all that is needed. We do not explore this further because our case does not involve an American citizen as the alleged infringer.

[\*HN7\*](#)<sup>↑</sup> [\*119] When the purported infringer is not an American citizen, and the alleged illegal activities occur outside the United States, then the analysis is different, and appears to rest solely on the foreign commerce power. Yet it is beyond much doubt that the Lanham Act [\*\*1617] can be applied against foreign corporations or individuals in appropriate cases; no court has ever suggested that the foreign citizenship of a defendant is always fatal. See, e.g., [\*Sterling Drug, Inc. v. Bayer AG\*, 14 F.3d 733, 746 \(2d Cir. 1994\)](#); [\*Wells Fargo & Co. v. Wells Fargo Express Co.\*, 556 F.2d 406, 429 \(9th Cir. 1977\)](#). [\*\*28] Some academics have criticized treating the Lanham Act differently from patent and copyright law, which generally are not applied extraterritorially. See C. Bradley, [\*Extraterritorial Application of U.S. Intellectual Property Law\*](#), [\*37 Va. J. Int'l L. 505 \(1997\)\*](#); but see R. Schechter, Comment, [\*The Case For Limited Extraterritorial Reach of the Lanham Act\*](#), [\*37 Va. J. Int'l L. 619 \(1997\)\*](#). Nonetheless, the Supreme Court recently reaffirmed the Steele approach to extraterritorial jurisdiction under the Lanham Act by distinguishing it in *Arabian American Oil Co.* See [\*499 U.S. at 252-53\*](#). The question becomes one of articulating a test for Lanham Act jurisdiction over foreign infringing activities by foreign defendants.

The decisions of the Supreme Court in the antitrust context seem useful to us as a guide. The Court has written in this area, on the issue of extraterritorial application, far more recently than it has written on the Lanham Act, and thus the decisions reflect more recent evolutions in terms of legal analysis of extraterritorial activity. As the Court noted in Steele, Lanham Act violations abroad often radiate unlawful [\*\*29] consequences into the United States, see [\*344 U.S. at 288\*](#); see also [\*Schechter, supra, at 629-30\*](#). One can easily imagine a variety of harms to American commerce arising from wholly foreign activities by foreign defendants. There could be harm caused by false endorsements, passing off, or product disparagement, or confusion over sponsorship affecting American commerce and causing loss of American sales. Further, global piracy of American goods is a major problem for American companies: annual losses from unauthorized use of United States trademarks, according to one commentator, now amount to \$ 200 billion annually. See [\*Schechter, supra, at 634\*](#). [\*HN8\*](#)<sup>↑</sup> In both the antitrust and the Lanham Act areas, there is a risk that absent a certain degree of extraterritorial enforcement, violators will either take advantage of international coordination problems or hide in countries without efficacious antitrust or trademark laws, thereby avoiding legal authority.

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<sup>7</sup> The nationality basis for extraterritorial jurisdiction is also explicit in certain statutes. For example, both the treason statute, see [\*18 U.S.C. § 1381\*](#), and the selective service statute, see 50 U.S.C. App. § 453, apply to all American citizens regardless of whether they might be located abroad.

In *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 125 L. Ed. 2d 612, 113 S. Ct. 2891 (1993), the Supreme Court addressed the issue of when a United States court could assert jurisdiction over Sherman Act [\*\*30] claims brought against foreign defendants for a conspiracy that occurred abroad to raise reinsurance prices. It held that [HN9](#) jurisdiction over foreign conduct existed under the antitrust laws if that conduct "was meant to produce and did in fact produce some substantial effect in the United States." *Id. at 796*; see also *United States v. Nippon Paper Indus. Co.*, 109 F.3d 1, 4 (1st Cir. 1997); *Doe I v. Unocal Corp.*, 395 F.3d 932, 961 (2d Cir. 2002) (applying the substantial effects test to determine whether jurisdiction should be asserted over foreign securities fraud).<sup>8</sup> [\*120] The *Hartford Fire* Court also held that [HN10](#) comity considerations, such as whether relief ordered by an American court would conflict with foreign law, were properly understood not as questions of whether a United States court possessed subject matter jurisdiction, but instead as issues of whether such a court should decline to exercise the jurisdiction that it possessed. See *id. at 797-98* & n.24.

[\*\*31] The framework stated in *Hartford Fire* guides our analysis of the Lanham Act jurisdictional question for foreign activities of foreign defendants. [HN11](#) We hold that the Lanham Act grants subject matter jurisdiction over extraterritorial conduct by foreign defendants only [\*\*\*1618] where the conduct has a substantial effect on United States commerce.<sup>9</sup> Absent a showing of such a substantial effect, at least as to foreign defendants, the court lacks jurisdiction over the Lanham Act claim. Congress has little reason to assert jurisdiction over foreign defendants who are engaging in activities that have no substantial effect on the United States, and courts, absent an express statement from Congress, have no good reason to go further in such situations. See 1A P. Areeda & H. Hovenkamp, *Antitrust Law* P 272f (2d ed. 2000) ("When a government's interest in a transaction is remote, minor, tangential, or otherwise insignificant, that government would presumably not seek to control it."); 1 W. Fugate, *Foreign Commerce and the Antitrust Laws* § 2.13, at 99-100 (5th ed. 1996).

[\*\*32] [HN12](#) The substantial effects test requires that there be evidence of impacts within the United States, and these impacts must be of a sufficient character and magnitude to give the United States a reasonably strong interest in the litigation. See, e.g., 1 Fugate, *supra*, §§ 2.9, 2.12, [\*121] 2.13; see also 1A Areeda & Hovenkamp, *supra*, P 272f2; *United Phosphorus*, 322 F.3d at 952-53. The "substantial effects" test must be applied in light of

<sup>8</sup>This effects test had its origins in *United States v. Aluminum Co. of Am.*, 148 F.2d 416 (2d Cir. 1945), although it took a considerable period of time to gain widespread acceptance. See generally 1 W. Fugate, *Foreign Commerce and the Antitrust Laws* § 2.10 (5th ed. 1996). An older and now discredited view, reflected in *American Banana Co. v. United Fruit Co.*, 213 U.S. 347, 356, 53 L. Ed. 826, 29 S. Ct. 511 (1909), was that antitrust laws were wholly territorial in nature. Notably, Steele cited *American Banana* and rejected a territorial interpretation of that case; it read *American Banana* as applying only when there were no effects in the United States from the foreign antitrust violation. See *Steele*, 344 U.S. at 288.

In 1982, Congress passed the FTAIA, which provided that the Sherman Act "shall not apply to conduct involving trade or commerce (other than import trade or import commerce) with foreign nations unless . . . such conduct has a direct, substantial, and reasonably foreseeable effect" on United States commerce. [15 U.S.C. § 6a](#); see 1 Fugate, *supra*, § 2.14. The Supreme Court has never explained the relationship between the FTAIA and the older, judicially-created effects test; thus it remains unclear the extent to which the FTAIA is a codification of that test and the extent to which the FTAIA amends it. See *Hartford Fire*, 509 U.S. at 796 n.23; see also *Nippon Paper*, 109 F.3d at 4.

<sup>9</sup>The traditional extraterritorial test for jurisdiction in the *antitrust* area has often, including in *Hartford Fire*, been articulated as containing a requirement that the defendant *intend* to cause the substantial effects on United States commerce that actually have been created. [509 U.S. at 796](#). The FTAIA's "reasonably foreseeable" requirement appears to be related to this traditional intent requirement. See [15 U.S.C. § 6a](#). We need not and do not decide whether a defendant's intent to target United States commerce plays any role in the jurisdictional inquiry for purposes of extraterritorial application of the *Lanham Act* -- either, for example, as a requirement in addition to the substantial effect requirement, or instead as a factor that, if present, may reduce the amount of effects on United States commerce that a plaintiff must show. It is evident that Delica, in this case, had no intent to target United States commerce.

We do note that lack of intent can sometimes change the scope of remedies under the Lanham Act. For example, an innocent infringer can generally only be subject to an injunction against future use. See [15 U.S.C. § 1114\(2\)](#). This, of course, is not a jurisdictional matter.

the core purposes of the Lanham Act, which are both to protect the ability of American consumers to avoid confusion and to help assure a trademark's owner that it will reap the financial and reputational rewards associated with having a desirable name or product. See, e.g., *Dastar Corp. v. Twentieth Century Fox Film Corp.*, 539 U.S. 23, 33-34, 156 L. Ed. 2d 18, 123 S. Ct. 2041 (2003); see also *Atl. Richfield Co. v. ARCO Globus Int'l Co.*, 150 F.3d 189, 193-94 (2d Cir. 1998). The goal of the jurisdictional test is to ensure that the United States has a sufficient interest in the litigation, as measured by the interests protected by the Lanham Act, to assert jurisdiction.

Of course, the [\*\*33] *Vanity Fair* test includes a "substantial effects" inquiry as part of its three-part test.<sup>10</sup> We differ from the *Vanity Fair* court in that we disaggregate the elements of its test: we first ask whether the defendant is an American citizen, and if he is not, then we use the substantial effects test as the sole touchstone to determine jurisdiction.

[\*\*34] **[HN13](#)** If the substantial effects test is met, then the court should proceed, in appropriate cases, to consider comity. We also transplant for Lanham Act purposes *Hartford Fire*'s holding that comity considerations are properly analyzed not as questions of whether there is subject matter jurisdiction, but as prudential questions of whether that jurisdiction should be exercised. See *Hartford Fire*, 509 U.S. at 798 n.24. Our analysis differs again from *Vanity Fair* on this point. See *Vanity Fair*, 234 F.2d at 642. *Vanity Fair* and other cases have considered as part of the basic jurisdictional analysis whether the defendant acted under color of protection of the trademark laws of his own country. We disagree and do not see why the scope of Congressional intent and power to create jurisdiction under the Lanham Act should turn on the existence and meaning of foreign law. [\*\*\*1619]

Congress could, of course, preclude the exercise of such Lanham Act jurisdiction by statute or by ratified treaty. Or it could by statute define limits in Lanham Act jurisdiction in such international cases, as it has chosen to do in the antitrust area. See [15 U.S.C. § 6a](#). [\*\*35] It has not done so.

## B. Application of the Framework

We apply the framework we have established to the facts of this case. Although district court fact-finding is permissible in a subject matter jurisdiction inquiry, and we defer to such fact-finding, **[HN14](#)** here all the relevant facts are undisputed and the district court did not find any facts.<sup>11</sup> [\*122] Our review is de novo, see, e.g., *Skwira v. United States*, 344 F.3d 64, 71-72 (1st Cir. 2003), and the burden is on McBee to establish jurisdiction, see, e.g., *Able Sales Co. v. Compania de Azucar de P.R.*, 406 F.3d 56, 61 (1st Cir. 2005).

### [\*\*36] 1. Claim for Injunction Barring Delica's United States Sales

McBee contends that his claim for an injunction against Delica's sales to consumers inside the United States does not constitute an extraterritorial application of the Lanham Act, and therefore the district court should have taken jurisdiction over this claim without pausing to consider whether there was a substantial effect on United States commerce. The factual predicate for this argument is the \$ 2,500 of "Cecil McBee" brand goods that Delica sold to

<sup>10</sup> Some courts have criticized *Vanity Fair*'s "substantial effects" inquiry as having been taken out of context, and have replaced it with a much less demanding "some effect" inquiry. These courts state that the "substantial effects" test was not clearly embraced in *Steele* and stems from attempts to determine when local commerce has a sufficient effect on interstate commerce to be congressionally reachable, which has no relevance to the question of determining when wholly foreign commerce can be reached. See *Am. Rice*, 701 F.2d at 414 n.8; *Wells Fargo & Co. v. Wells Fargo Express Co.*, 556 F.2d 406, 428 (9th Cir. 1977). *American Rice* involved domestic defendants, although the court did not restrict the modification of its test to such situations. The Supreme Court has embraced the "substantial effects" test for extraterritorial application of the antitrust laws, and Congress, in the FTAIA, has either codified that understanding or established an even more restrictive test. We see no reason to treat the Lanham Act differently.

<sup>11</sup> As we noted above, the subject matter jurisdiction issue was determined on a summary judgment record, after extensive discovery; McBee did not file a [Rule 56\(f\)](#) affidavit below stating that he needed more discovery. We note also that in this context, the jurisdictional inquiry will generally not be wholly distinct from the merits. See 1A Areeda & Hovenkamp, *supra*, P 273a.

McBee's investigators in Maine; there is no evidence of any other sales made by Delica to United States consumers. McBee is correct that the court had subject matter jurisdiction over this claim.

**HN15** [+] There can be no doubt of Congress's power to enjoin sales of infringing goods into the United States, and as a matter of Congressional intent there can be no doubt that Congress intended to reach such sales via the Lanham Act. Courts have repeatedly distinguished between domestic acts of a foreign infringer and foreign acts of that foreign infringer; the extraterritoriality analysis to determine jurisdiction attaches only to the latter. See, e.g., *Totalplan Corp. of Am. v. Colborne*, 14 F.3d 824, 829-30 (2d Cir. 1994); [\*\*37] *Sterling Drug*, 14 F.3d at 744-47 & n.8; *Wells Fargo*, 556 F.2d at 426-30; *Vanity Fair*, 234 F.2d at 638-39, 645; see also 4 J. T. McCarthy, *McCarthy on Trademarks and Unfair Competition* § 29:56, at 29-151 (4th ed. 2005). Since sales in the United States are domestic acts, McBee need not satisfy the "substantial effect on United States commerce" test for this claim; jurisdiction exists because, under the ordinary domestic test, the \$ 2,500 worth of goods sold by Delica to McBee's investigators in the United States were in United States commerce, at least insofar as some of those goods were shipped directly by Delica to the buyers in the United States. See *Carpet Group Int'l v. Oriental Rug Importers Ass'n, Inc.*, 227 F.3d 62, 71-75 (3d Cir. 2000).

Our holding that the extraterritoriality tests are inapplicable where plaintiff seeks a remedy for imported goods sold to American consumers is supported in the antitrust context by the language of the FTAIA. The FTAIA provides that **HN16** [+] the Sherman Act:

shall not apply to conduct involving trade or commerce (other than import trade or import commerce) with foreign [\*\*38] nations unless . . . such conduct has a direct, substantial, and reasonably foreseeable effect (A) on trade or commerce which is not trade or commerce with foreign nations, or on import trade or import commerce with foreign nations; or (B) on export trade or export commerce with foreign nations, of a person engaged in such trade or commerce in the United States . . . .

**15 U.S.C. § 6a(1)**. The statute exempts "import trade or import commerce" from its extraterritoriality effects test; such import trade or import commerce would seem to be reachable so long as the domestic commerce tests are met. See *Carpet Group Int'l*, 227 F.3d at 71-75; W. Fugate [\*123] & L. Simonwitz, *Foreign Commerce and the Antitrust Laws* § 2.14, at 30 (5th ed. Supp. 2004).

The district court thus had subject matter jurisdiction over McBee's claim for an injunction against Delica's sales of "Cecil McBee" goods in the United States. Nonetheless, dismissal [\*\*\*1620] of the claim was appropriate for reasons stated later.<sup>12</sup>

#### [\*\*39] 2. Claim for Injunction Barring Access to Internet Website

McBee next argues that his claim for an injunction against Delica's posting of its Internet website in a way that is visible to United States consumers also does not call for an extraterritorial application of the Lanham Act. Here McBee is incorrect: granting this relief would constitute an extraterritorial application of the Act, and thus subject matter jurisdiction would only be appropriate if McBee could show a substantial effect on United States commerce. <sup>13</sup> McBee has not shown such a substantial effect from Delica's website.

We begin with McBee's argument that his website claim, like his claim for Delica's sales into the United States, is not an extraterritorial application of the Lanham Act. McBee does not seek to reach the website because it is a method, by Delica, for selling "Cecil McBee" goods into the United States. In such a case, if a court had jurisdiction to enjoin sales of goods within the United States, it might have jurisdiction to enjoin the website as well,

<sup>12</sup> We do not reach the more complicated question of whether comity concerns would ever allow a court to decline to exercise jurisdiction when an injunction is sought against sales in the United States.

<sup>13</sup> Preliminarily, Delica disputes whether it is technologically possible to prevent access by American consumers while simultaneously allowing access to the website in the rest of the world. We lack the information to resolve this dispute, and at any rate we need not resolve it in order to decide this dispute.

or at least those parts of the website that are necessary to allow the sales to occur.<sup>14</sup> Rather, the injury McBee complains about from the website is that its mere existence has caused him harm, because United States citizens can view the website and become confused about McBee's relationship with the Japanese clothing company. In particular, McBee argues that he has suffered harm from the fact that Delica's website often comes up on search engines ahead of fan sites about McBee's jazz career.

[\*\*41] Delica's website, although hosted from Japan and written in Japanese, happens to be reachable from the United States just as it is reachable from other countries. That is the nature of the Internet. The website is hosted and managed overseas; its visibility within the United States is more in the nature of an effect, which occurs only when someone in the United States decides to visit the website. To hold that any website in a foreign language, wherever hosted, is automatically reachable under the Lanham Act so long as it is visible in the United States would be senseless. The United States often will have no real interest in hearing trademark lawsuits about websites that are written in a foreign language and hosted in other countries. McBee attempts to analogize the existence of Delica's website, which happens to be visible in any country, to the direct mail advertising that the *Vanity Fair* court considered to be domestic conduct [\*\*124] and so held outside the scope of the extraterritoriality analysis. See [Vanity Fair, 234 F.2d at 638-39](#). The analogy is poor for three reasons: first, the advertising in *Vanity Fair* was closely connected with mail-order sales; second, [\*\*42] direct mail advertising is a far more targeted act than is the hosting of a website; and third, Delica's website, unlike the advertising in *Vanity Fair*, is in a foreign language.

Our conclusion that McBee's website claim calls for extraterritorial application of the Lanham Act is bolstered by a consideration of the now extensive case law relating to treatment of Internet websites with respect to personal jurisdiction. We recognize that the contexts are distinct, but the extraterritorial application of jurisdiction under the Lanham Act evokes concerns about territorial restraints on sovereigns that are similar to concerns driving personal jurisdiction. To put the principle broadly, [HN17](#)<sup>15</sup> the mere existence of a website that is visible in a forum and that gives information about a company and its products is not enough, by itself, to subject a defendant to personal jurisdiction in that forum. See, e.g., [Jennings v. AC Hydraulic A/S, 383 F.3d 546, 549-50 \(7th Cir. 2004\)](#); [ALS Scan, Inc. v. Digital Serv. Consultants, Inc., 293 F.3d 707, 713-15 \(4th Cir. 2002\)](#).

Something more is necessary, such as interactive features which allow the successful [\*\*43] online ordering of the defendant's products. See, e.g., [Jennings, 383 F.3d at 549](#). The mere existence of a website does not show that a defendant [\*\*1621] is directing its business activities towards every forum where the website is visible; as well, given the omnipresence of Internet websites today, allowing personal jurisdiction to be premised on such a contact alone would "eviscerate" the limits on a state's jurisdiction over out-of-state or foreign defendants. [Id. at 549-50](#).

Similarly, allowing subject matter jurisdiction under the Lanham Act to automatically attach whenever a website is visible in the United States would eviscerate the territorial curbs on judicial authority that Congress is, quite sensibly, presumed to have imposed in this area.

Our conclusion does not make it impossible for McBee to use the Lanham Act to attack a Japan-based website; it merely requires that McBee first establish that the website has a substantial effect on commerce in the United States before there is subject matter jurisdiction under the Lanham Act. We can imagine many situations in which the presence of a website would ensure (or, at least, help to ensure) that [\*\*44] the United States has a sufficient interest. The substantial effects test, however, is not met here.

Delica's website is written almost entirely in Japanese characters; this makes it very unlikely that any real confusion of American consumers, or diminution of McBee's reputation, would result from the website's existence. In fact, most American consumers are unlikely to be able to understand Delica's website at all. Further, McBee's claim that Americans looking for information about him will be unable to find it is unpersuasive: the Internet searches reproduced in the record all turned up both sites about McBee and sites about Delica's clothing line on their first

<sup>14</sup> The cases cited by McBee involve such situations and are therefore easily distinguishable; as well, they contain no analysis at all of the question McBee has raised. See [Euromarket Designs, Inc. v. Crate & Barrel Ltd., 96 F. Supp. 2d 824, 831-33 \(N.D. Ill. 2000\)](#); [Playboy Enters. v. Chuckleberry Publ'g, Inc., 939 F. Supp. 1032, 1039-40 \(S.D.N.Y. 1996\)](#).

page of results. The two sets of results are easily distinguishable to any consumer, given that the Delica sites are clearly shown, by the search engines, as being written in Japanese characters. Finally, we stress that McBee has produced no evidence of any American consumers going to the website and then becoming confused about whether McBee had a relationship with Delica.

### [\*125] 3. *Claim for Damages for Delica's Japanese Sales*

McBee's claim for damages due to Delica's sales in Japan fares no better, because these sales [\*\*45] as well have no substantial effect on commerce in the United States. McBee seeks damages for Delica's sales in Japan to Japanese consumers based on (a) tarnishing of McBee's image in the United States, and (b) loss of income in the United States due to loss of commercial opportunity as a jazz musician in Japan, stemming from the tarnishing of McBee's reputation there. The alleged tarnishing -- both in the United States and Japan -- is purportedly caused by the confusion of McBee's name with a brand selling (sometimes provocative) clothing to young teenage girls in Japan. McBee presents essentially no evidence that either type of tarnishing has occurred, much less that it has any substantial effect on United States commerce.

McBee's first argument, that *American* consumers are being confused and/or led to think less of McBee's name because of Delica's Japanese sales, cuts very close to the core purposes of the Lanham Act. See [Atl. Richfield Co., 150 F.3d at 193](#); [Sterling Drug, Inc., 14 F.3d at 746](#); see also Schechter, *supra*, at 628-30 (arguing that what distinguishes the Lanham Act from areas like patent or copyright, and makes extraterritorial [\*\*46] jurisdiction proper in the trademark context while it is improper in those other areas, is the risk that the trademark infringer's foreign sales will eventually confuse domestic consumers, thus costing the mark holder sales domestically as well as abroad). Such [HN18](#)[<sup>18</sup>] confusion and reputational harm in the eyes of American consumers can often -- although not always -- be inferred from the fact that American consumers have been exposed to the infringing mark. But no inference of dilution or other harm can be made in situations where American citizens are not exposed at all to the infringing product. The trouble with McBee's argument is that there is virtually no evidence that American consumers are actually seeing Delica's products.

Quite commonly, plaintiffs in these sorts of cases can meet their burden by presenting evidence that while the initial sales of infringing goods may occur in foreign countries, the goods subsequently tend to enter the United States in some way and in substantial quantities. See, e.g., [Steele, 344 U.S. at 286](#); [Nintendo of Am., 34 F.3d at 249, 251](#); [Atl. Richfield Co., 150 F.3d at 193](#); [Totalplan, 14 F.3d at 830](#). [\*\*47] McBee has presented essentially no evidence that Delica's products have been brought into the United States after their initial sale in Japan. McBee's own statement, [\*\*\*1622] without more, that people have seen women wearing Delica clothing in the United States does not show very much; likewise, McBee's evidence that Delica's goods are occasionally sold on eBay shows little, given particularly that such goods need not have been auctioned to buyers in the United States. The evidence indicates only one incident in which an American citizen saw McBee advertisements while traveling in Japan and demonstrated confusion upon returning to the United States.

Beyond that, there is also nothing that indicates any harm to McBee's career in the United States due to Delica's product sales. McBee's argument that there has potentially been harm to McBee's career as a product endorser is most unlikely, especially given his own disinterest in performing such endorsements. Further, McBee's statement that his teaching career may have been hindered by Delica is speculation.

McBee's second argument is that Delica's sales have confused Japanese consumers, hindering McBee's record sales and [\*126] touring career in Japan. [\*\*48] Evidence of economic harm to McBee in Japan due to confusion of Japanese consumers is less tightly tied to the interests that the Lanham Act intends to protect, since there is no United States interest in protecting *Japanese consumers*. American courts do, however, arguably have an interest in protecting American commerce by protecting McBee from lost income due to the tarnishing of his trademark in Japan. [HN19](#)[<sup>19</sup>] Courts have considered sales diverted from American companies in foreign countries in their analyses. See [Totalplan, 14 F.3d at 830-31](#); see also *Am. Rice*, 701 F.2d at 414-15 (considering diverted sales in finding "some effects" test met).

Assuming *arguendo* that evidence of harm to an American plaintiff's economic interests abroad, due to the tarnishing of his reputation there, might sometimes meet the substantial effects test, McBee has presented no evidence of such harm in this case. McBee has presented no evidence of economic harm due to losses in record sales or touring opportunities in Japan. McBee's statement that he might have expected more Japanese touring opportunities by now, and may have had such opportunities absent Delica's [\*\*49] sales, is wholly speculative. There is no probative evidence of any decline in McBee's touring revenue as compared to past patterns, nor is there any evidence of any decline in McBee's Japanese record sales.

McBee has not shown that Delica's Japanese sales have a substantial effect on United States commerce, and thus McBee's claim for damages based on those sales, as well as McBee's claim for an injunction against Delica's website, must be dismissed for lack of subject matter jurisdiction. We need not reach the issue of whether we should decline jurisdiction because of comity.<sup>15</sup> Were we to assert jurisdiction in this case, where there is no evidence of any harm to American commerce beyond the facts that the plaintiff is an American citizen and that the allegedly infringing goods were sold and seen in a foreign country, we would be forced to find jurisdiction in almost all false endorsement or trademark cases involving an American plaintiff and allegedly infringing sales abroad.

#### [\*\*50] C. Frivolousness of Claim Based on Delica's Product Sales in the United States

Because we do have subject matter jurisdiction over McBee's claim for an injunction against Delica's sales in the United States,<sup>16</sup> we proceed on that claim. [\*\*\*1623]

[\*127] We dispose of a preliminary issue: whether there is any required [\*\*51] order for deciding the remaining issues. We would ordinarily next reach Delica's defense that the federal district court, sitting in Maine, lacked personal jurisdiction over it. See, e.g., *United States v. Swiss Am. Bank, Ltd.*, 191 F.3d 30, 46 (1st Cir. 1999). But we choose to decide this case on much simpler grounds. Although the Supreme Court in *Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 140 L. Ed. 2d 210, 118 S. Ct. 1003 (1998), generally barred the practice of "hypothetical jurisdiction," we have noted that "the rule does not appear to be an absolute one," *Parella v. Ret. Bd. of the R.I. Employees' Ret. Sys.*, 173 F.3d 46, 53-56 (1st Cir. 1999), and we have consistently interpreted the rule as applying in its strict form only to issues going to Article III's requirements. See, e.g., *Cozza v. Network Assocs., Inc.*, 362 F.3d 12, 15 (1st Cir. 2004); *Restoration Pres. Masonry v. Grove Europe Ltd.*, 325 F.3d 54, 59-60 (1st Cir. 2003); *United States v. Woods*, 210 F.3d 70, 74 n.2 (1st Cir. 2000); *Parella*, 173 F.3d at 53-56.

**HN21** [↑] The requirements [\*\*52] of personal jurisdiction are not rooted in Article III, although they do have constitutional resonance through the *Due Process clause*. See *Ins. Corp. of Ir. v. Compagnie des Bauxites de*

<sup>15</sup> Were we to reach comity principles, they would most likely counsel for dismissal of McBee's claim seeking damages for Delica's sales in Japan. McBee argues that so long as he seeks only damages and not an injunction, there is no "true conflict" with Japanese law because it would be theoretically possible for Delica to comply with both Japanese and United States law. See *Hartford Fire*, 509 U.S. at 798-99. McBee's argument makes no sense: an injunction would no more create a "true conflict" under this definition than damages, for under either form of relief it would be theoretically possible for Delica to comply with both nations' laws by not using the trademark. There is no meaningful distinction between an injunction and damages for this purpose. The reasoning developed in the antitrust context in *Hartford Fire* is not "automatically transferable" to the trademark context: "It is one thing for the British reinsurers in *Hartford Fire* to be barred under United States law from boycotting activity that they might be free to engage in without violating British law. But it is quite a different thing for the holder of rights in a mark under German law to be ordered to refrain from uses of that mark protected by German law." *Sterling Drug*, 14 F.3d at 746-47.

<sup>16</sup> It is true that **HN20** [↑] we lack subject matter jurisdiction over claims that involve no real federal controversy because they "clearly appear[] to be immaterial and made solely for the purpose of obtaining jurisdiction or where such a claim is wholly insubstantial and frivolous." *Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 89-90, 140 L. Ed. 2d 210, 118 S. Ct. 1003 (1998). This test goes to whether, legally, there is any real federal interest involved in the case. The fatal flaw in McBee's claim here, as we explain below, is that the only sales made to the United States were sales instigated at his own behest. This sort of factual weakness in a claim does not go to subject matter jurisdiction.

*Guinee*, 456 U.S. 694, 702-03, 72 L. Ed. 2d 492, 102 S. Ct. 2099 (1982). Unlike subject matter jurisdiction under Article III, which goes to the fundamental institutional competence of the court and can be raised sua sponte at any time, personal jurisdiction is an individual liberty right and is therefore waivable; a court cannot raise personal jurisdiction sua sponte. See *id. at 702-05*. In *Parella*, we held that *Eleventh Amendment* immunity is not subject to the strict form of *Steel Co.* and can be bypassed in certain cases, stressing the waivability of the immunity and the fact that a court need not raise it sua sponte. See *Parella*, 173 F.3d at 54-55. As in the sovereign immunity area, **HN22**[<sup>17</sup>] we do not wish to force defendants to expend resources on difficult personal jurisdiction issues or courts to reach more difficult issues when there is an exceptionally easy method -- on the merits -- for the defendant to prevail. See *id. at 56*.

Here, where **[\*\*53]** McBee's claim for an injunction barring Delica's sales in the United States is wholly without merit, and where the personal jurisdiction question is briefed only as a subsidiary issue by both sides, providing us with little guidance, we have the power to pretermit the personal jurisdiction question.<sup>17</sup> We reach these merits now, noting that **HN23**[<sup>18</sup>] the questions appealed to us were decided on a summary **[\*128]** judgment record and that we may affirm on any ground supported by that record, see, e.g., *Cimon v. Gaffney*, 401 F.3d 1, 4 (1st Cir. 2005), as well as that the ground for our decision on the merits is closely tied to the facts we used to decide the jurisdictional question.

**[\*\*54]** As to the merits, there is no evidence of existing confusion or dilution due to Delica's past sales, since these few sales were all made to McBee's own investigators, who were brought in to assist in this litigation and therefore fully understood McBee's lack of any relationship with Delica. See *Millennium Enters., Inc. v. Millennium Music, Inc.*, 33 F. Supp. 2d 907, 911 (D. Or. 1999) (gravamen of unfair competition claim is whether defendant's actions have created confusion; sale to plaintiff's agent could not have created any). There is no evidence of any other sales, nor any evidence that Delica has any desire to sell into the United States in the future. All the evidence, in fact, is to the contrary. Thus, there is no justification for injunctive relief, and summary judgment must enter for Delica on this claim.

**HN24**[<sup>19</sup>] Absent any viable federal claim, the district court's dismissal of all of McBee's pendent state law claims (without prejudice to their being refiled in state court) was fully appropriate and was not an abuse of discretion -- McBee has not argued otherwise. See *28 U.S.C. § 1367(c)*; *Gonzalez-de-Blasini v. Family Dep't*, 377 F.3d 81, 89 (1st Cir. 2004). **[\*\*55]** We need not reach Delica's laches or collateral estoppel arguments. **[\*\*1624]**

#### IV.

The district court's decision ordering judgment for the defendant Delica is **affirmed**. Costs are awarded to Delica.

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<sup>17</sup> *Ruhrgas AG v. Marathon Oil Co.*, 526 U.S. 574, 143 L. Ed. 2d 760, 119 S. Ct. 1563 (1999), is not to the contrary. Although *Ruhrgas* contained language on the importance of personal jurisdiction, the decision merely established that a court can, in some circumstances, dispose of a case on a different threshold ground before reaching subject matter jurisdiction. See *id. at 584-85*; see also *Tenet v. Doe*, 544 U.S. 1, 161 L. Ed. 2d 82, 125 S. Ct. 1230, 1234 n.4 (2005). The thrust of *Ruhrgas* was to increase judicial flexibility, not to decrease it. See *Ruhrgas AG*, 526 U.S. at 587-88.



## *In re Enron Corp.*

United States Bankruptcy Court for the Southern District of New York

August 5, 2005, Decided

Chapter 11, Case No. 01-16034 (AJG), Jointly Administered

### **Reporter**

328 B.R. 75 \*; 2005 Bankr. LEXIS 1463 \*\*; 45 Bankr. Ct. Dec. 38

In re: ENRON CORP., et al., Reorganized Debtors.

**Subsequent History:** Affirmed by [\*Oscar's Photo Lab v. Enron Corp., 2006 U.S. Dist. LEXIS 66681 \(S.D.N.Y., Apr. 27, 2006\)\*](#)

## **Core Terms**

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electricity, filed rate doctrine, manipulation, wholesale, markets, proof of claim, preemption, tariff, original claim, rates, natural gas, anti trust law, regulation, preempted, motion to amend, market-based, energy, cases, trading, sales, courts, prong, anti-competitive, transactions, state law, interstate, violations, misconduct, Partial, reasons

## **LexisNexis® Headnotes**

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Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Energy & Utilities Law > Utility Companies > Rates > General Overview

### **HN1[ State & Territorial Government Licensing, Gaming & Lotteries**

The California Independent System Operator (ISO) tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as taking unfair advantage of the rules and procedures set forth in the California Power Exchange (PX) or the ISO tariffs, Protocols or Activity Rule to the detriment of the efficiency of, and of consumers in, the ISO markets.

Constitutional Law > Supremacy Clause > Federal Preemption

Governments > Federal Government > US Congress

Constitutional Law > Supremacy Clause > General Overview

## **HN2** **Supremacy Clause, Federal Preemption**

Federal preemption of state law is rooted in the Supremacy Clause, U.S. Const. art. VI, cl. 2. Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction.

Constitutional Law > Supremacy Clause > General Overview

## **HN3** **Constitutional Law, Supremacy Clause**

In the absence of an express preemption by Congress, state law is preempted: (1) when Congress intends that federal law occupy a given field. (field preemption); and (2) to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress. (conflict preemption)

Energy & Utilities Law > Pipelines & Transportation > Electricity Transmission

Transportation Law > Interstate Commerce > Federal Powers

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > Exclusive Jurisdiction

Constitutional Law > ... > Commerce Clause > Interstate Commerce > General Overview

Energy & Utilities Law > Administrative Proceedings > Preemption

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > ... > US Federal Energy Regulatory Commission > Civil Actions > Jurisdiction

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > General Overview

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers

#### **HN4** Pipelines & Transportation, Electricity Transmission

The statute's framework under the Federal Power Act supports the conclusion that the Federal Energy Regulatory Commission (FERC) has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the FERC exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which Congress has made explicitly subject to regulation by the states. Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states. Federal Power Act, [16 U.S.C.S. §§ 824-824m](#).

Energy & Utilities Law > Electric Power Industry > Electricity Distribution & Transmission > General Overview

Communications Law > Regulators > US Federal Communications Commission > Jurisdiction

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Wholesale Rates

Energy & Utilities Law > Utility Companies > Rates > General Overview

#### **HN5** Electric Power Industry, Electricity Distribution & Transmission

Section 206(a) of the Federal Power Act, [16 U.S.C.S. § 824e](#), provides that upon a determination by the Federal Energy Regulatory Commission (FERC) that any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any transmission or sale subject to the jurisdiction of the FERC, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory or preferential, the FERC shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order.

Administrative Law > Agency Adjudication > Informal Agency Action

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > US Federal Energy Regulatory Commission

Energy & Utilities Law > Oil, Gas & Mineral Interests > Purchase Contracts > General Overview

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

Energy & Utilities Law > Electric Power Industry > Deregulation & Restructuring

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN6** Agency Adjudication, Informal Agency Action

Pursuant to the Federal Power Act, the Federal Energy Regulatory Commission (FERC) possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue discrimination on the part of individual utilities. §§ 205 and 206(a) of the Federal Power Act, [16 U.S.C.S. §§ 824d, 824e](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.S. § 7173\(c\)](#).

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

#### **HN7** Energy & Utilities Law, Antitrust Issues

Each participant in the California Power Exchange (PX) and the California Independent System Operator (ISO) markets is required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market. Entities that transact through the ISO or the PX and engage in improper practices are in violation of filed tariffs. The Federal Energy Regulatory Commission (FERC) and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement.

Business & Corporate Compliance > ... > Governments > State & Territorial Governments > Gaming & Lotteries

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Cogeneration & Independent Companies > Independent System Operators

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

#### **HN8** State & Territorial Government Licensing, Gaming & Lotteries

Since 1998, the California Power Exchange (PX) and the California Independent System Operator (ISO) tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric

power. "Anomalous market behavior" is: (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation; or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include: (1) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; (2) unexplained or unusual redeclarations of availability; (3) unusual trades or transactions; (4) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and (5) unusual activity or circumstances relating to imports from or exports to other markets or exchanges.

Administrative Law > Separation of Powers > Legislative Controls > Implicit Delegation of Authority

Antitrust & Trade Law > Regulated Industries > Energy & Utilities > General Overview

Business & Corporate Law > Corporations > Dissolution & Receivership > Involuntary Dissolution

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Antitrust Issues > General Overview

#### **HN9** [blue icon] **Legislative Controls, Implicit Delegation of Authority**

Implicit in Federal Energy Regulatory Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority.

Administrative Law > Separation of Powers > Jurisdiction

Governments > Federal Government > Claims By & Against

Administrative Law > Separation of Powers > Primary Jurisdiction

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

#### **HN10** [blue icon] **Separation of Powers, Jurisdiction**

The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. The filed rate doctrine forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority. The purpose of the doctrine is preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Electric Power Industry > Federal Power Act > Federal Rate Regulation

## [\*\*HN11\*\*](#) [blue download icon] Exemptions & Immunities, Filed Rate Doctrine

While market-based rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine.

Energy & Utilities Law > Antitrust Issues > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

## [\*\*HN12\*\*](#) [blue download icon] Energy & Utilities Law, Antitrust Issues

The reporting requirements are an integral part of a tariff, with the Federal Energy Regulatory Commission's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates.

Administrative Law > Separation of Powers > Legislative Controls > Implicit Delegation of Authority

Energy & Utilities Law > Antitrust Issues > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Energy & Utilities Law > Electric Power Industry > Federal Power Act > General Overview

## [\*\*HN13\*\*](#) [blue download icon] Legislative Controls, Implicit Delegation of Authority

Implicit in Federal Energy Regulatory Commission (FERC) orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. Moreover, the United States Court of Appeals for the Ninth Circuit has indirectly recognized the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. Without the availability of retroactive refunds, parties aggrieved by an illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the Federal Power Act.

Business & Corporate Compliance > ... > Transportation Law > Carrier Duties & Liabilities > Rates & Tariffs

Transportation Law > Carrier Duties & Liabilities > Damages

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > Restraints of Trade

## [\*\*HN14\*\*](#) [blue download icon] Common Carrier Duties & Liabilities, Rates & Tariffs

In addressing the right of action that a violation of the antitrust laws give to one who has been injured in its business or property, the United States Supreme Court has stated that injury implies violation of a legal right. The Supreme Court concluded that the legal rights of a shipper as against a carrier in respect to a rate are measured by the published tariff. A rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the Antitrust Act. What rates are legal is determined by the Act to Regulate Commerce. Under § 8 of the latter act, the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of damages sustained in consequence of any such violation.

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers](#)

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Energy & Utilities Law > Antitrust Issues > General Overview](#)

#### **[HN15](#)[] Exemptions & Immunities, Filed Rate Doctrine**

Under the filed rate doctrine, the Federal Energy Regulatory Commission alone is empowered to make a judgment regarding rates, and until it has done so, no rate other than the one on file may be charged.

[Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > General Overview](#)

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers](#)

[Energy & Utilities Law > Administrative Proceedings > General Overview](#)

[Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine](#)

[Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview](#)

[Energy & Utilities Law > Oil, Gas & Mineral Interests > Purchase Contracts > Remedies for Breach](#)

#### **[HN16](#)[] Regulators, US Federal Energy Regulatory Commission**

Remedies for breach and non-performance of operating agreements in the interstate wholesale electricity market approved by the Federal Energy Regulatory Commission (FERC) fall within the exclusive domain of FERC.

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers](#)

[Energy & Utilities Law > Electric Power Industry > Electric Power Rates > Filed Rate Doctrine](#)

[Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview](#)

[Energy & Utilities Law > Regulators > Public Utility Commissions > Ratemaking Procedures](#)

#### **[HN17](#)[] Filed Rate Doctrine, Public Utilities & Telecommunications Carriers**

The filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that: (1) legislatively appointed regulatory bodies have institutional competence to address rate-making issues; (2) courts lack the competence to set utility rates; and (3) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime.

Bankruptcy Law > ... > Bankruptcy > Claims > Allowance of Claims

Governments > Legislation > Statute of Limitations > Time Limitations

Bankruptcy Law > Claims > Proof of Claim > Effects & Procedures

Governments > Legislation > Statute of Limitations > General Overview

### **HN18** [ ] **Claims, Allowance of Claims**

*Fed. R. Bankr. P. 3003(c)(3)* directs a bankruptcy court to establish a bar date beyond which proofs of claim are disallowed in a Chapter 11 case. The bar date is critically important to the administration of a successful Chapter 11 case for it intended to be a mechanism providing the debtor and its creditors with finality. In particular, a bar date order serves the important purpose of enabling the parties to a bankruptcy case to identify with reasonable promptness the identity of those making claims against the bankruptcy estate and the general amount of the claims, a necessary step in achieving the goal of successful reorganization. Therefore, a bar date order does not function merely as a procedural gauntlet, but as an integral part of the reorganization process. Accordingly, a bar date is likened to a statute of limitations which generally must be strictly observed.

Bankruptcy Law > Claims > Proof of Claim > Effects & Procedures

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Bankruptcy Law > Claims > Proof of Claim > General Overview

### **HN19** [ ] **Proof of Claim, Effects & Procedures**

The decision to grant or deny an amendment to a timely-filed proof of claim rests with the sound discretion of a bankruptcy judge. Although amendments to proofs of claim should in the absence of contrary equitable considerations or prejudice to the opposing party be freely permitted, such amendments are not automatic. The amendments are allowed, however, where the purpose is to cure a defect in the claim as originally filed, to describe the original claim with greater particularity or to plead a new theory of recovery on the facts set forth in the original claim. Nevertheless, an amendment may not be used as a mechanism for circumventing the bar date. Therefore, a bankruptcy court must carefully scrutinize a post bar-date amendment to ensure that the amendment is truly amending timely-filed proofs of claims and not asserting an entirely new claim. An amendment will not be permitted when its purpose is to create an entirely new claim.

Bankruptcy Law > Claims > Proof of Claim > Effects & Procedures

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

### **HN20** [ ] **Proof of Claim, Effects & Procedures**

When deciding whether to permit an amendment to a proof of claim, a bankruptcy court is guided by a two-prong test. A court must first look to whether there was timely assertion of a similar claim or demand evidencing an intention to hold the estate liable. If there were such a timely assertion, the court then examines each fact within the case and determines whether it would be equitable to allow the amendment. In balancing the equities, the court considers the following equitable factors: (1) undue prejudice to opposing party; (2) bad faith or dilatory behavior on part of the claimant; (3) whether other creditors would receive a windfall were the amendment not allowed; (4) whether other claimants might be harmed or prejudiced; and (5) the justification for the inability to file the amended claim at the time the original claim was filed. This second prong of the test is applied only if the first prong is satisfied and the claim qualifies as an amendment and not a new claim.

[Bankruptcy Law > Procedural Matters > Adversary Proceedings > Commencement of Adversary Proceedings](#)

[Bankruptcy Law > Claims > Proof of Claim > Effects & Procedures](#)

[Bankruptcy Law > Procedural Matters > Contested Matters](#)

[Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview](#)

[Civil Procedure > ... > Pleadings > Amendment of Pleadings > Relation Back](#)

## **HN21** [+] **Adversary Proceedings, Commencement of Adversary Proceedings**

Neither the Bankruptcy Code nor the Federal Rules of Bankruptcy Procedure directly address an amendment of a proof of claim. Nevertheless, in determining whether to permit a post-bar date amendment to a timely-filed proof of claim under the first prong of the two-prong test, several courts have applied [Fed. R. Civ. P. 15\(c\)](#) by analogy or explicitly, pursuant to [Fed. R. Bankr. P. 7015](#) and [Fed. R. Bankr. P. 9014\(c\)](#), to analyze such an amendment.

[Bankruptcy Law > Procedural Matters > Adversary Proceedings > Commencement of Adversary Proceedings](#)

[Bankruptcy Law > ... > Bankruptcy > Claims > Objections to Claims](#)

[Bankruptcy Law > Procedural Matters > General Overview](#)

[Bankruptcy Law > Procedural Matters > Adversary Proceedings > General Overview](#)

[Bankruptcy Law > Procedural Matters > Contested Matters](#)

[Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview](#)

## **HN22** [+] **Adversary Proceedings, Commencement of Adversary Proceedings**

[Fed. R. Bankr. P. 7015](#) provides that [Fed. R. Civ. P. 15](#) applies in adversary proceedings. Although the filing of an objection to a proof of claim is a contested matter, and not an adversary proceeding, [Fed. R. Bankr. P. 9014](#) permits a bankruptcy court, at its discretion, to extend [Fed. R. Bankr. P. 7015](#) to contested matters as well as adversary proceedings.

[Bankruptcy Law > Procedural Matters > Adversary Proceedings > Commencement of Adversary Proceedings](#)

[Governments > Courts > Rule Application & Interpretation](#)

Bankruptcy Law > Procedural Matters > Contested Matters

### **HN23** [blue icon] Adversary Proceedings, Commencement of Adversary Proceedings

Fed. R. Bankr. P. 9014(c) states that the court may at any stage in a particular matter direct that one or more of the other rules in Part VII, which includes Fed. R. Bankr. P. 7015, shall apply and, further, the Advisory Committee Note to the rule provides that when the rules of Part VII are applicable to a contested matter, reference in the Part VII rules to adversary proceedings is to be read as a reference to a contested matter. Part VII of the Federal Rules of Bankruptcy Procedure is based on the premise that to the extent possible practice before the bankruptcy courts and the district courts should be the same.

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Relation Back

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

### **HN24** [blue icon] Amendment of Pleadings, Relation Back

See Fed. R. Civ. P. 15(c)(2).

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Relation Back

Governments > Legislation > Statute of Limitations > Time Limitations

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Governments > Legislation > Statute of Limitations > General Overview

### **HN25** [blue icon] Amendment of Pleadings, Relation Back

After the statute of limitations has run, Fed. R. Civ. P. 15(c)(2) is used for amending an original pleading to add a claim or defense.

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Energy & Utilities Law > Electric Power Industry > State Regulation > General Overview

### **HN26** [blue icon] Pleadings, Amendment of Pleadings

Courts, in general, have moved away from the cause of action test in allowing an amendment under Fed. R. Civ. P. 15, and instead, an amendment has been allowed which adds another claim if it is arising out of the same transaction or occurrence.

Energy & Utilities Law > Antitrust Issues > General Overview

### **HN27** [blue icon] Energy & Utilities Law, Antitrust Issues

Wash trading occurs when a party simultaneously buys and sells the same commodity at or near the same price within a very short period time so that the party has no financial risk in the transactions. Wash trading establishes

"bogus" prices which are not related to real conditions in the gas market, and creates an illusion of volume and liquidity which encourages other market participants to engage in the frenzy.

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > Public Utilities & Telecommunications Carriers

Energy & Utilities Law > Regulators > US Federal Energy Regulatory Commission > Authorities & Powers

Antitrust & Trade Law > Exemptions & Immunities > Filed Rate Doctrine > General Overview

Energy & Utilities Law > Natural Gas Industry > General Overview

Energy & Utilities Law > Natural Gas Industry > Distribution & Sale

## **HN28** Filed Rate Doctrine, Public Utilities & Telecommunications Carriers

The essential purpose of the filed rate doctrine is to protect the jurisdiction of a regulatory body that Congress has designated to determine whether rates charged, such as those in the natural gas market, are just and reasonable.

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**Judges:** ARTHUR J. GONZALEZ, United States Bankruptcy Judge.

**Opinion by:** ARTHUR J. GONZALEZ

## **Opinion**

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### **[\*77] OPINION SUSTAINING DEBTORS' OBJECTION TO PROOFS OF CLAIM NO. 15229-35 FILED BY OSCAR'S PHOTO LAB AND MOTION TO AMEND CERTAIN PROOFS OF CLAIM FILED BY OSCAR'S PHOTO LAB**

In August 2002, the Federal Energy Regulatory Commission ("FERC") issued **[\*78]** the Initial Report on Price Manipulation in Western Markets: Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Price ("Initial Report"). On October 15, 2002, Oscar's Photo Lab ("OPL") filed separate proofs of claims (Claim Nos. 15229-35, collectively, the "Claims") in unliquidated amounts against Enron Corp. ("Enron") and certain of its affiliated entities (collectively, the "Debtors"). OPL alleges that **[\*\*2]** the Debtors manipulated the wholesale electricity market in California and overcharged for energy through unlawful and anti-competitive acts during the western power crisis of 2000 and 2001. OPL maintains the alleged manipulation in the wholesale electricity market constitutes a violation of state **antitrust law** and unfair competition law, and seeks disgorgement, restitution, actual and treble damages together with interest and injunctive relief.<sup>1</sup> In March 2003, FERC issued the Final Report on Price Manipulation in Western Markets: Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Price ("Final Report"). In September 2003, OPL filed Partial Objection of Claimant OPL to Motion of Enron

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<sup>1</sup> [California Unfair Competition Law, Business & Professional Code § 17200](#). OPL alleges that the Debtors' violation of Business & Professional Code [§ 17200](#)'s proscription against engaging in unlawful business acts and practices.

Corp., et. al. for Order Establishing Procedures to Estimate Disputed, Unliquidated, or Contingent Claims (the "Partial Objection"). In footnote 2 of the Partial Objection, OPL asserts that the misconduct relating to the natural gas trading platform is at issue in determining the Debtors' liability to California ratepayers under the timely-filed original Claims. On February 1, 2005, the Debtors filed objections to the Claims and argued that the Federal Power Act (the **[\*\*3]** "FPA") preempts the Claims and the filed rate doctrine precludes consideration of them.

On March 16, 2005, OPL filed the motion to amend proofs of claim (Claim Nos. 15231-33),<sup>2</sup> **[\*\*4]** to include a cause of action based on the Debtors' alleged manipulation of the California natural gas market. (collectively, the "Gas Claims"). On April 11, 2005, the Debtors filed its objection the relief sought by OPL.<sup>3</sup>

The issues before the Court are (1) whether the Claims are preempted by the Federal Power Act (the "FPA") and precluded by the filed rate doctrine, (2) whether OPL may amend the Claims to include additional claims concerning the alleged manipulation of California's gas market. Upon consideration of the pleadings and arguments of the parties, the Court finds that because the FERC has exclusive jurisdiction over interstate sales of wholesale electricity, the Claims sought to be enforced by OPL are preempted by the FPA. Further, the filed rate doctrine also precludes consideration of the Claims. In addition, the Court finds that OPL's **[\*79]** request to amend its original proofs of claim against the Debtors is not warranted since OPL has failed to meet the standard for a motion to amend. In that, it has included new claims **[\*\*5]** or created new causes of action in its request, and the amendment was not timely asserted. Therefore, the Court sustains the Debtors' objection to the Claims and the Debtors' objection to the motion to amend. Further, the Court finds that even if the amendment regarding the Gas Claims were granted, the filed rate doctrine would preclude the Court from considering such claims.

## I. BACKGROUND

Commencing on December 2, 2001, and from time to time continuing thereafter, the Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). On July 15, 2004, the Court entered an Order confirming the Debtors' Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors (the "Plan") in these cases. The Plan became effective on November 17, 2004.

This litigation arises out of the California energy crisis of 2000-01. Prior to the energy crisis, the California legislature had passed Assembly Bill 18904 (the "Bill")<sup>4</sup> to create two non-governmental entities, the California Power Exchange (the "PX") and the California Independent System Operator (the "ISO"), to operate markets and manage the sale of electricity. The PX and **[\*\*6]** the ISO were organized under California law, but regulated by FERC. *California v. Dynegy, Inc., 375 F.3d 831, 850 (9th Cir. 2004)*. The central transactions, wholesale sales of energy in interstate commerce, were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Further, the centralized wholesale spot electricity markets operated by the ISO and the PX were established subject to FERC review and approval. The ISO and the PX served as clearinghouses. Since August 2, 2000, FERC has commenced refund proceeding, and partnership and gaming proceeding to investigate certain of the Debtors. FERC found that the Debtors engaged in gaming<sup>5</sup> in the form of inappropriate trading strategies and further

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<sup>2</sup> OPL filed the motion to amend its original proofs of claim against Enron North America Corp. (Claim No. 15231), Enron Corp. (Claim No. 15232), and Enron Energy Services, Inc (Claim No. 15233) based on their alleged manipulation of the natural gas market in California. Because OPL did not file the amendment against Enron Energy Marketing Corp. (Claim No. 15229), Enron Power Marketing Inc. (Claim No. 15230), Enron Energy Services, LLC (Claim No. 15234) and Enron Energy Services North American, Inc (Claim No. 15235), it is presumed that these entities did not involve the gas market manipulation.

<sup>3</sup> The Debtors responded to the relief sought by OPL as if it included a request for leave to file late proofs of claim. However, since OPL neither briefed nor argued such a request, the Court only addresses the relief sought as a request to amend OPL's timely-filed original Claims.

<sup>4</sup> 1996 Cal. Stat. 854

engaged in the deliberate submission of false information or the deliberate omission of material information. [Enron Power Mktg., Inc., et al., 106 FERC P 61,024 \(2004\)](#). Both proceedings are ongoing, including the determination of remedies by FERC.

## [\*\*7] II. DISCUSSION

### 1. Preemption and Filed Rate Doctrine

#### A. Legal Standard of Preemption

[HN2](#) [↑] "Federal preemption of state law is rooted in the [Supremacy Clause, Article VI, clause 2, of the United States Constitution](#)." *Transmission Agency v. Sierra Pac. Power Co.*, 295 F.3d 918, 928 (9th Cir. 2002). Where Congress manifests intent to occupy an entire regulatory field, any remedy sought outside of the congressional scheme is considered completely preempted. [Metropolitan Life Ins. Co. v. Taylor](#), 481 U.S. 58, 63-64, 95 L. Ed. 2d 55, 107 S. Ct. 1542 (1987). Federal courts have rarely identified legislation that has been found to completely preempt state jurisdiction. [Caterpillar, Inc. v. \[\\*80\] Williams](#), 482 U.S. 386, 393, 96 L. Ed. 2d 318, 107 S. Ct. 2425 (1987).

Here, neither party raises the argument that complete preemption is applicable, nor is there any evidence in the record that would support the conclusion that Congress intended for complete preemption to apply in this case.

[HN3](#) [↑] In the absence of an express preemption by Congress, state law is preempted (1) "when Congress intends that federal law occupy a given field." [Silkwood v. Kerr-McGee Corp.](#), 464 U.S. 238, 248, 78 L. Ed. 2d 443, 104 S. Ct. 615 (1984) [\*\*8] ("Field Preemption"), and (2) "to the extent that state law actually conflicts with federal law, that is, when it is impossible to comply with both state and federal law, or where the state law stands as an obstacle to the accomplishment of the full purposes and objectives of Congress." *Id.* ("Conflict Preemption").

#### B. Preemption

##### 1) Field Preemption

The Debtors, in support of their position that the Claims should be barred by FERC's exclusive jurisdiction, cite to [Public Util. Dist. No 1 v. IDACORP Inc.](#), 379 F.3d 641 (9th Cir. 2004), Dynegy, and [Public Util. Dist. No. 1 v. Dynegy Power Mktg., Inc.](#), 384 F.3d 756 (9th Cir. 2004). These cases addressed FERC's exclusive jurisdiction and its remedial power concerning the wholesale electricity market. The Debtors argue that the Claims, alleging violations of state antitrust and unfair competition law, are nearly identical to those involved in the cited cases, therefore, for the reasons set forth in those cases, field preemption is applicable here.

The Dynegy court ruled that "state actions against wholesale electricity suppliers alleging violations of California's unfair business practices law are [\*\*9] preempted by FPA because the conduct the state sought to condemn was expressly governed by the ISO tariffs and they encroach upon the substantive provisions of the tariff, an area reserved exclusively to FERC, both to enforce and to seek remedy." [375 F.3d at 852](#).

The Court finds that [HN4](#) [↑] the statute's framework under the FPA supports the conclusion in [Dynegy](#) that FERC has been granted broad authority by Congress, in addition to the authority to determine the "just and reasonable rates" for wholesale power. The statute delegates to the Federal Energy Commission "exclusive authority to regulate the transmission and sale at wholesale of electric energy in interstate commerce except those which

<sup>5</sup> [HN1](#) [↑] The ISO tariff, through the ISO's Market Monitoring and Information Protocol defines gaming, in part, as "taking unfair advantage of the rules and procedures set forth in the PX or the ISO tariffs, Protocols or Activity Rule . . . to the detriment of the efficiency of, and of consumers in, the ISO markets." [Am. Electric Power Service Corp., et al., 103 FERC P 61,346 \(2003\)](#).

Congress has made explicitly subject to regulation by the states. . . . Retail sales of electricity and wholesale intrastate sales are within the exclusive jurisdiction of the states." Federal Power Act, [16 U.S.C. § 824-824m](#).

Neither party disputes that the transactions at issue involved wholesale interstate sales of electricity. Further, there has been no evidence presented or any representation by either party that the sales that gave rise to this dispute **[\*\*10]** should be characterized as either retail sales of electricity or wholesale intrastate sales. [HN5](#)<sup>↑</sup> The statute provides that upon a determination by FERC that "any rate charge, or classification, demanded, observed, charged, or collected by any public utility for any *transmission or sale* subject to the jurisdiction of the Commission, or that any rule, regulation, *practice, or contract affecting such rate, charge, or classification* is unjust, unreasonable, unduly discriminatory or preferential, *the Commission shall determine* the just and reasonable rate, charge, classification, rule, regulation, *practice, or contract* to be thereafter observed and in force, and shall fix the same **[\*81]** by order." Federal Power Act, [16 U.S.C. § 824e](#) (emphasis added).

Moreover, [HN6](#)<sup>↑</sup> pursuant to the statute, FERC possesses broad remedial authority to address anti-competitive behavior, specifically through profit disgorgement and refunds. Further, FERC can proceed by rulemaking rather than case-by-case adjudication, and can rely on general findings of systemic monopoly conditions and the resulting potential for anti-competitive behavior, rather than evidence of monopoly and undue **[\*\*11]** discrimination on the part of individual utilities. Federal Power Act, §§ 205, 206(a), as amended, [16 U.S.C.A. §§ 824d, 824e](#); Department of Energy Organization Act, § 403(c), [42 U.S.C.A. § 7173\(c\)](#).

In addition, after the deregulation of California energy markets, the central transactions and the wholesale sales of energy in interstate commerce were governed by FERC approved rules and a FERC "jurisdictional" ISO and PX. Having examined FERC's regulatory authority over the deregulated electricity market in California, the *Snohomish* court concluded, "FERC is doing enough regulation to justify federal preemption of state laws under the market-based system of setting wholesale electricity rates." [Public Util. Dist. No. 1, 384 F.3d at 760-61](#). For instance,

(1) FERC continued to oversee wholesale electricity rates by reviewing and approving a variety of documents filed by the PX and the ISO. FERC approved the market-based tariffs only upon a showing that the seller lacked or had mitigated its market power. (2) FERC required each seller to file quarterly reports under FPA § 205(c) [16 U.S.C. § 824d\(c\)](#). (3) **[\*\*12]** FERC reviewed and approved detailed tariffs filed by the PX and the ISO, which described in detail how the markets operated by each entity would function. *Id.*

In addition, [HN7](#)<sup>↑</sup> "each participant in the PX and the ISO markets was required to sign an agreement acknowledging that the tariff filed by either the PX or the ISO would govern all transactions in that market." *Id.* The Court also recognizes that "entities that transact through the ISO or [the] PX and engage in improper practices<sup>6</sup> are in violation of filed tariffs. . . . FERC and the Market Surveillance Unit are directed by the ISO's Market Monitoring and Information Protocol to refer matters to the FERC for enforcement." [103 FERC P 61,346](#).

**[\*\*13]** Moreover, the Court finds that [Otter Tail Power Co. v. United States, 410 U.S. 366, 35 L. Ed. 2d 359, 93 S. Ct. 1022 \(1973\)](#), and [California v. Federal Power Commission, 369 U.S. 482, 8 L. Ed. 2d 54, 82 S. Ct. 901 \(1962\)](#) are not controlling in the instant case. In both cases, the Supreme Court found that Congress does not intend to bar the government from bringing actions in violation of antitrust laws related to filed tariffs before regulatory commissions. However, two important differences exist. First, both cases discussed issues of the **[\*82]** interaction between federal administrative law and federal antitrust law; thereby no state law preemption issue was presented

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<sup>6</sup> [HN8](#)<sup>↑</sup> Since 1998, the ISO and the PX tariffs have contained provisions that identify and prohibit "gaming" and "anomalous market behavior" in the sale of electric power. "Anomalous market behavior" is (1) behavior that departs significantly from the normal behavior in competitive markets that do not require continuing regulation or (2) as behavior leading to unusual or unexplained market outcomes. Circumstances include a) withholding of generation capacity under circumstances in which it would normally be offered in a competitive market; b) unexplained or unusual redeclarations of availability; c) unusual trades or transactions; d) pricing and bidding patterns that are inconsistent with prevailing supply and demand conditions; and e) unusual activity or circumstances relating to imports from or exports to other markets or exchanges." [Am. Elec. Power Serv. Corp. et al., 103 F.E.R.C. P 61346 \(2003\)](#).

in these cases. In *California v. Federal Power Commission*, a gas company filed a motion to dismiss the antitrust suit pursuant to the Clayton Act, § 7 as amended [15 U.S.C.A. § 18](#), or in the alternative, to stay it, pending completion of the proceedings for its authority to acquire another company's assets pursuant to the Natural Gas Act (the "NGA"), § 7(c) as amended [15 U.S.C.A. § 717f\(c\)](#), before the [Power Energy Commission](#). [369 U.S. at 483](#). In *Otter Tail Power*, the government brought [\*\*14] an action against an electric power company to enjoin violations of the Sherman Act, [15 U.S.C.A. § 2](#). [410 U.S. at 368](#). In order to protect market competition in certain cases, Congress did not expressly displace federal antitrust laws. The Court will not address whether Congress has left room for enforcement of state antitrust laws because OPL does not argue that state [antitrust law](#) and federal [antitrust law](#) would be impacted the same way. Further, the Court notes that the Ninth Circuit in *Snohomish* and *Dynegy* did not discuss the issue of the similarity between California [antitrust law](#) and [Sherman Act](#).<sup>7</sup>

[\*\*15] Second, and more importantly, a critical distinction between the instant matter and the two cited cases is that there is a regulatory scheme against anti-competitive behavior that has been entrusted to FERC. As the Court discussed above, the statute under [16 U.S.C.A. §§ 824d, 824e\(a\)](#) provides FERC with broad remedial authority to address anti-competitive behavior. In fact, FERC has exercised this power to act in the proceedings instituted against the Debtors concerning alleged market manipulation during the energy crisis. FERC has asserted that it "can order disgorgement of monies above the post-October 2, 2000 refunds ordered in the California Refund Proceeding, if it finds violations of the ISO and the PX tariffs and finds that a monetary remedy is appropriate for such violations. It can additionally order additional disgorgement of unjust profits for tariff violations that occurred after October 2, 2000." [103 FERC P 61,346](#). Further, [HN9](#)<sup>↑</sup> "implicit in Commission orders granting market-based rates to the marketers is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. Companies failing to adhere to such standards [\*\*16] were and are subject to revocation of their market-based rate authority." [106 FERC P 61,024](#).

In contrast, the court in *California v. Federal Power Commission* concluded that the NGA did not contain a provision to immunize the carriers involved in the mergers from the [Clayton Act](#). [369 U.S. at 485](#). "The Commission's standard, set forth in [§ 7 of the NGA](#), will serve the public convenience and necessity.' If existing natural gas companies violate the antitrust laws, the Commission is directed by [§ 20\(a\)](#) to transmit such evidence' to the Attorney General." [Id. at 486](#). Similarly, the Court in *Otter Tail Power* found that the limited authority of the Federal Power Commission to order interconnections was not intended to be a substitute for the [Sherman Act](#). [410 U.S. at 375](#). Moreover, the Supreme Court in *Carnation Co. v. Pacific Westbound Conference*, [383 U.S. 213, 383 U.S. 932, 15 L. Ed. 2d 709, 86 S. Ct. 781 \(1966\)](#) [\*83] declined to grant antitrust immunity to a shipping company because "the provisions of the Shipping Act, 46 U.S.C.A. § 801, can not reasonably be construed as an implied repeal of antitrust regulation of the shipping industry's [\*\*17] rate-making activities." [Id. at 217](#). The Shipping Act does not give the Federal Maritime Commission (the "FMC") any mandate to regulate rate competition and the statutory scheme was designed to minimize the role of the FMC. *Square D Co. v. Niagara Frontier Tariff Bureau*, [476 U.S. 409, 422, 90 L. Ed. 2d 413, 106 S. Ct. 1922 \(1986\)](#).

The Court further finds that *Grays Harbor* and *Gulf States Util. Co. v. Alabama Power Co.*, [824 F.2d 1465 \(5th Cir. 1987\)](#) are not applicable in the instant case. The courts in both cases concluded that the Claims concerning contractual disputes were not within the scope of FERC's jurisdiction. The Court finds that the facts here are distinguishable. First, the Claims in the cited cases were related to contractual issues, which exclusively fall within a state's jurisdiction. The court in *Grays Harbor* granted the utility leave to amend its complaint to seek declaratory relief only as to issues of contract formation. [379 F.3d. at 652-53](#). Similarly, the court in *Gulf States* held that executed contract performance, such as the failure to negotiate in good faith and fraud, were not preempted by the FPA. [824 F.2d at 1474](#). [\*\*18] Here, no evidence or argument presented before the Court demonstrates that there is an issue involving contractual disputes. Second, contract formation issues would not necessarily intrude upon the

<sup>7</sup> In *Snohomish*, consumer utility in Washington sued generators and traders of wholesale electricity, for violations of California state antitrust and consumer protection laws. [384 F.3d 756](#). In *Dynegy*, Attorney General of the State of California brought state court actions against wholesale electricity suppliers for violations of California's unfair business practices law. [375 F.3d 831](#).

rate-setting jurisdiction of FERC. [Public Util. Dist. No 1, 379 F.3d. at 653.](#) Therefore, field preemption bars OPL from pursuing the Claims.

#### C. Conflict Preemption

As to conflict preemption, for the foregoing reasons, the Court concludes that FERC has broad authority concerning anti-competitive activities related to the filed rate, apart from that FERC has authority to determine the "just and reasonable" rates for wholesale power. A conflict between the FPA in which grants FERC jurisdiction over the anti-competitive acts and state antitrust claims exists. Accordingly, conflict preemption also bars OPL from pursuing the Claims.

#### D. Filed Rate Doctrine

Another threshold question before the Court is whether the Court would have to determine a tariff. [HN10](#)<sup>↑</sup> The filed rate doctrine is essentially a rule of jurisdiction whose applicability is circumscribed by both the congressionally mandated jurisdiction of the regulatory agency and the occurrence of the triggering event of [\\*\\*19](#) filing a rate or tariff. The filed rate doctrine is applicable where rates were filed with a federal regulatory agency and where the offending transactions are carried out with reference to a filed tariff. *E& J. Gallo Winery v. Encana Energy Servs., Inc.*, Case No. CV F 03-5412 AWILJO. at 15. The Court recognizes that the filed rate doctrine "forbids a regulated entity from charging rates for its service other than those properly filed with the appropriate federal regulatory authority." [Ark. L.A. Gas Co. v. Frank Hall, 453 U.S. 571, 577-78, 69 L. Ed. 2d 856, 101 S. Ct. 2925 \(1981\)](#). The Court also acknowledges that the purpose of the doctrine is "preservation of the agency's primary jurisdiction over reasonableness of rates and the need to insure that regulated companies charge only those rates of which the agency has been made cognizant." [Cleveland v. Federal Power Comm'n, 174 U.S. App. D.C. 1, 525 F.2d 845, 854 \(D.C. Cir. 1976\).](#)

In addition, FERC required each seller to file quarterly reports pursuant to FPA § 205(c) [16 U.S.C. § 824d\(c\)](#) on transaction-specific [\\*84](#) information about its sales and purchases at market-based rates. The court in *Grays Harbor* concluded [HN11](#)<sup>↑</sup> "while market-based [\\*\\*20](#) rates may not have historically been the type of rate envisioned by the filed rate doctrine, they do not fall outside the purview of the doctrine." [379 F.3d at 651.](#)

Further, the Court agrees with the opinion of the *California v. FERC* court which concluded that [HN12](#)<sup>↑</sup> "the reporting requirements are an integral part of a tariff, with FERC's implied enforcement mechanisms sufficient to provide substitute remedies for the obtaining of refunds for the imposition of unjust, unreasonable and discriminatory rates." [Cal. ex rel. Lockyer v. FERC, 383 F.3d 1006 at 1016.](#) On August 13, 2002, FERC's Initial Report in Docket No. PA02-2-000 concluded that the Debtors engaged in the deliberate submission of false information or the deliberate omission of material information.<sup>8</sup> Then, FERC concluded that such behavior constituted market manipulation and resulted in unjust and unreasonable rates and violated the express requirements in the orders allowing the Debtors to make sales at market-based rates. [106 FERC P 61,024.](#) As noted by FERC,

[HN13](#)<sup>↑</sup> implicit in Commission orders granting market-based rates is a presumption that a company's behavior will not involve fraud, deception or misrepresentation. [\\*\\*21](#) Companies failing to adhere to such standards were and are subject to revocation of their market-based rate authority. The Debtors were expressly directed, when they were granted market-based rate authority, to inform the FERC promptly of changes in

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<sup>8</sup> FERC found that the Debtors failed to inform FERC in a timely manner of changes in their market shares that resulted from their gaining influence/control over others' facilities, as required under their market-based rate authorization. [106 FERC P 61,024.](#)

status (which would include changes in their generation market shares) that reflect a departure from the characteristics that the FERC relied upon in granting market-based rate authority. *Id.*

Moreover, the Court in *California v. FERC*, indirectly recognized the application of the filed rate doctrine when marketers had not properly reported to FERC where such improper reporting affected the reasonableness of the tariff approved by FERC. [383 F.3d at 1016](#).

Without the availability of retroactive refunds, "parties aggrieved by the illegal rate would have no FERC remedy, and the filed rate doctrine would preclude a direct action against the offending seller. That result does not comport with the underlying theory or the regulatory structure established by the FPA." *Id.*

[\*\*22] The Court finds that determining the liability or the legal right of OPL against the Debtors for violation of the antitrust laws would have to be measured by the tariff. [HN14](#)<sup>↑</sup> In addressing the right of action that a violation of the antitrust laws gives to one who has been injured in its business or property, the Supreme Court in *Keogh v. Chicago & N.W.R. Y. Co.*, [260 U.S. 156, 67 L. Ed. 183, 43 S. Ct. 47 \(1922\)](#), stated that "injury implies violation of a legal right." [Id. at 163](#). The Supreme Court concluded that "the legal rights of [a] shipper as against [a] carrier in respect to a rate are measured by the published tariff." [Id. at 163](#). Justice Brandeis explained "[a] rate is not necessarily illegal because it is the result of a conspiracy in restraint of trade in violation of the *Anti-Trust Act*. What rates are legal is determined by the Act to Regulate Commerce. Under *Section 8* of the latter act . . . the exaction of any illegal rate makes the carrier liable to the person injured thereby for the full amount of [\*85] damages sustained in consequence of any such violation." [Id. at 162](#). Thus, the finding of liability in antitrust laws would be integral [\*\*23] to the Court's determination of whether the Debtors are liable due to their violations of state **antitrust law** and unfair competition law. For instance, the Court could not determine the overcharge claim owed by the Debtors for any electricity market manipulation without first deciding the reasonableness of the filed tariff.

The Supreme Court case, *Arkansas Louisiana*, further supports the Court's position that the filed rate doctrine should apply here. "In asserting that the filed rate doctrine had no application, respondents in *Arkansas Louisiana* contended that the state court has done no more than determine the damages they have suffered as a result of the breach of a contract by a gas company." [453 U.S. at 579](#). The Supreme Court rejected this argument by reasoning that "the mere fact that respondents brought this suit under state law would not rescue it, for when Congress has established an exclusive form of regulation . . . there can be no divided authority over interstate commerce. . . . [HN15](#)<sup>↑</sup> Under the filed rate doctrine, FERC alone is empowered to make that judgment, and until it has done so, no rate other than the one on file may be charged." [Id. at 580-84](#). [\*\*24]

Moreover, to award monetary relief, the Court would have to determine a "fair price." Thus, the filed rate doctrine bars the Court from awarding monetary damages sought by OPL. Nonetheless, the Court finds that injunctive relief would also be unavailable to OPL. The Court agrees with the Ninth Circuit's decision in *Snohomish*, which declined to grant injunctive relief because such relief is barred by the filed rate doctrine and preemption principle. [384 F.3d at 762](#). [HN16](#)<sup>↑</sup> "Remedies for breach and non-performance of FERC-approved operating agreements in the interstate wholesale electricity market fall within the exclusive domain of FERC." [Dynegy, 375 F.3d at 836](#).

The decisions from the Second Circuit in *Sun City Taxpayers' Association v. Citizens Utilities Co.*, [45 F.3d 58 \(2d Cir. 1995\)](#) and *Wegoland Ltd. v. NYNEX Corp.*, [27 F.3d 17 \(2d Cir. 1994\)](#), provide an additional basis for dismissal of the Claims sought by OPL. The Second Circuit in *Sun City Taxpayers' Association* affirmed the decision from the district court, which had declined the plaintiff's invitation to find a fraud exception to the filed rate doctrine. In [\*\*25] determining whether the filed rate doctrine applied, the court focused on the impact the court's decision would have on agency procedures and rate determination. *Sun City Taxpayers' Ass'n v. Citizens Utils. Co.*, [847 F.Supp. 281, 291 \(D. Conn. 1994\)](#). The Second Circuit in *Wegoland* recognized that [HN17](#)<sup>↑</sup> the filed rate doctrine exists for reasons independent of the type of plaintiff maintaining the action. Those reasons include that (a) legislatively appointed regulatory bodies have institutional competence to address rate-making issues, (b) courts lack the competence to set utility rates, and (c) the interference of courts in the rate-making process would subvert the authority of rate-setting bodies and undermine the regulatory regime. [27 F.3d at 21](#).

Therefore, having considered the policy objectives, the Court finds it is inappropriate to frustrate FERC's jurisdiction afforded by Congress. The Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. The Court, therefore, rejects OPL's challenge to the application of the filed [\*86] rate [\*\*26] doctrine. Accordingly, the filed rate doctrine bars the relief sought by OPL.

## 2. Motion to Amend<sup>9</sup>

### A. General Standards For Permitting A Post-Bar Date Amendment To Timely-Filed Proofs Of Claim

**HN18**[] Bankruptcy [Rule 3003\(c\)\(3\)](#) directs a bankruptcy court to establish a bar date beyond which proofs of claim are disallowed in a chapter 11 case. The bar date is critically important to the administration of a successful chapter 11 case for it intended "to be a mechanism providing the debtor and its creditors with finality." [\*In re Manville Forest Products Corp.\*, 89 B.R. 358, 374 \(Bankr. S.D.N.Y. 1988\)](#). In particular, a "bar [date] [\*\*27]" order serves the important purpose of enabling the parties to a bankruptcy case to identify with reasonable promptness the identity of those making claims against the bankruptcy estate and the general amount of the claims, a necessary step in achieving the goal of successful reorganization." [\*In re Keene Corp.\*, 188 B.R. 903, 907 \(Bankr. S.D.N.Y. 1995\)](#) (quoting [\*First Fidelity Bank, N.A. v. Hooker Invs., Inc.\* \(\*In re Hooker Invs., Inc.\*\), 937 F.2d 833, 840 \(2d Cir. 1991\)](#)). Therefore, a bar date order "does not function merely as a procedural gauntlet,' . . . but as an integral part of the reorganization process." *Id.* (quoting [\*First Fidelity\*, 937 F.2d at 840](#) (quoting, in turn, [\*United States v. Kolstad\* \(\*In re Kolstad\*\), 928 F.2d 171, 173 \(5th Cir. 1991\)](#))). Accordingly, a bar date is likened to a statute of limitations which generally must be strictly observed. *Id.* (citing [\*Maxwell Macmillan Realization Liquidating Trust & MCA GAO, Inc. v. Aboff\* \(\*In re Macmillan\*\), 186 B.R. 35, 49 \(Bankr. S.D.N.Y. 1995\)](#)).

**HN19**[] The decision to grant or deny an amendment to a timely-filed proof of claim rests with the sound [\*\*28] discretion of a bankruptcy judge." [\*In re McLean Industries, Inc.\*, 121 B.R. 704, 708 \(Bankr. S.D.N.Y. 1990\)](#). "Although amendments to proofs of claim should in the absence of contrary equitable considerations or prejudice to the opposing party be freely permitted, such amendments are not automatic. . . ." [\*In re W.T. Grant Co.\*, 53 B.R. 417, 420 \(Bankr. S.D.N.Y. 1985\)](#). The amendments "are allowed, [however,] where the purpose is to cure a defect in the claim as originally filed, to describe the [original] claim with greater particularity or to plead a new theory of recovery on the facts set forth in the original claim." *Id.*; [\*In re G.L. Miller & Co.\*, 45 F.2d 115, 116 \(2d Cir. 1930\)](#) (enumerating same three factors for amending claims). Nevertheless, an "amendment may not be used as a mechanism for circumventing the bar date." [\*In re Drexel Burnham Lambert Group\*, 151 B.R. 684, 694 \(Bankr. S.D.N.Y. 1993\)](#). Therefore, a bankruptcy court must carefully scrutinize a post bar-date amendment "to ensure that the amendment is truly amending timely-filed [proofs of] claims and not asserting an entirely new claim." [\*In re Macmillan\*, 186 B.R. at 49](#); [\*\*29] see [\*In re Alexander's Inc.\*, 176 B.R. 715, 723 \(Bankr. S.D.N.Y. 1995\)](#) (citing [\*In re W.T. Grant\*, 53 B.R. at 422](#)). An amendment will not be permitted when its purpose is to create an entirely new claim. [\*In re Andover Togs, Inc.\*, 231 B.R. 521, 549 \(Bankr. S.D.N.Y. 1999\)](#).

**HN20**[] When deciding whether to permit an amendment to a proof of claim, a bankruptcy court is guided by a two-prong [\*87] test. [\*Integrated Resources, Inc. v. Ameritrust Co. N.A.\* \(\*In re Integrated Resources, Inc.\*\), 157 B.R. 66, 70 \(S.D.N.Y. 1993\)](#) (citing [\*In re Black & Geddes, Inc.\*, 58 B.R. 547, 553 \(S.D.N.Y. 1983\)](#)). "A court must first look to whether there was timely assertion of a similar claim or demand evidencing an intention to hold the estate liable." *Id.* (quoting [\*Black & Geddes\*, 58 B.R. at 553](#)). If there were such a timely assertion, the court then examines each fact within the case and determines whether it would be equitable to allow the amendment. *Id.* In balancing the equities, the court considers the following equitable factors:

<sup>9</sup>The Court addressed issue of whether a Claimant may amend a timely-filed proof of claim to include an additional claim in its memorandum decision in [\*In re Enron Corp.\*, 298 B.R. 513, 518-26 \(Bankr. S.D.N.Y. 2003\)](#). This section of the Opinion is based on the legal analysis regarding an amendment as set forth in *In re Enron Corp.*

(1) undue prejudice to opposing party; (2) bad faith or dilatory behavior [\*\*30] on part of the claimant; (3) whether other creditors would receive a windfall were the amendment not allowed; (4) whether other claimants might be harmed or prejudiced; and (5) the justification for the inability to file the amended claim at the time the original claim was filed.

Integrated Resources, 157 B.R. at 70 (quoting McLean Industries, 121 B.R. at 708); see also In re Miss Glamour Coat Co., 1980 U.S. Dist. LEXIS 14545, at \*12-13 (S.D.N.Y. 1980) (formulating similar equitable factors for considering in applying the two-prong test in permitting an amendment to a proof of claim). This second prong of the test is applied "only if the first prong is satisfied and the claim qualifies as an amendment and not a new claim." In re Sage-Dey, Inc., 170 B.R. 46, 49 (Bankr. N.D.N.Y. 1994).

#### B. Application Of Rule 15(c) Of The Federal Rules Of Civil Procedure

**HN21**[↑] Neither the Bankruptcy Code nor Bankruptcy Rules directly address an amendment of a proof of claim. Nevertheless, in determining whether to permit a post-bar date amendment to a timely-filed proof of claim [\*\*31] under the first prong of the two-prong test, several courts have applied Rule 15(c) of the Federal Rules of Civil Procedure ("Rule") by analogy or explicitly, pursuant to Bankruptcy Rules 7015 and 9014(c), to analyze such an amendment. See Enjet, Inc. v. Maritime Challenge Corp. (In re Enjet, Inc.), 220 B.R. 312, 315 (E.D. La. 1998) (noting that "numerous courts have applied Rule 7015 and Rule 15(c) explicitly or by analogy in non-adversary [bankruptcy] proceedings"); In re Brown, 159 B.R. 710, 714 (Bankr. D.N.J. 1993) (noting that Rule 15's "standards for allowing amendments to pleadings in adversary proceedings . . . also apply to amendments to a proof of claim"); Liddle v. Drexel Burnham Lambert Group, Inc., 159 B.R. 420, 425 (S.D.N.Y. 1993) ("Several courts have held that the analysis for amendment of claims in bankruptcy is identical to the analysis required by Rule 15"); McLean Industries, 121 B.R. at 710 ("The test under Rule 15 is basically the same as that developed in the case law for amending claims in bankruptcy . . .").

**HN22**[↑] Bankruptcy Rule 7015 provides that "Rule [\*\*32] 15 . . . applies in adversary proceedings." Although "the filing of an objection to a proof of claim is a contested matter,' [and] not an adversary proceeding[,] . . . Bankruptcy Rule 9014 permits a [bankruptcy] court, at its discretion, to extend Rule 7015 to contested matters as well as adversary proceedings." In re Stavriots, 977 F.2d 1202, 1204 (7th Cir. 1992) (citations omitted). In particular, **HN23**[↑] Bankruptcy Rule 9014(c) states that "the court may at any stage in a particular matter direct that one or more of the other rules in Part VII [which includes Bankruptcy Rule 7015] shall apply" and, further, the Advisory Committee Note to the rule provides that "when the rules of Part VII are applicable to a contested matter, reference in the Part VII rules to [\*88] adversary proceedings is to be read as a reference to a contested matter." "Part VII of the Bankruptcy Rules is based on the premise that to the extent possible practice before the bankruptcy courts and the district courts should be the same." Stavriots, 977 F.2d at 1204 (quoting Advisory Committee Note to Bankruptcy Rule 7001). Accordingly, the Court exercises its discretion under Bankruptcy [\*\*33] Rule 9014(c) in applying by analogy the standards of subsections (c)(2) of Rule 15 to determine whether OPL's Gas Claims relate back to its original Claims against the Debtors.

Rule 15(c) provides, in pertinent part, that

**HN24**[↑] an amendment of a pleading relates back to the date of the original pleading when  
 (2) the claim or defense asserted in the amended pleading arose out of the conduct, transaction, or occurrence set forth or attempted to be set forth in the original pleading,

Fed. R. Civ. P. 15(c)(2) (2004). **HN25**[↑] After the statute of limitations has run (here, the Bar Date), Rule 15(c)(2) is used for amending an original pleading (here, the original Proof of Claim) to add a claim or defense.

**HN26**[↑] "Courts, in general, have moved away from the cause of action' test in allowing an amendment under Rule 15 . . . , and instead, on [sic] amendment has been allowed which adds another claim if it is arising out of the same transaction or occurrence." Miss Glamour, 1980 U.S. Dist. LEXIS 14545, at \*9; see CIT Group/Factoring Mfrs. Hanover, Inc. v. Srour, 138 B.R. 413, 418 (Bankr. S.D.N.Y. 1992) (holding same). The Claims concerning

market manipulation [\*\*34] in the wholesale electricity market arise out of certain trading strategies that the Debtors utilized in the California wholesale electricity markets, which allegedly wrongfully inflated the electricity bills of California ratepayers. The trading strategies, which OPL alleges as unlawful, unfair and fraudulent business practices in the original Claims, include as follows:

(1) The Debtors manipulated supplies in the California *wholesale electricity markets* by withholding supplies from the PX and ISO markets. Thus creating artificial shortages of electricity which, in turn, raised prices, (2) the Debtors engaged in a "megawatt laundering," whereby Enron purchased electricity from a California generator, but instead of directly bidding the power into the PX or ISO markets, the trader sold the rights to the power to an affiliate outside of California. The affiliate then would sell the rights to the power back into California at even greater prices in order to inflate the price of electricity, (3) the Debtors engaged in a practice of scheduling energy over a transmission line that it knew would be congested at a given point, even though it had no intention of actually using [\*\*35] that line for transmission, in order to receive a payment not to use that line. (emphasis added).

By comparison, the practices of market manipulation in the Gas Claims include wash trades, also known as churning, and false reporting of gas market transactions to publications for compilation and price indexes. [HN27](#)<sup>10</sup> Wash trading occurs when a party simultaneously buys and sells the same commodity at or near the same price within a very short period time so that the party has no financial risk in the transactions. Wash trading establishes "bogus" prices which are not related to real conditions in the gas market, and creates an illusion of volume and liquidity which encourages other market participants to engage in the frenzy. Thus, the Court finds that the underlying alleged practices by [\*89] the Debtors in two markets were vastly different.

Additionally, the legal analysis regarding each of the two markets is different because they are regulated by different federal acts. The Natural Gas Act (the "NGA") regulates the gas market, while the FPA regulates the electricity market. While the jurisdictional provisions of the FPA and the NGA may be similar, because of the unique context of the natural [\*\*36] gas market during the energy crisis in California, the legal conclusion on whether the NGA preempts state law claims may be drawn differently from the Court's finding in the electricity market. Actually, the district court in Nevada, [\*In re: Western States Wholesale Natural Gas Antitrust Litigation\*, 346 F.Supp.2d 1123 \(D. Nev. 2004\)](#), held that NGA did not completely preempt state law claims. While the Court does not address herein the issue as to whether the NGA preempts state law claims, the Court notes the differences in the two markets. For instance,

unlike the electricity market, where FERC reviews and approves detailed tariffs filed by the PX and the ISO, at the time of the alleged misconduct in the natural gas market, FERC granted blanket approval for most gas sales. Unlike the energy market, the natural gas market largely was deregulated at the time of the alleged anti-competitive conduct. At that time, [section 284.402 of the FERC](#) regulations contained no explicit guidelines on misconducts, such as churning, spot market, wash sales and netting agreements in gas market. Unlike the energy industry, which partially was regulated by the FERC-supervised ISO [\*\*37] and PX, the natural gas industry was driven almost completely by the market forces of supply and demand.<sup>10</sup>

[Rule 15\(c\)\(2\)](#) requires the Court to consider whether the asserted Gas Claims arose out of the same transaction or occurrence set forth in the original Claims. In its original Claims, OPL made it clear that the perimeter of the alleged market manipulation claims against the Debtors is drawn by OPL within the wholesale electricity market, by stating as follows: "the [original] Claims arise out of certain trading strategies that the Debtors utilized in the California *wholesale electricity markets*, which wrongfully inflated the electricity bills of California ratepayers. By engaging in these unlawful, unfair, and fraudulent business practices, Enron violated [various state laws]."  
(emphasis added).

[\*\*38] See OPL's Statement Regarding Proof of Claim.

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<sup>10</sup> Final Report on Price Manipulation in Western Markets: Fact-Finding Investigation of Potential Manipulation of Electric and Natural Gas Price, Docket No. PA02-2-00, II-61 (Mar. 2003).

Here, the Court has found that the trading strategies in the gas markets are not the same as those stated in the original Claims. Further, since vast differences between the gas and electricity market exist, these two markets are not be interchangeable. The Court agrees that the amendment would change the nature of the original Claims by introducing significantly different factual and legal allegations. Accordingly, the Court finds that the Gas Claims do not arise out of the same transaction or occurrence set forth in the original Claims, that is, these two claims are not related under a [Rule 15\(c\)](#) analysis. Moreover, the Court finds that OPL's Gas Claims are not for the purpose of curing a defect in the original Claims, or supplementing the original Claims with greater particularity or to pleading a new theory of recovery on the facts set forth in the Claims.

[\*90] Additionally, in the first prong of the test, "[a] court must first look to whether there was timely assertion of a similar claim or demand evidencing an intention to hold the estate liable." [Integrated Resources](#) (quoting [Black & Geddes, 58 B.R. at 553](#)). [\*\*\*39] Here, even if the Gas Claims are similar to the original Claims, the Court finds that OPL failed to timely assert the Gas Claims. OPL argues that it put the Court and the Debtors "on notice" in the footnote of the Partial Objection in September 2003. In the footnote, OPL states as follows: "information regarding the Debtor's misuse of the Enron Online natural gas trading platform and its impact on California electricity and natural gas prices, did not become public until after the Claimant filed the Proofs of claim. This misconduct, as well as the Debtors' other misconduct described in the FERC report, is equally at issue in determining the Debtors' liability to California ratepayers." See, footnote 2 of the Partial Objection.

The Court finds that even if footnote 2 sufficiently placed the Debtors on notice as to the inclusion of the alleged gas market manipulation claims in its original Claims against the Debtors under the standard of a motion to amend, such notice was not timely. In that, in August 2002, FERC issued the Initial Report, containing, *inter alia*, the relevant findings regarding the assertions of the Debtors' natural gas market manipulation. On October 11, 2002, Attorney [\*\*\*40] General of the California timely filed proofs of claim regarding the Debtors' alleged manipulation in the electricity and gas markets. In March 2003, FERC issued the Final Report. The claimed notice came six months after the FERC's Final Report and thirteen months after the FERC's Initial Report was available. Both FERC reports discussed the Debtors' alleged manipulation in the electricity and gas markets.

Further, regarding the timing of the motion to amend, the Debtors' Plan was confirmed on July 15, 2004 and the Plan became effective on November 17, 2004. OPL filed motion to amend eight months after the confirmation of the Plan and four months after the Plan had become effective, as well as roughly two and half years after the October 15, 2002 bar date. Most significantly, OPL's motion to amend was filed at least eighteen months after OPL referenced the gas market manipulation claims in its claimed notice, and thirty-one months after FERC's Initial Report became available, containing the relevant information regarding the assertions of the Debtors' gas market manipulation (the State of California and California Department of Water Resources asserted the gas manipulation claims [\*\*\*41] in their timely filed proofs of claim dated October 11, 2002, based on the FERC's finding on the Debtors' alleged misconduct in the gas market in Initial Report. In that FERC's Final Report was not issued until March 2003). Accordingly, the Court finds that the length of the delay in filing the Gas Claims here is substantial.

Thus, OPL has failed to meet the first prong of the test, *i.e.*, it has failed to establish that the amendment was a timely assertion of a similar claim or demand evidencing an intention to hold the estate liable. The second prong of the test on equitable factors is applied "only if the first prong is satisfied, and the claim qualifies as an amendment and not a new claim." [In re Sage-Dey, Inc., 170 B.R., at 49](#). Here, OPL's Gas Claims are new and do not relate back to its original Claims. Thus, the Court does not need to address the second prong of the test. Additionally, the Court considers OPL's new Gas Claims as "other or further claims" that are barred, absent some form of relief, by, [\*\*\*91] *inter alia*, the Confirmation Order.<sup>11</sup> Therefore, based upon OPL's failure to satisfy the first prong of the test, the motion to amend is denied.

<sup>11</sup> The Confirmation Order provides that "all Persons and Entities are hereby precluded from asserting against the Debtors . . . any other or further Claims based upon any act or omission, transaction or other activity of any kind or nature that occurred prior to the Confirmation Date, whether or not the facts or legal bases therefore were known or existed prior to the Confirmation Date. . . ." See, Order Confirming Supplemental Modified Fifth Amended Joint Plan of Affiliated Debtors Pursuant to Chapter 11 of the United States Bankruptcy Code, and Related Relief, p. 22.

**[\*\*42] 3. Filed Rate Doctrine Bars the Gas Claims**

The filed rate doctrine would apply to preclude the Court from considering the Gas Claims even if the motion to amend were allowed. As discussed previously, there were vast differences between the gas and the electricity markets during the energy crisis in California, and the Court notes that the Neveda court in [Natural Gas Antitrust Litigation, 346 F.Supp.2d 1123](#), held that NGA did not completely preempt state law claims. However, regardless of the outcome of preemption issue, the Court is barred from considering the Gas Claims because determining the Debtors' liability or the legal right of OPL against the Debtors for violation of the antitrust laws would have to be measured by the tariff. The Court agrees with the Neveda court in its separate decision concerning the filed rate doctrine, [In re W. States Wholesale Natural Gas Antitrust Litig. 368 F. Supp. 2d 1110 \(D. Nev. 2005\)](#). [HN28](#) "The essential purpose of the filed rate doctrine is to protect the jurisdiction of a regulatory body that Congress has designated to determine whether rates charged, such as those in the natural gas market, [\\*\\*43](#) are just and reasonable. Under the NGA, FEC retains statutory authority over wholesale natural gas prices and therefore the filed rate doctrine applies even though FERC, in exercising its authority, chose to move toward a market-based system." [Id. at 1116](#). Based on the reasons that the Court discussed previously in Section 1.D (Filed Rate Doctrine), the Court lacks authority to impose a different rate than the one approved by a federal agent. Any other conclusion departing from this principle would undermine the filed rate doctrine. Accordingly, the filed rate doctrine would bar the relief sought by OPL, even if the motion to amend were granted.

**IV. CONCLUSION**

For the foregoing reasons, the Court concludes that the Claims sought by OPL concerning electricity market manipulation are preempted by the FPA and precluded by the filed rate doctrine. Therefore, the Court sustains the Debtors' objection to the Claims filed by OPL. Further, because OPL's Gas Claims do not relate back to its original Claims, and the amendment was not timely filed, the motion to amend is denied. The Court further finds that even if the Gas Claims were allowed to be filed, the filed rate doctrine would [\\*\\*44](#) bar the Court from considering the OPL's Gas Claims against the Debtors.

Counsel for the Debtors is directed to settle an order consistent with this Opinion.

Dated: New York, New York

August 5, 2005

Arthur J. Gonzalez

UNITED STATES BANKRUPTCY JUDGE



## Wine & Spirits Retailers, Inc. v. Rhode Island

United States Court of Appeals for the First Circuit

August 10, 2005, Decided

No. 05-1549

**Reporter**

418 F.3d 36 \*; 2005 U.S. App. LEXIS 16718 \*\*

WINE AND SPIRITS RETAILERS, INC. AND JOHN HARONIAN, Plaintiffs, Appellants, v. STATE OF RHODE ISLAND ET AL., Defendants, Appellees.

**Subsequent History:** Motion denied by [Wine & Spirits Retailers, Inc. v. R.I. & Providence Plantations, 2006 U.S. Dist. LEXIS 105612 \(D.R.I., Apr. 11, 2006\)](#)

Subsequent appeal at [Wine & Spirits Retailers, Inc. v. Rhode Island, 481 F.3d 1, 2007 U.S. App. LEXIS 6412 \(1st Cir. R.I., Mar. 20, 2007\)](#)

**Prior History:** [\*\*1] APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF RHODE ISLAND. Hon. Ernest C. Torres, U.S. District Judge.

[Wine And Spirits Retailers, Inc. v. Rhode Island, 364 F. Supp. 2d 172, 2005 U.S. Dist. LEXIS 6093 \(D.R.I., Apr. 8, 2005\)](#)

## Core Terms

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liquor license, advertising, franchisees, rights, holders, retail, licensed, liquor, entity, franchisor, franchise, preliminary injunction, commercial speech, injunction, advice, regulation, alcoholic beverage, package, franchise agreement, district court, coordinated, merits, business activity, anti trust law, license holder, chain store, free speech, trade name, restrictions, concerted

## LexisNexis® Headnotes

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Governments > State & Territorial Governments > Licenses

### [HN1](#) State & Territorial Governments, Licenses

Under Rhode Island law, any individual or entity engaged in the manufacture, sale, or importation of alcoholic beverages must hold a valid license issued by the Department of Business Regulation (DBR). [R.I. Gen. Laws § 3-5-1](#). A Class A retail license entitles the holder to obtain alcoholic beverages from licensed wholesalers and to operate a retail package store, from which the beverages may be sold in sealed containers. [R.I. Gen. Laws §§ 3-7-1, 3-7-3](#). Since 1933, the State has prohibited chain store organizations from holding Class A liquor licenses. [R.I. Gen. Laws § 3-5-11](#). This enactment gave the DBR full discretion to determine whether an entity fell into the "chain store" category.

Business & Corporate Compliance > ... > Governments > Agriculture & Food > Product Promotions

Governments > State & Territorial Governments > Licenses

## **HN2** Agriculture & Food, Food Product Promotions

The Rhode Island General Assembly amended [R.I. Gen. Laws § 3-5-11](#) to identify a set of licensee activities that would allow the Department of Business Regulation (DBR) to find that an entity was in fact a chain store organization. The new statute, enacted July 8, 2004, and effective April 1, 2005, expanded the term "chain store organization" to encompass any group of one or more holders of Class A liquor licenses who engage in one or more of the following practices with respect to the business conducted under such licenses, either directly or indirectly, or have any direct or indirect beneficial interest in the following practices: (i) common, group, centralized, or coordinated purchases of wholesale merchandise; (ii) common billing or utilization of the services of the same person or the same entity in the management or operation of more than one liquor licensed business; (iii) participation in a coordinated or common advertisement with one or more liquor licensed business in any advertising media; (iv) coordinated or common planning or implementation of marketing strategies; (v) participation in agreed upon or common pricing of products; and (vi) any term or name identified as a chain or common entity. [R.I. Gen. Laws § 3-5-11\(b\)\(1\)](#).

Business & Corporate Law > Distributorships & Franchises > Disclosure & Registration > Enforcement of Franchise Requirements

Business & Corporate Law > Distributorships & Franchises > Causes of Action > Restraints of Trade

Business & Corporate Law > Distributorships & Franchises > Franchise Relationships > General Overview

Governments > State & Territorial Governments > Licenses

## **HN3** Disclosure & Registration, Enforcement of Franchise Requirements

By its terms, [R.I. Gen. Laws § 3-5-11\(b\)\(1\)](#) restricts a holder of a Class A liquor license from participating in many business activities that are typical of a franchise relationship.

Business & Corporate Law > Distributorships & Franchises > Disclosure & Registration > Enforcement of Franchise Requirements

Governments > State & Territorial Governments > Licenses

Business & Corporate Law > Distributorships & Franchises > Franchise Relationships > Franchise Agreements

## **HN4** Disclosure & Registration, Enforcement of Franchise Requirements

Simultaneous with the enactment of [R.I. Gen. Laws § 3-5-11\(b\)](#), the Rhode Island General Assembly passed [R.I. Gen. Laws § 3-5-11.1](#). This provision has a similar but more direct effect: it explicitly excludes franchisees from holding Class A liquor licenses.

Business & Corporate Law > Distributorships & Franchises > Disclosure & Registration > Enforcement of Franchise Requirements

Governments > State & Territorial Governments > Licenses

## **HN5** Disclosure & Registration, Enforcement of Franchise Requirements

[R.I. Gen. Laws § 3-5-11.1\(a\).](#)

Business & Corporate Law > Distributorships & Franchises > Franchise Relationships > Franchise Agreements

Business & Corporate Law > Distributorships & Franchises > Causes of Action > General Overview

Business & Corporate Law > Distributorships & Franchises > Disclosure & Registration > Enforcement of Franchise Requirements

Business & Corporate Law > Distributorships & Franchises > Termination > General Overview

Criminal Law & Procedure > ... > Alcohol Related Offenses > Distribution & Sale > Penalties

Governments > State & Territorial Governments > Licenses

## **HN6** Franchise Relationships, Franchise Agreements

[R.I. Gen. Laws § 3-5-11.1](#) nullifies all franchise agreements involving the retail sale of alcoholic beverages, [R.I. Gen. Laws § 3-5-11.1\(b\)](#), stipulates that any franchisor or franchisee who is a party to such an agreement must terminate it within 30 days of the statute's effective date, [R.I. Gen. Laws § 3-5-11.1\(c\)](#), and empowers the Department of Business Regulation to fine violators (including franchisors) and to revoke or suspend a transgressor's liquor license and/or franchise registration, [R.I. Gen. Laws § 3-5-11.1\(d\)](#).

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > The Judiciary > Case or Controversy > General Overview

Civil Procedure > Preliminary Considerations > Justiciability > General Overview

Civil Procedure > Appeals > Dismissal of Appeals > Involuntary Dismissals

Constitutional Law > The Judiciary > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

## **HN7** Justiciability, Standing

It is axiomatic that U.S. Const. art. III standing is a constitutional precondition to a federal court's power to adjudicate a case. When standing is put in issue, a reviewing court is warranted in confirming its existence before proceeding to tackle the merits of the case.

Civil Procedure > ... > Justiciability > Standing > General Overview

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Constitutional Law > ... > Case or Controversy > Standing > General Overview

Evidence > Burdens of Proof > General Overview

## [HN8](#) Justiciability, Standing

The burden of establishing standing lies with the party invoking federal jurisdiction. Accordingly, that party must show that (1) it personally has suffered some actual or threatened injury, (2) the injury fairly can be traced to the challenged conduct, and (3) a favorable decision likely will redress the injury.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > Third Party Standing

Constitutional Law > ... > Case or Controversy > Standing > General Overview

## [HN9](#) Justiciability, Standing

The requirement that an alleged injury be fairly traceable to the defendant's action does not mean that the defendant's action must be the final link in the chain of events leading up to the alleged harm. Nor does that requirement exclude injuries produced by coercive effect upon the action of someone else. Given these principles, the fact that the deleterious effect of a statute is indirect will not by itself defeat standing.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

## [HN10](#) Justiciability, Standing

To ground a claim of standing, harm must be actual or imminent rather than conjectural or speculative.

Civil Procedure > Remedies > Injunctions > Preliminary & Temporary Injunctions

Civil Procedure > ... > Injunctions > Grounds for Injunctions > General Overview

Civil Procedure > ... > Injunctions > Grounds for Injunctions > Public Interest

## [HN11](#) Injunctions, Preliminary & Temporary Injunctions

A district court must weigh four factors in determining whether to issue a preliminary injunction: (1) the likelihood of success on the merits; (2) the potential for irreparable harm to the movant if the injunction is denied; (3) the balance of relevant impositions, i.e., the hardship to the nonmovant if enjoined as contrasted with the hardship to the movant if no injunction issues; and (4) the effect (if any) of the court's ruling on the public interest. The sine qua non of this four-part inquiry is likelihood of success on the merits: if the moving party cannot demonstrate that he is likely to succeed in his quest, the remaining factors become matters of idle curiosity.

Civil Procedure > Appeals > Standards of Review > Abuse of Discretion

418 F.3d 36, \*36LAW2005 U.S. App. LEXIS 16718, \*\*1

Civil Procedure > Remedies > Injunctions > Preliminary & Temporary Injunctions

Civil Procedure > Appeals > Standards of Review > Clearly Erroneous Review

Civil Procedure > Appeals > Standards of Review > De Novo Review

#### **HN12** [down] **Standards of Review, Abuse of Discretion**

An appellate court reviews the grant or denial of a preliminary injunction for abuse of discretion. Under that rubric, findings of fact are reviewed for clear error and issues of law are reviewed de novo. Judgment calls and issues that demand the balancing of conflicting factors are reviewed deferentially. In the last analysis, then, the appellate court will set aside a district court's ruling on a preliminary injunction motion only if the court clearly erred in assessing the facts, misapprehended the applicable legal principles, or otherwise is shown to have abused its discretion.

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > Bill of Rights > State Application

#### **HN13** [down] **Fundamental Freedoms, Freedom of Speech**

The Free Speech Clause provides that Congress shall make no law abridging the freedom of speech. [U.S. Const. amend. I](#). By incorporation through the [Fourteenth Amendment](#), this prohibition applies to states and their political subdivisions.

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

#### **HN14** [down] **Freedom of Speech, Commercial Speech**

Some profit-directed speech, such as legal or medical advice, is entitled to constitutional protection.

Business & Corporate Law > Distributorships & Franchises > Disclosure & Registration > Enforcement of Franchise Requirements

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Governments > State & Territorial Governments > Licenses

#### **HN15** [down] **Disclosure & Registration, Enforcement of Franchise Requirements**

[R.I. Gen. Laws § 3-5-11\(b\)\(1\)](#) simply does not prohibit the communication of advice between a franchisor and the holders of Class A liquor licenses.

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

#### **HN16** [blue speech bubble icon] **Freedom of Speech, Commercial Speech**

The [First Amendment](#) does not guarantee that speech will be profitable to the speaker or desirable to its intended audience.

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

#### **HN17** [blue speech bubble icon] **Freedom of Speech, Commercial Speech**

A case in which the statute imposes no burden on the communication between the speaker and the intended audience but has the effect of decreasing the audience's demand for a particular kind of business advice, is distinguishable from cases dealing with a state's direct imposition of financial burdens on the dissemination of particular kinds of speech.

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

#### **HN18** [blue speech bubble icon] **Freedom of Speech, Commercial Speech**

The [First Amendment](#) does not safeguard against changes in commercial regulation that render previously profitable information valueless. The [First Amendment's](#) core concern is with the free transmission of a message or idea from speaker to listener, not with the speaker's ability to turn a profit or with the listener's ability to act upon the communication.

Constitutional Law > ... > Freedom of Speech > Commercial Speech > Advertising

Governments > State & Territorial Governments > Licenses

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

#### **HN19** [blue speech bubble icon] **Commercial Speech, Advertising**

Commercial speech, including truthful liquor advertising, is entitled to a measure of protection under the [First Amendment](#).

Business & Corporate Compliance > ... > Trademark Law > Conveyances > Licenses

Governments > State & Territorial Governments > Licenses

418 F.3d 36, \*36LAW2005 U.S. App. LEXIS 16718, \*\*1

Trademark Law > Special Marks > Trade Names > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

## **HN20** [💡] Conveyances, Licenses

The commercial speech doctrine protects the communication of truthful information to potential customers about a proposed commercial transaction. The provision of advertising and licensing services is not speech that proposes a commercial transaction and therefore does not constitute commercial speech.

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Expressive Conduct

Evidence > Burdens of Proof > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

## **HN21** [💡] Freedom of Speech, Expressive Conduct

It is the duty of the party seeking to engage in allegedly expressive conduct to demonstrate that the [First Amendment](#) applies to that conduct.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Standing

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > Third Party Standing

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > General Overview

## **HN22** [💡] Justiciability, Standing

A party ordinarily has no standing to assert the [First Amendment](#) rights of third parties. There is an isthmian exception that applies when some barrier or practical obstacle deters a third party from asserting its rights.

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Overbreadth & Vagueness of Legislation

Governments > Legislation > Overbreadth

Civil Procedure > Preliminary Considerations > Justiciability > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Civil Procedure > ... > Justiciability > Standing > Third Party Standing

Constitutional Law > ... > Case or Controversy > Standing > Third Party Standing

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Judicial & Legislative Restraints > Standing Governments > Legislation > General Overview

### **HN23** [blue icon] **Judicial & Legislative Restraints, Overbreadth & Vagueness of Legislation**

In some circumstances, out of concern that an overly broad statute might chill constitutionally protected speech, the United States Supreme Court has relaxed the prudential limitations on third-party standing to permit a litigant to pursue a facial challenge to such a statute on overbreadth grounds, even though the litigant's own conduct could be regulated validly by a more narrowly drawn statute. The overbreadth doctrine is inapplicable in the commercial speech context.

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Assembly

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

### **HN24** [blue icon] **Fundamental Freedoms, Freedom of Assembly**

Freedom of speech embraces the freedom to engage in association for the advancement of beliefs and ideas. This freedom of expressive association emerges from the insight that expressive rights explicitly guaranteed by the [First Amendment](#) could not be vigorously protected from interference by the state unless a correlative freedom to engage in group effort toward those ends were not also guaranteed. Because protection of the right to associate evolves from the [First Amendment's](#) guarantees of speech, assembly, petition, and free exercise, the scope of protection for association corresponds to the constitutional solicitude afforded to the mode of [First Amendment](#) expression in which a particular group seeks collectively to engage.

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

### **HN25** [blue icon] **Fundamental Freedoms, Freedom of Association**

In a free speech case, an association's expressive purpose may pertain to a wide array of ends, including economic ends, but the embedded associational right protects only collective speech and expressive conduct in pursuit of those ends; it does not cover concerted action that lacks an expressive purpose. So viewed, the right to expressive association does not confer a generalized freedom for individuals or entities collectively to engage in activity that is otherwise regulable when undertaken by a single individual or entity. The United States Supreme Court has tended to view the right of association as dependent on underlying individual rights of expression; there is no right of association in the abstract.

418 F.3d 36, \*36LAW2005 U.S. App. LEXIS 16718, \*\*1

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

## **HN26** [blue speech bubble icon] **Fundamental Freedoms, Freedom of Association**

Business entities have no *First Amendment* right to combine operations or coordinate market activities for the purpose of obtaining a greater market share for each participant. The fact that communication serves as the primary instrument of conducting business among separate enterprises does not alter this conclusion.

Constitutional Law > ... > Freedom of Speech > Free Press > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Scope

## **HN27** [blue speech bubble icon] **Freedom of Speech, Free Press**

Although courses of conduct are, in most instances, effectuated by speaking or writing, it has never been deemed an abridgment of freedom of speech or press to make a course of conduct illegal merely because the conduct was in part initiated, evidenced, or carried out by means of language. Indeed, such an expansive interpretation of the constitutional guaranties of speech and press would make it practically impossible ever to enforce laws against agreements in restraint of trade as well as many other agreements and conspiracies deemed injurious to society. The state does not lose its power to regulate commercial activity deemed harmful to the public whenever speech is a component of that activity.

Constitutional Law > Prohibition

Criminal Law & Procedure > ... > Alcohol Related Offenses > Distribution & Sale > Elements

Criminal Law & Procedure > Criminal Offenses > Alcohol Related Offenses > General Overview

Criminal Law & Procedure > ... > Alcohol Related Offenses > Distribution & Sale > General Overview

Criminal Law & Procedure > ... > Alcohol Related Offenses > Transportation > Elements

## **HN28** [blue speech bubble icon] **Constitutional Law, Prohibition**

U.S. Const. amend. XXI, § 2, prohibits the transportation or importation, for delivery or use, of intoxicating liquors into any state in violation of state law.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Governments > State & Territorial Governments > Licenses

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

## **HN29** [blue speech bubble icon] **Public Enforcement, State Civil Actions**

The constitutionality of the antitrust laws is not open to debate. Such laws, by definition, regulate the ways in which market players may pool their capabilities to acquire market power. While the state cannot regulate the right of speakers to band together to convey a common message in the marketplace of ideas, it most assuredly can exercise control over the efforts of market players to exploit the principle of strength in numbers in the marketplace of goods.

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > General Overview

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

Constitutional Law > ... > Fundamental Freedoms > Freedom of Speech > Political Speech

### **HN30** [blue icon] **Fundamental Freedoms, Freedom of Association**

The case law dealing with claimed exceptions to antitrust or commercial conspiracy laws on First Amendment associational grounds indicates that the state's right to enforce such laws against collusive market behavior must abate only in instances in which the joint activity constitutes an exercise of a core speech right.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom of Association

Constitutional Law > ... > Freedom of Speech > Commercial Speech > General Overview

### **HN31** [blue icon] **Public Enforcement, State Civil Actions**

In the absence of anything uniquely expressive about the concerted commercial activity, no First Amendment exception to the enforcement of an otherwise valid antitrust law is warranted.

Constitutional Law > Equal Protection > Nature & Scope of Protection

Evidence > Burdens of Proof > General Overview

Constitutional Law > Substantive Due Process > Scope

Evidence > Inferences & Presumptions > General Overview

### **HN32** [blue icon] **Equal Protection, Nature & Scope of Protection**

When economic legislation neither employs suspect classifications nor infringes on fundamental rights, the legislation need only survive rational basis scrutiny. Under that standard, an inquiring court must uphold the legislation as long as the means chosen by the legislature are rationally related to some legitimate government purpose. In conducting that analysis, the state's legislative choices bear a strong presumption of validity. A challenger can overcome this presumption only by demonstrating that there exists no fairly conceivable set of facts

that could ground a rational relationship between the challenged classification and the government's legitimate goals.

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Joseph S. Larisa, Jr., with whom Larisa Law and Consulting, LLC was on brief, for intervenor-appellee.

**Judges:** Before Selya, Circuit Judge, Hill, \* Senior Circuit Judge, and Lynch, Circuit Judge.

**Opinion by:** SELYA

## Opinion

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[\*41] **SELYA, Circuit Judge.** Rhode Island, like many states, regulates the intrastate channels through which alcoholic beverages may be manufactured, imported, and sold. One recently enacted piece of this regulatory mosaic prevents any franchisor or franchisee from holding a Class A retail liquor license. See [R.I. Gen. Laws § 3-5-11.1](#) [\*\*2]. Another piece, enacted at the same time, amended a related statute, which prohibits any "chain store organization" from holding such a license, *id.* [§ 3-5-11\(a\)](#), so that it explicitly [\*42] encompasses package stores that engage in certain coordinated business activities, see *id.* [§ 3-5-11\(b\)](#).

Plaintiff Wine & Spirits Retailers, Inc. (W & S), a franchisor of package stores, brought this action against the State seeking, *inter alia*, to enjoin the enforcement of those new enactments.<sup>1</sup> W & S premised its suit on the thesis that the two statutes, singly and in combination, violate (i) its [First Amendment](#) rights to speech and association and (ii) its [Fourteenth Amendment](#) right to equal protection.

[\*\*3] In this early chapter of the litigation, W & S appeals from the district court's denial of its motion for a preliminary injunction. Having weighed the considerations relevant to the preliminary injunction balance, we conclude that the district court did not abuse its discretion in determining that W & S failed to show a likelihood of success on the merits of its claims and, therefore, did not demonstrate an entitlement to preliminary injunctive relief.

### I. BACKGROUND

**HN1** [↑] Under Rhode Island law, any individual or entity engaged in the manufacture, sale, or importation of alcoholic beverages must hold a valid license issued by the Department of Business Regulation (DBR). See [R.I. Gen. Laws § 3-5-11](#). A Class A retail license entitles the holder to obtain alcoholic beverages from licensed wholesalers and to operate a retail package store, from which the beverages may be sold in sealed containers. See *id.* [§§ 3-7-1, 3-7-3](#). Since 1933, the State has prohibited chain store organizations from holding Class A liquor licenses. See 1933 R.I. Pub. Laws ch. 2013, § 6 (current version at [R.I. Gen. Laws § 3-5-11](#)). This enactment [\*\*4] gave the DBR full discretion to determine whether an entity fell into the "chain store" category. *Id.*

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\* Of the Eleventh Circuit, sitting by designation.

<sup>1</sup> Posturing this action as one brought by W & S against the State is a harmless oversimplification. In fact, W & S's principal, John Haronian, is also a plaintiff and Jeffrey J. Greer, in his official capacity as associate director of Rhode Island's Department of Business Regulation, is also a defendant. Because their presence is essentially superfluous, we opt for simplicity and proceed as if W & S and the State were the only parties.

The ingenuity of lawyers is nearly endless and, recently, franchised package stores began to crop up throughout Rhode Island. In an apparent effort to block this easy evasion of the chain store prohibition, [HN2](#)<sup>↑</sup> the Rhode Island General Assembly amended [section 3-5-11](#) to identify a set of licensee activities that would allow the DBR to find that an entity was in fact a chain store organization. The new statute, enacted July 8, 2004 and effective April 1, 2005, expanded the term "chain store organization" to encompass:

Any group of one or more holders of Class A liquor licenses who engage in one or more of the following practices with respect to the business conducted under such licenses, either directly or indirectly, or have any direct or indirect beneficial interest in the following practices:

- (i) Common, group, centralized or coordinated purchases of wholesale merchandise.
- (ii) Common billing or utilization of the services of the same person or the same entity in the management or operation of more than one liquor licensed business.

(iii) Participation in [\\*\\*5](#) a coordinated or common advertisement with one or more liquor licensed business in any advertising media.

(iv) Coordinated or common planning or implementation of marketing strategies.

[\[\\*43\]](#) (v) Participation in agreed upon or common pricing of products.

(vi) Any term or name identified as a chain or common entity.

[R.I. Gen. Laws § 3-5-11\(b\)\(1\)](#). [HN3](#)<sup>↑</sup> By its terms, this statute restricts a holder of a Class A liquor license from participating in many business activities that are typical of a franchise relationship.

[HN4](#)<sup>↑</sup> Simultaneous with the enactment of [section 3-5-11\(b\)](#), the General Assembly passed what is now [section 3-5-11.1](#). This provision has a similar but more direct effect: it explicitly excludes franchisees from holding Class A liquor licenses. The amended statute reads in pertinent part:

[HN5](#)<sup>↑</sup> To promote the effective and reasonable control and regulation of the Rhode Island alcoholic beverage industry and to help the consumer by protecting their choices and ensuring equitable pricing. Class A liquor licenses authorized by this title shall not be granted, issued, renewed or transferred to or for the use of any liquor franchisor or franchisee. [\\*\\*6](#) Class A liquor license holders are expressly prohibited from utilizing the provisions of the Franchise Investor [sic] Act, [[R.I. Gen. Laws](#)] [§ 19-28-1 et seq.](#)

*Id.* [HN6](#)<sup>↑</sup> [§ 3-5-11.1\(a\)](#). The latter statute also nullifies all franchise agreements involving the retail sale of alcoholic beverages, *id.* [§ 3-5-11.1\(b\)](#); stipulates that any franchisor or franchisee who is a party to such an agreement must terminate it within thirty days of the statute's effective date, *id.* [§ 3-5-11.1\(c\)](#); and empowers the DBR to fine violators (including franchisors) and to revoke or suspend a transgressor's liquor license and/or franchise registration, *id.* [§ 3-5-11.1\(d\)](#).

At the time these bills were passed, W & S had been operating for roughly seven years as a franchisor of independently owned Class A liquor retailers. It had a portfolio of eleven franchise agreements in Rhode Island, all of which were registered under the Franchise Investment Act, [R.I. Gen. Laws §§ 19-28.1-1 to 19-28.1-34](#). These franchisees conducted business under names owned by W & S (seven under the name "Douglas Wine & Spirits" and four under the name "People's [\\*\\*7](#) Liquor Warehouse").

In general, W & S's franchise agreements provided that, for an annual fee, royalties, a commitment to maintain certain quality standards, and a pledge to pay into a joint advertising and promotion fund, the franchisee would receive an exclusive franchise territory. The franchisee also would receive the right to use either the Douglas or People's trade name and other proprietary marks, and would be given access to a compendium of marketing, advertising, training, accounting, purchasing, and consulting services. Additionally, the franchise agreements authorized W & S to require the franchisees to carry certain products, to designate vendors for those items, and to dictate the layout of each retail store (including product placement).

In July of 2004 (when [sections 3-5-11\(b\)](#) and [3-5-11.1](#) were enacted), W & S was negotiating with two more potential Rhode Island franchisees. Recognizing the relevance of the new statutes to its operation, W & S wrote to

the DBR on August 12, 2004, asking whether it would be permissible to register those two new franchises prior to the statutes' effective date. The DBR responded on September 1, 2004, explaining that W & S would have [\*\*8] to submit applications in order for any new franchise registrations to be considered. The DBR's letter left no doubt that this would be an exercise in futility; the epistle declared the DBR's position to be "that as of April 1, 2005, all store franchise agreements as of that time will become null and void and it [thereafter] will be illegal for a [\*44] Class A package store to operate under a franchise agreement."

## II. TRAVEL OF THE CASE

With the death knell set to toll, W & S filed this action on September 29, 2004. Its complaint set forth eight statements of claim. On January 18, 2005, W & S moved to enjoin enforcement of the challenged provisions throughout the currency of the litigation. In the motion for preliminary injunctive relief, it relied on only three of its eight claims: (i) that [sections 3-5-11](#) and [3-5-11.1](#) prohibit it from engaging in expression protected by the [First Amendment](#); (ii) that the laws violate its [First Amendment](#) right to association; and (iii) that the laws violate the [Equal Protection Clause of the Fourteenth Amendment](#) by treating it differently from others who are similarly situated. The State opposed the motion. The United Independent Liquor Retailers [\*\*9] of Rhode Island (UILRRI), an association of Class A licensees that had lobbied for passage of the challenged laws, successfully moved to intervene as a party defendant and sided with the State.

Following a hearing, the district court denied the request for a preliminary injunction, principally on the ground that W & S had not demonstrated a likelihood of success on the merits. See [Wine & Spirits Retailers, Inc. v. Rhode Island, 364 F. Supp. 2d 172, 176-83 \(D.R.I. 2005\)](#). W & S filed a timely notice of appeal. See [Fed. R. App. P. 4\(a\); 28 U.S.C. § 1292\(a\)\(1\)](#). We granted expedited review.

In the meantime, the district court had granted an injunction pending appeal, see [Fed. R. Civ. P. 62\(c\)](#), to prevent the State "from enforcing [R.I. Gen. Laws § 3-5-11](#) to the extent that the enforcement action is based solely on a Class A licensee's use of a name similar to or the same as that of another licensee." [Wine & Spirits Retailers, Inc. v. Rhode Island](#), No. 04-418 (D.R.I. April 29, 2005) (unpublished order). At W & S's request, we [\*\*10] extended that injunction to the date of the issuance of our mandate but, like the lower court, denied other requested relief. See [Wine & Spirits Retailers, Inc. v. Rhode Island](#), No. 05-1549 (1st Cir. May 23, 2005) (unpublished order); see also [Fed. R. App. P. 8\(a\)\(2\)](#). We heard oral argument on June 7, 2005 and took the matter under advisement. We now affirm.

## III. JUSTICIABILITY

W & S maintains that the district court wrongfully denied its request for a preliminary injunction against the enforcement of [sections 3-5-11](#) and [3-5-11.1](#). Both the State and UILRRI assert that W & S lacks Article III standing to challenge those laws.

**HN7** It is axiomatic that Article III standing is a constitutional precondition to a federal court's power to adjudicate a case. [Osediacz v. City of Cranston, 414 F.3d 136, 140, 2005 U.S. App. LEXIS 13382 \(1st Cir. 2005\)](#) [No. 04-2673, slip op. at 2]; [R.I. Ass'n of Realtors, Inc. v. Whitehouse, 199 F.3d 26, 30 \(1st Cir. 1999\)](#). When standing is put in issue, a reviewing court is warranted in confirming its existence before proceeding to tackle the merits of the case. We do so here.

**HN8** The [\*\*11] burden of establishing standing lies with the party invoking federal jurisdiction. [Osediacz, F.3d at , 2005 U.S. App. LEXIS 13382 \[slip op. at 3\]](#). Accordingly, W & S "must show that (1) it personally has suffered some actual or threatened injury, (2) the injury fairly can be traced to the challenged conduct, and (3) a favorable decision likely will redress [the injury]." [R.I. Ass'n of Realtors, 199 F.3d at 30](#).

W & S easily satisfies these requirements with respect to [section 3-5-11.1](#). After all, it alleges that [section 3-5-11.1](#)'s [\*45] prohibition on liquor franchises nullifies its franchise agreements with no fewer than eleven franchisees and subjects it, as a franchisor, to monetary penalties should it attempt to maintain its franchise relationships. See [R.I. Gen. Laws § 3-5-11.1\(b\), \(d\)](#). Those imminent consequences satisfy the requirement of an injury in fact. That injury, in turn, is fairly traceable to the statute and redressable in a federal court proceeding. Consequently, W & S has standing to press its constitutional claims insofar as those claims implicate [section 3-5-11.1](#).

With respect to [section 3-5-11](#), the defendants' cardinal [\*12] contention is that W & S cannot meet the standing requirement because it does not itself hold a Class A liquor license and, therefore, is not subject to any enforcement action or penalty under the statute's terms. This contention has a patina of plausibility. [Section 3-5-11](#) does not carry any direct penalties applicable to franchisors but, rather, applies directly to holders of Class A liquor licenses. Thus, it cannot be enforced against a franchisor, like W & S, which does not itself possess such a license.

In the end, however, this statutory configuration does not undermine the allegation that W & S has suffered an injury that is fairly traceable to the statute. That allegation draws its essence from W & S's claim that [section 3-5-11](#), by restricting the holders of Class A liquor licenses from engaging in certain business activities vital to franchise arrangements, infringes on a franchisor's [First Amendment](#) rights of speech and association and thereby causes W & S economic harm. No more is exigible to clear the standing hurdle.

**HN9** [↑] The requirement that an alleged injury be fairly traceable to the defendant's action does not mean that the defendant's action must be the final link in [\*13] the chain of events leading up to the alleged harm. See [Bennett v. Spear, 520 U.S. 154, 168-69, 137 L. Ed. 2d 281, 117 S. Ct. 1154 \(1997\)](#). Nor does that requirement exclude injuries produced by "coercive effect upon the action of someone else." *Id. at 169*. Given these principles, the fact that the deleterious effect of a statute is indirect will not by itself defeat standing. See [Becker v. FEC, 230 F.3d 381, 387 \(1st Cir. 2000\)](#); see also [Eulitt v. Me. Dep't of Educ., 386 F.3d 344, 353 \(1st Cir. 2004\)](#) (holding that parents had sufficiently alleged an Article III injury even though "it [was] the educational institution, not the parents," that was denied access to certain tuition payments under the challenged statute); [Houlton Citizens' Coalition v. Town of Houlton, 175 F.3d 178, 183 \(1st Cir. 1999\)](#) (finding that trash hauler had standing to assert a constitutional challenge to an ordinance mandating residents' use of a town-designated competitor); [Wash. Legal Found. v. Mass. Bar Found., 993 F.2d 962, 972 \(1st Cir. 1993\)](#) (finding that client had standing based on alleged injury [\*14] to her constitutional rights that was fairly traceable to a rule, enforceable only against attorneys, that required them to place client funds in a pooled interest-bearing account).

These precedents are determinative here. [Section 3-5-11\(b\)\(1\)](#) has an obviously coercive effect on W & S's franchisees; under its terms, those franchisees either must desist from engaging in certain collective business activities with W & S or forfeit their Class A liquor licenses. Either way, W & S's business relationship with the franchisees, which it claims to be constitutionally protected, is damaged.<sup>2</sup> [\*46] Consequently, the economic harm that W & S alleges is fairly traceable to the statute (and, thus, to the State).

[\*\*15] To cinch matters, the threat to the franchisees is both actual and imminent. It is undisputed that the DBR has taken preliminary steps to enforce the statute against non-compliant holders of Class A liquor licenses and has warned that it will undertake such enforcement from and after the statute's effective date. That is enough to show that the threatened harm is imminent. See, e.g., [Aroostook Band of Micmacs v. Ryan, 404 F.3d 48, 65-66 \(1st Cir. 2005\)](#); [Montalvo-Huertas v. Rivera-Cruz, 885 F.2d 971, 976 \(1st Cir. 1989\)](#); see also [Berner v. Delahanty, 129 F.3d 20, 24 \(1st Cir. 1997\)](#) (noting that **HN10** [↑] to ground a claim of standing, harm must be actual or imminent rather than conjectural or speculative). Granting the requested declaratory and injunctive relief plainly would palliate this threatened harm.

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<sup>2</sup> There is no suggestion here that any of W & S's franchisees plan to terminate the franchise relationships for reasons unrelated to the threatened enforcement of the new statutory provisions. Therefore, this is not a case in which "the injury complained of is 'the result [of] the *independent* action of some third party not before the court.'" [Bennett, 520 U.S. at 169](#) (alterations and emphasis in original) (quoting [Lujan v. Defenders of Wildlife, 504 U.S. 555, 560-61, 119 L. Ed. 2d 351, 112 S. Ct. 2130 \(1992\)](#)).

To say more on this point would be to paint the lily. For the reasons elucidated above, we conclude, without serious question, that W & S has alleged an injury fairly traceable to each of the challenged statutes and redressable by the federal courts. Accordingly, it has standing to pursue the claims that it asserts.

#### [\*\*16] IV. THE PRELIMINARY INJUNCTION STANDARD

We turn next to the legal standards that apply to the grant or denial of preliminary injunctions. [HN11](#) A district court must weigh four factors in determining whether to issue a preliminary injunction:

(1) the likelihood of success on the merits; (2) the potential for irreparable harm [to the movant] if the injunction is denied; (3) the balance of relevant impositions, i.e., the hardship to the nonmovant if enjoined as contrasted with the hardship to the movant if no injunction issues; and (4) the effect (if any) of the court's ruling on the public interest.

[Bl\(a\)ck Tea Soc'y v. City of Boston](#), 378 F.3d 8, 11 (1st Cir. 2004) (citing [Ross-Simons of Warwick, Inc. v. Baccarat, Inc.](#), 102 F.3d 12, 15 (1st Cir. 1996)). "The sine qua non of this four-part inquiry is likelihood of success on the merits: if the moving party cannot demonstrate that he is likely to succeed in his quest, the remaining factors become matters of idle curiosity." [New Comm Wireless Servs., Inc. v. SprintCom, Inc.](#), 287 F.3d 1, 9 (1st Cir. 2002).

[HN12](#) This court reviews the grant or denial of a preliminary [\[\\*\\*17\]](#) injunction for abuse of discretion. [Bl\(a\)ck Tea Soc'y](#), 378 F.3d at 11; [Ross-Simons](#), 102 F.3d at 16. Under that rubric, findings of fact are reviewed for clear error and issues of law are reviewed de novo. [Air Line Pilots Ass'n, Int'l. v. Guilford Transp. Indus., Inc.](#), 399 F.3d 89, 95 (1st Cir. 2005); [New Comm Wireless Servs.](#), 287 F.3d at 9. Judgment calls and issues that demand the balancing of conflicting factors are reviewed deferentially. [Bl\(a\)ck Tea Soc'y](#), 378 F.3d at 11. In the last analysis, then, we will set aside a district court's ruling on a preliminary injunction motion only if the court clearly erred in assessing the facts, misapprehended the applicable legal principles, or otherwise is shown to have abused its discretion. [McGuire v. Reilly](#), 260 F.3d 36, 42 (1st Cir. 2001).

#### V. THE [FIRST AMENDMENT](#) CHALLENGE

W & S asserts that [sections 3-5-11](#) and [3-5-11.1](#) impair its [First Amendment](#) [\[\\*47\]](#) rights to free speech and expressive association by (i) constricting its ability to peddle marketing and management advice, advertising services, and trade name protection to [\[\\*\\*18\]](#) holders of Class A liquor licenses and (ii) making it unlawful to engage in a franchise relationship with those license holders. We consider these assertions separately.

##### A. *The Free Speech Claim.*

[HN13](#) The Free Speech Clause provides that "Congress shall make no law . . . abridging the freedom of speech." [U.S. Const. amend. I](#). By incorporation through the [Fourteenth Amendment](#), this prohibition applies to states and their political subdivisions. [Knights of Columbus v. Town of Lexington](#), 272 F.3d 25, 30 (1st Cir. 2001).

In this case, W & S directs its free speech claim to [section 3-5-11\(b\)\(1\)](#). It asseverates that various provisions of that section adversely affect its ability to sell business advice ([sub-paragraphs \(i\), \(ii\), \(iv\),](#) and [\(v\)](#)), advertising design and placement services ([sub-paragraph \(iii\)](#)), and trade name rights ([sub-paragraph \(vi\)](#)) to the holders of Class A liquor licenses. Thus, the law unduly infringes on W & S's right to communicate with the license holders. We examine this asseveration.

As an initial matter, we assess each of the activities identified by W & S in light of its allegation that [section 3-5-11\(b\)\(1\)](#) operates to prohibit or [\[\\*\\*19\]](#) unduly curtail the activity. We then consider the contention that the activity constitutes protected speech or expressive conduct.

**1. Business Advice.** W & S maintains that the provision of business advice for a fee is speech protected by the [First Amendment](#). The advice in question takes the form of a marketing and management plan (including

recommendations about purchasing and pricing). The Supreme Court has recognized that [HN14](#)<sup>1</sup> some profit-directed speech, such as legal or medical advice, is entitled to constitutional protection. See [Board of Trustees v. Fox, 492 U.S. 469, 482, 106 L. Ed. 2d 388, 109 S. Ct. 3028 \(1989\)](#). Here, however, we need not determine whether and to what extent the business advice offered by W & S to Class A license holders fits within this taxonomy. The plain, hard fact is that [HN15](#)<sup>1</sup> [section 3-5-11\(b\)\(1\)](#) simply does not prohibit the communication of advice between a franchisor and the holders of Class A liquor licenses.

To begin, nothing in the statute prevents W & S from selling or otherwise communicating its recipe for the operation of a successful package store to a Class A license holder. Nor does the statute forbid a license holder [\[\\*\\*20\]](#) from purchasing or receiving that information. While the statute prevents certain conduct -- the implementation of W & S's business model -- that prohibition imposes no legally cognizable burden on the exchange of information between the speaker (W & S) and the invited audience (the holders of Class A liquor licenses).

Stripped of rhetorical flourishes, W & S's real complaint is that [section 3-5-11\(b\)\(1\)](#) will have the incidental effect of suppressing or eliminating the market demand for the particular type of business advice that W & S offers (that is, marketing and management strategies whose successful implementation requires the coordination of business activities with those of other market players). That circumstance does not suffice to hoist the red flag of constitutional breach: [HN16](#)<sup>1</sup> the [First Amendment](#) does not guarantee that speech will be profitable to the speaker<sup>3</sup> or desirable [\[\\*48\]](#) to its intended audience. See [AMSAT Cable Ltd. v. Cablevision of Conn. Ltd. P'ship, 6 F.3d 867, 871 \(2d Cir. 1993\)](#); see also [Young v. Am. Mini Theatres, Inc., 427 U.S. 50, 78, 49 L. Ed. 2d 310, 96 S. Ct. 2440 \(1976\)](#) (Powell, J., concurring) (noting that "the inquiry for [First](#) [\[\\*\\*21\]](#) [Amendment](#) purposes is not concerned with economic impact; rather, it looks only to the effect of [the challenged] ordinance upon freedom of expression").

[\[\\*\\*22\]](#) By the same token, [HN18](#)<sup>1</sup> the [First Amendment](#) does not safeguard against changes in commercial regulation that render previously profitable information valueless. That is a commonplace occurrence in today's fast-moving world (an example would be the closing of a tax loophole that renders a previously profitable tax shelter worthless). The [First Amendment's](#) core concern is with the free transmission of a message or idea from speaker to listener, not with the speaker's ability to turn a profit or with the listener's ability to act upon the communication.

That ends this aspect of the matter. Because [section 3-5-11\(b\)\(1\)](#), on its face, imposes no burden on the ability of a business advisor to relay marketing and management advice to holders of Class A liquor licenses, W & S is unlikely to succeed on this facet of its [First Amendment](#) claim.

**2. Advertising Services and Trade Names.** W & S suggests that [section 3-5-11\(b\)\(1\)\(iii\)](#)'s proscription on the ability of the holders of Class A liquor licenses to participate jointly "in a coordinated or common advertisement" and [section 3-5-11\(b\)\(1\)\(vi\)](#)'s prohibition on a license holder's use of "any term or name identified as a chain or common [\[\\*\\*23\]](#) entity" constitute undue restraints on commercial speech. We take no view on that suggestion for two reasons: first, it would require us to examine the commercial speech rights of Class A licensees -- none of whom are before this court -- and second, W & S has not established any basis upon which it can assert those rights on behalf of third parties (including its franchisees). The only question properly before us is narrower: whether the joint advertising and common naming restrictions infringe on any speech or expressive conduct of W & S that is protected by the [First Amendment](#). We answer that question in the negative.

<sup>3</sup> [HN17](#)<sup>1</sup> A case like this one, in which the statute imposes no burden on the communication between the speaker and the intended audience but has the effect of decreasing the audience's demand for a particular kind of business advice, is distinguishable from cases dealing with the State's direct imposition of financial burdens on the dissemination of particular kinds of speech. See, e.g., [Simon & Schuster, Inc. v. Members of N.Y. State Crime Victims Bd., 502 U.S. 105, 115-18, 123, 116 L. Ed. 2d 476, 112 S. Ct. 501 \(1991\)](#) (invalidating law requiring publisher to place convicted criminals' income derived from publications about their crimes into escrow for victim compensation); [Minneapolis Star & Tribune Co. v. Minn. Comm'r of Rev., 460 U.S. 575, 581-83, 75 L. Ed. 2d 295, 103 S. Ct. 1365 \(1983\)](#) (finding that tax on paper and ink products consumed in newspaper production imposed an unconstitutional burden on freedom of the press). In such cases, the government, not waning market demand, was directly responsible for the financial disincentive to speak.

Let us be perfectly clear. We agree with W & S's underlying premise that [HN19](#) [↑] commercial speech, including truthful liquor advertising, is entitled to a measure of protection under the [\*First Amendment\*](#). See [\*44 Liquormart, Inc. v. Rhode Island\*, 517 U.S. 484, 501, 516, 134 L. Ed. 2d 711, 116 S. Ct. 1495 \(1996\)](#); [\*Cent. Hudson Gas & Elec. Corp. v. Pub. Serv. Comm'n\*, 447 U.S. 557, 566, 65 L. Ed. 2d 341, 100 S. Ct. 2343 \(1980\)](#); [\*Va. State Bd. of Pharmacy v. Va. Citizens Consumer Council, Inc.\*, 425 U.S. 748, 770, 48 L. Ed. 2d 346, 96 S. Ct. 1817 \[\\*491\] \(1976\)](#). We nonetheless [\*\*24] reject W & S's suggestion because, in performing its role in the activities in question, it does not engage in commercial speech.

The activities that W & S claims to be protected as commercial speech are its provision of advertising services, including designing advertisements, arranging for their placement in various media, and licensing the common use of trade names that, according to W & S, have become synonymous with quality and value. See Appellants' Br. at 5, 8; see also [\*Wine & Spirits\*, 364 F. Supp. 2d at 177](#). [HN20](#) [↑] The commercial speech doctrine protects the communication of truthful information to potential customers about a proposed commercial transaction. See [\*Fox\*, 492 U.S. at 482](#); [\*Cent. Hudson\*, 447 U.S. at 561-63](#). W & S's assertions do not amount to a claim that the joint advertising and common naming restrictions impede its right to communicate with its potential customers, rather, the claim is that those restrictions interfere with a right to provide certain services. The provision of advertising and licensing services is not speech that proposes a commercial transaction and therefore does not constitute commercial speech. [\*\*25] See [\*Fox\* 492 U.S. at 482](#) (distinguishing between the proposal of a commercial transaction, "which is what defines commercial speech," and the provision of certain services for a profit, which is not commercial speech).

Nor do these activities -- W & S's creation of advertisements, assistance in their placement, and facilitation of the use of its trade names by franchisees -- fall into the broader category of expressive activity in which conduct itself can be said to convey a particularized message and, thus, be entitled to protection as symbolic speech. See [\*United States v. O'Brien\*, 391 U.S. 367, 376-77, 20 L. Ed. 2d 672, 88 S. Ct. 1673 \(1968\)](#); see generally [\*Hurley v. Irish-Am. Gay, Lesbian & Bisexual Group\*, 515 U.S. 557, 569-70, 132 L. Ed. 2d 487, 115 S. Ct. 2338 \(1995\)](#) (discussing instances in which the Supreme Court has found conduct to be inherently communicative). [HN21](#) [↑] It is the duty of the party seeking to engage in allegedly expressive conduct to demonstrate that the [\*First Amendment\*](#) applies to that conduct. [\*Clark v. Cmty. for Creative Non-Violence\*, 468 U.S. 288, 293 n.5, 82 L. Ed. 2d 221, 104 S. Ct. 3065 \(1984\)](#). W & S has offered no plausible argument [\*\*26] as to why the provision of advertising services is an inherently expressive activity.

Of course, W & S also complains that the advertising and common naming restrictions infringe on the franchisees' rights jointly to propose retail liquor sales through newspaper advertisements and the like. Though loudly bruted, that complaint lacks force because W & S has not established standing to pursue it.

[HN22](#) [↑] A party ordinarily has no standing to assert the [\*First Amendment\*](#) rights of third parties. See [\*Eulitt\*, 386 F.3d at 351](#). While there is an isthmian exception that applies when some barrier or practical obstacle deters a third party from asserting its rights, see, e.g., [\*Powers v. Ohio\*, 499 U.S. 400, 414-15, 113 L. Ed. 2d 411, 111 S. Ct. 1364 \(1991\)](#) (allowing criminal defendant to assert rights of jurors because they lack financial incentive to undertake the burden of litigation), nothing in the record indicates that W & S's franchisees are unable or unlikely to protect their own rights.

[HN23](#) [↑] In some circumstances, out of concern that an overly broad statute might chill constitutionally protected speech, the Supreme Court has relaxed the prudential limitations on third-party [\*\*27] standing to permit a litigant to pursue a facial challenge to such a statute on overbreadth grounds, [\*50] even though the litigant's own conduct could be regulated validly by a more narrowly drawn statute. [\*Broadrick v. Oklahoma\*, 413 U.S. 601, 612, 37 L. Ed. 2d 830, 93 S. Ct. 2908 \(1973\)](#). Here, however, any assertion that the advertising and common naming provisions substantially overreach would fail because the overbreadth doctrine is inapplicable in the commercial speech context. See, e.g., [\*Vill. of Hoffman Estates v. Flipside, Hoffman Estates, Inc.\*, 455 U.S. 489, 496-97, 71 L. Ed. 2d 362, 102 S. Ct. 1186 \(1982\)](#); [\*Bates v. State Bar of Ariz.\*, 433 U.S. 350, 380-81, 53 L. Ed. 2d 810, 97 S. Ct. 2691 \(1977\)](#).

To recapitulate, W & S has not laid any groundwork sufficient to establish third-party standing, so it cannot assert the commercial speech rights of Class A license holders. W & S's spavined attempt to assert a facial challenge affords no safety net for this claim. Accordingly, we endorse the district court's conclusion that W & S's free speech claim has little chance of succeeding on the merits.

#### **B. The Freedom of Association Claim.**

W & S strives to persuade [\*\*28] us that the challenged statutes, by directly and indirectly prohibiting the holders of Class A liquor licenses from engaging in franchise relationships, impinge on its [First Amendment](#) right to associate with its franchisees for the purposes of joint advertising and development of common management and marketing strategies. We are not convinced.

The Supreme Court long has recognized that [HN24](#)[] freedom of speech embraces the "freedom to engage in association for the advancement of beliefs and ideas." [NAACP v. Alabama, 357 U.S. 449, 460, 2 L. Ed. 2d 1488, 78 S. Ct. 1163 \(1958\)](#). This freedom of expressive association emerges from the insight that expressive rights explicitly guaranteed by the [First Amendment](#) "could not be vigorously protected from interference by the State unless a correlative freedom to engage in group effort toward those ends were not also guaranteed." [Roberts v. United States Jaycees, 468 U.S. 609, 622, 82 L. Ed. 2d 462, 104 S. Ct. 3244 \(1984\)](#). Because protection of the right to associate evolves from the [First Amendment's](#) guarantees of speech, assembly, petition, and free exercise, the scope of protection for association corresponds to the constitutional solicitude afforded [\*\*29] to the mode of [First Amendment](#) expression in which a particular group seeks collectively to engage. See *id.*

It follows logically that, [HN25](#)[] in a free speech case, an association's expressive purpose may pertain to a wide array of ends (including economic ends), see *id.*, but the embedded associational right protects only collective speech and expressive conduct in pursuit of those ends; it does not cover concerted action that lacks an expressive purpose, see [City of Dallas v. Stanglin, 490 U.S. 19, 24-25, 104 L. Ed. 2d 18, 109 S. Ct. 1591 \(1989\)](#). So viewed, the right to expressive association does not confer a generalized freedom for individuals or entities collectively to engage in activity that is otherwise regulable when undertaken by a single individual or entity. See *id.* As one treatise has noted, "the Court has tended to view the right of association as dependent on underlying individual rights of expression; there is no right of association in the abstract." Kathleen M. Sullivan & Gerald Gunther, Constitutional Law 1337 (14th ed. 2001). Thus, W & S must demonstrate that [sections 3-5-11](#) and [3-5-11.1](#) unduly curtail its associational right to engage in activities protected [\*\*30] by the [First Amendment](#). Elsewise, it cannot prevail on its associational claim.

We already have explained why [section 3-5-11\(b\)\(1\)](#) does not violate any of W & [\*\*51] S's speech rights. See *supra* Part V(A). The question, then, reduces to whether [section 3-5-11.1](#) may be said to work such a violation. To this end, W & S labors to characterize its concerted business activities as speech or expressive conduct protected by the [First Amendment](#). That effort fails.

[HN26](#)[] Business entities have no [First Amendment](#) right to combine operations or coordinate market activities for the purpose of obtaining a greater market share for each participant. The fact that communication serves as the primary instrument of conducting business among separate enterprises does not alter this conclusion. The Supreme Court elaborated on this point more than half a century ago in [Giboney v. Empire Storage & Ice Co., 336 U.S. 490, 93 L. Ed. 834, 69 S. Ct. 684 \(1949\)](#).

The *Giboney* Court acknowledged that, [HN27](#)[] although courses of conduct are, in most instances, effectuated by speaking or writing, "it has never been deemed an abridgment of freedom of speech or press to make a course of conduct illegal merely because the [\*\*31] conduct was in part initiated, evidenced, or carried out by means of language." *Id. at 502*. Indeed, "such an expansive interpretation of the constitutional guarantees of speech and press would make it practically impossible ever to enforce laws against agreements in restraint of trade as well as many other agreements and conspiracies deemed injurious to society." *Id.*; see also [Calif. Motor Transp. Co. v. Trucking Unlimited, 404 U.S. 508, 513-15, 30 L. Ed. 2d 642, 92 S. Ct. 609 \(1972\)](#) (explaining that while communication is an integral part of joint conduct, that fact cannot be used as a pretext for obtaining immunity from

laws prohibiting anticompetitive commercial activities). After all, the Court has made clear that "the State does not lose its power to regulate commercial activity deemed harmful to the public whenever speech is a component of that activity." *Ohrlik v. Ohio State Bar Ass'n*, 436 U.S. 447, 456, 56 L. Ed. 2d 444, 98 S. Ct. 1912 (1978) (citing "the exchange of price and production information among competitors" as an example of "communications that are regulated without offending the *First Amendment*").

Against this backdrop, we turn [\*\*32] to the case at hand. In enacting [section 3-5-11.1](#), Rhode Island exercised its police power, including its power under the [Twenty-First Amendment](#),<sup>4</sup> to regulate commercial transactions involving liquor and the organizational structure of the market in which such transactions take place. Seen in this light, the statute is tantamount to an **antitrust law** -- a category of regulation that recognizes the authority of the State to adjust the distribution of market power among commercial entities so as to prevent conditions that are, in its reasonably held view, harmful to healthy competition and free trade.

It is black letter law that [HN29](#)[] "the constitutionality of the antitrust laws is not open to debate." *Calif. Motor Transp.*, 404 U.S. at 515. Such laws, by definition, regulate the ways in which [\*\*33] market players may pool their capabilities to acquire market power. While the State cannot regulate the right of speakers to band together to convey a common message in the marketplace of ideas, it most assuredly can exercise control over the efforts of market players to exploit the principle of strength in numbers in the [\*52] marketplace of goods. See [United States Jaycees](#), 468 U.S. at 638 (O'Connor, J., concurring) (positing that "there is only minimal constitutional protection of the freedom of *commercial* association," *id. at 634*, and that, in all events, "no *First Amendment* interest stands in the way of a State's rational regulation of economic transactions by or within a commercial association"); Kathleen M. Sullivan, *Free Speech and Unfree Markets*, 42 U.C.L.A. L. Rev. 949, 950 (1995) (observing that, in the modern constitutional order, legislatures are free to pass laws "that override private economic arrangements on allocative grounds -- such as correcting for collective action problems, externalities, information asymmetries, or monopolies - - or for reasons of redistribution or paternalism").

[HN30](#)[] The case law dealing with claimed exceptions to antitrust [\*\*34] or commercial conspiracy laws on [First Amendment](#) associational grounds indicates that the State's right to enforce such laws against collusive market behavior must abate only in instances in which the joint activity constitutes an exercise of a core speech right. In *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 5 L. Ed. 2d 464, 81 S. Ct. 523 (1961), the Supreme Court recognized that commercial actors' concerted petitioning for legislative change was a form of political expression protected by the [First Amendment](#) and, therefore, exempt from certain applications of the antitrust laws. *Id. at 136-38*. In *NAACP v. Claiborne Hardware Co.*, 458 U.S. 886, 73 L. Ed. 2d 1215, 102 S. Ct. 3409 (1982), where black citizens had banded together to boycott white merchants as a means of protesting discriminatory practices, the Supreme Court held that the merchants could not premise liability for state antitrust violations and common law conspiracy on the boycotters' collective exercise of [First Amendment](#) rights. See *id. at 890-92, 915, 933*. Finding that the boycott involved the exercise of core [First Amendment](#) rights (speech, [\*\*35] petition, and assembly), the Court ruled that the State's right "to regulate economic activity could not justify a complete prohibition against a nonviolent, politically motivated boycott designed to force governmental and economic change and to effectuate rights guaranteed by the Constitution." *Id. at 914*. Several other cases in that lineage also turned on the fact that the concerted activity implicated exceptions to the antitrust laws designed to protect core speech rights. See, e.g., *Pro'l Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc.*, 508 U.S. 49, 56-60, 123 L. Ed. 2d 611, 113 S. Ct. 1920 (1993) (explaining that antitrust liability cannot be imposed upon entities that collectively pursue objectively reasonable litigation, even when an anticompetitive intent motivates the suit); *United Mine Workers of Am. v. Pennington*, 381 U.S. 657, 669-70, 14 L. Ed. 2d 626, 85 S. Ct. 1585 (1965) (decreeing that antitrust laws cannot be interpreted to prohibit joint efforts to influence public officials through otherwise legal methods).

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<sup>4</sup> In pertinent part, [HN28](#)[] that amendment prohibits "the transportation or importation . . . for delivery or use . . . of intoxicating liquors [into any state]" in violation of state law. U.S. Const. amend. XXI, § 2.

These cases must be contrasted with cases such as *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 107 L. Ed. 2d 851, 110 S. Ct. 768 (1990), <sup>\*\*36</sup> in which the Court upheld the imposition of an injunction under the *Sherman Act* against a cadre of court-appointed lawyers that enjoined their concerted refusal to accept further case assignments pending a requested fee increase. See *id. at 426-36*. The Court explained that "the undenied objective of [the] boycott was an economic advantage for those who agreed to participate," *id. at 426*, and that the lawyers' joint activity was aimed at "profiting financially from a <sup>\*53</sup> lessening of competition in the boycotted market," *id. at 427* (internal quotation marks omitted). In those circumstances, the Court refused to accept the lawyers' claim that the law, as applied, violated their right to associate for expressive purposes because to do so would be to "exaggerate[] the significance of the expressive component in the [lawyers'] boycott." *Id. at 430*. **HN31**<sup>↑</sup> In the absence of anything uniquely expressive about the concerted commercial activity, no *First Amendment* exception to the enforcement of an otherwise valid *antitrust law* was warranted. *Id. at 431* (noting that "the most blatant, naked price-fixing agreement <sup>\*\*37</sup> is a product of communication, but that is surely not a reason for viewing it with special solicitude"); accord *National Soc. of Professional Engineers v. United States*, 435 U.S. 679, 697, 55 L. Ed. 2d 637, 98 S. Ct. 1355 (1978) (upholding, against a *First Amendment* challenge, an antitrust injunction that prohibited a professional society "from adopting any official opinion, policy statement, or guideline stating or implying that competitive bidding is unethical").

Here, it is nose-on-the-face plain that W & S's commercial conduct exhibits nothing that even the most vivid imagination might deem uniquely expressive. Certainly, the mere fact that the joint activities that define the business relationship between the franchisor and its franchisees have some communicative component cannot, in and of itself, establish an entitlement to the prophylaxis of the *First Amendment*. See *Superior Court Trial Lawyers*, 493 U.S. *at 430*. Consequently, that conduct does not warrant overriding the State's historic right to regulate market forces in the retail liquor industry.<sup>5</sup>

<sup>\*\*38</sup> In sum, W & S has not established that the neoteric laws prohibiting the holders of Class A liquor licenses from conducting joint business activities infringe upon any right to advance its beliefs or ideas by engaging in activities protected by the *First Amendment*. Accordingly, there is scant reason to believe that W & S can succeed on the merits of its freedom of expressive association claim.

## VI. THE EQUAL PROTECTION CLAIM

As a last resort, W & S mounts an equal protection challenge to *sections 3-5-11* and *3-5-11.1*. Its complaint is that these statutes apply to package stores but not to other entities licensed to sell alcoholic beverages at retail (such as restaurants and bars). Its contrived attempt to tease an equal protection violation out of this imperfect analogy is unpersuasive.

**HN32**<sup>↑</sup> When economic legislation neither employs suspect classifications nor infringes on fundamental rights, the legislation need only survive rational basis scrutiny. *Hodel v. Indiana*, 452 U.S. 314, 331, 69 L. Ed. 2d 40, 101 S. Ct. 2376 (1981). Under that standard, an inquiring court must uphold the legislation as long as the means chosen by the legislature are rationally related to some <sup>\*\*39</sup> legitimate government purpose. *Id.* In conducting that analysis, the State's legislative choices "bear[] a strong presumption of validity." *Kittery Motorcycle, Inc. v. Rowe*, 320 F.3d 42, 47 (1st Cir. 2003) (internal quotation marks omitted). A challenger can overcome this presumption only by "demonstrating <sup>\*54</sup> that there exists no fairly conceivable set of facts that could ground a rational relationship between the challenged classification and the government's legitimate goals." *Eulitt*, 386 F.3d *at 356*.

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<sup>5</sup> The conclusion that otherwise valid regulation of commercial interactions between business entities does not offend the *First Amendment* merely because such interactions have a communicative component would apply with equal force to our analysis in Part V(A)(1), had we found that the relevant sub-paragraphs of *section 3-5-11(b)(1)* did in fact impede communications between W & S and the holders of Class A liquor licenses.

These rules are dispositive here. The legislation at issue is economic in nature. It neither utilizes suspect classifications nor trenches upon fundamental rights.<sup>6</sup> Its purpose, as stated by the Rhode Island General Assembly, is to protect consumer choice and ensure the equitable pricing of retail liquor products. See [R.I. Gen. Laws § 3-5-11.1\(a\)](#). W & S has not explained why, given the unexceptionable goal of maintaining a competitive retail liquor industry, it is irrational for Rhode Island to enact measures aimed at preventing anticompetitive practices by ensuring that holders of Class A liquor licenses operate [\\*\\*40](#) independently. By like token, W & S has wholly failed to show that restaurants and bars (which are licensed to sell alcoholic beverages only for consumption on their licensed premises) are similarly situated entities vis-a-vis package stores (which are licensed to sell alcoholic beverages only in sealed containers and for off-premises consumption).<sup>7</sup> Finally, it has failed to support its contention that Rhode Island's decision to devise a special regulatory scheme for the retail liquor market is arbitrary; for example, it has not negated the possibility that healthy competition already exists with respect to other sectors of the liquor industry (thus rendering regulation unnecessary).

[\\*\\*41](#) The short of it is that W & S has not demonstrated that the challenged legislation lacks a rational basis. Accordingly, the district court did not miscalculate in finding it improbable that W & S would prevail on its equal protection claim.

## VII. CONCLUSION

We need go no further. W & S has not shown that it is likely to succeed on the merits of any of its claims. Since such a showing is a precondition to the securing of a preliminary injunction, [New Comm Wireless Servs., 287 F.3d at 9](#), we need not probe the other components of the applicable four-part test. It suffices to say that the district court acted well within the encirclement of its discretion in denying W & S's request for preliminary injunctive relief.

**Affirmed.**

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<sup>6</sup> To be sure, W & S contends that the challenged statutes burden its fundamental rights of speech and association. We dismiss that contention out of hand. See *supra* Part V (establishing that the challenged statutes do not impermissibly impinge upon W & S's [First Amendment](#) rights).

<sup>7</sup> Even in the improbable event that the two markets were to be deemed substantially similar, that showing alone would not ensure W & S's success. Regulation must start somewhere. See [FCC v. Beach Communications, 508 U.S. 307, 316, 124 L. Ed. 2d 211, 113 S. Ct. 2096 \(1993\)](#) (explaining that "the legislature must be allowed leeway to approach a perceived problem incrementally").



## N. Jackson Pharm., Inc. v. Caremark RX, Inc.

United States District Court for the Northern District of Illinois, Eastern Division

August 12, 2005, Decided ; August 12, 2005, Filed

No. 04 C 5674

### **Reporter**

385 F. Supp. 2d 740 \*; 2005 U.S. Dist. LEXIS 17020 \*\*; 2005-2 Trade Cas. (CCH) P74,900

NORTH JACKSON PHARMACY, INC., et al., etc., Plaintiffs, v. CAREMARK RX, INC., et al., Defendants.

**Prior History:** [N. Jackson Pharm., Inc. v. Express Scripts, Inc., 345 F. Supp. 2d 1279, 2004 U.S. Dist. LEXIS 23413 \(N.D. Ala., 2004\)](#)

## **Core Terms**

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Sponsors, cooperative, pharmacies, rule of reason, prescription drug, purchasing, prices, conspiracy, horizontal, ancillary, buyers, allegations, negotiation, retail, reimbursement rate, common agent, anticompetitive, network, antitrust, monopsony, license, venture, dispensing, functions, drugs, naked, alleged agreement, discounted, enterprise, costs

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > Pretrial Matters > Conferences > General Overview

### **HN1 [down arrow] Summary Judgment, Supporting Materials**

In part [Fed. R. Civ. P. 16\(c\)](#) permits a court to take appropriate action, with respect to (1) the formulation and simplification of the issues and (9) such other matters as may facilitate the just, speedy, and inexpensive disposition of the action. Resolution of issues as a matter of law under [Rule 16](#) is analogous to a [Fed. R. Civ. P. 56\(d\)](#) proceeding as to those issues (but not as to the entire case) in the summary judgment area. But there is at least one important difference: [Fed. R. Civ. P. 16](#) motions need not be accompanied by evidentiary statements called for by U.S. Dist. Ct., N.D. Ill., 56.1, as is required for [Fed. R. Civ. P. 56](#) motions for summary judgment. Such evidentiary statements, which serve to highlight which facts are disputed and which are agreed upon as an aid to determining whether the definitive disposition of a case or a discrete portion of a case is appropriate, are not called for when a party moves under [Fed. R. Civ. P. 16](#) only for an order narrowing the legal issues in a case.

Antitrust & Trade Law > Regulated Industries > Higher Education & Professional Associations > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## **HN2** [+] Regulated Industries, Higher Education & Professional Associations

Two complementary categories of antitrust analysis may be applied to determine whether an alleged restraint of trade is unreasonable. Which applies depends on the nature and effects of the alleged restraint. Where the competitive effect of an alleged restraint is not readily apparent, the "rule of reason" supplies the standard of analysis. To that end the factfinder evaluates the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed to form a judgment about the restraint's competitive significance. But in other cases a restraint's effect on competition is more obvious, so that the "per se" rule is applied instead. Per se treatment is appropriate for a restraint that falls into the category of agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm caused or the business excuse for their use. Per se treatment, rather than being a distinct method of analysis, follows from the rule of reason and is applied only once experience with a particular restraint enables courts to predict with confidence that the rule of reason will condemn it.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

## **HN3** [+] Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

Courts must avoid "formalistic line drawing" and must be hesitant to declare, as illegal per se, restraints imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > Price Fixing

Business & Corporate Compliance > ... > Business & Corporate Law > Cooperatives > Formation

Mergers & Acquisitions Law > Antitrust > Joint Ventures

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Business & Corporate Law > Cooperatives > General Overview

Business & Corporate Law > Joint Ventures > General Overview

Business & Corporate Law > Joint Ventures > Formation

## **HN4** [+] Cartels & Horizontal Restraints, Price Fixing

A horizontal conspiracy among buyers to stifle competition is as unlawful as one among sellers. But even so, a cooperative purchasing agreement among competing buyers does not necessarily stifle competition. Economists recognize that where buyers join to make purchases, any one of three economic models may exist. First, "cooperative buying" may be nothing more than a euphemism for collusive monopsony that drives prices below competitive levels and has negative economic effects on social welfare similar to those caused by price fixing sellers. Second, a cooperative buyer effort may not result in an aggregation of buying power at all and therefore, the

use of this power cannot be the motivation. Instead, these joint ventures are formed for the purpose of exploiting the productive efficiencies that result from conducting business on a larger scale. A third possibility is to have elements of both monopsony, with the attendant losses in allocative efficiency, and joint purchasing efficiency, resulting in productivity gains, at the same time. Which of those models will stem from a given cooperative purchasing agreement will not always be apparent immediately, so that the question becomes how to analyze such agreements under [§ 1](#) of the Sherman Act, [15 U.S.C. § 1](#). Antitrust's "ancillary restraints" doctrine is well-suited to that task.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

#### [HN5](#) Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

Under the ancillary restraints doctrine, courts must distinguish between "naked" restraints, those in which the restriction on competition is unaccompanied by new production or products, and "ancillary" restraints, those that are part of a larger endeavor whose success they promote. Naked restraints are unlikely to have any redeeming value and so are usually accorded per se treatment. But ancillary restraints that may contribute to the success of a cooperative venture that promises greater productivity and output demand the more thorough analysis provided by the rule of reason.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

#### [HN6](#) Price Fixing & Restraints of Trade, Cartels & Horizontal Restraints

The evaluation of ancillary restraints under the Rule of Reason does not imply that ancillary agreements are not real horizontal restraints. They are. But because [antitrust law](#) is designed to ensure an appropriate blend of cooperation and competition, not to require all economic actors to compete full tilt every moment, such restraints are excluded from per se treatment where they contribute to productivity through integration of efforts.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Business & Corporate Compliance > ... > Business & Corporate Law > Cooperatives > Formation

#### [HN7](#) Price Fixing & Restraints of Trade, Cartels & Horizontal Restraints

An agreement is not anticompetitive because it seeks to lower prices, and antitrust plaintiffs have to do more than complain about their failure to make more money.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

#### [HN8](#) Price Fixing & Restraints of Trade, Per Se Rule & Rule of Reason

While it is clear that substantial market power is an indispensable ingredient of every claim under the Rule of Reason, there appears to be no authority to support the notion that substantial market power is a sufficient, rather than a necessary, basis for finding that a given restraint is per se unlawful under [§ 1](#) of the Sherman Act, [15 U.S.C. § 1](#).

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**Judges:** Milton I. Shadur, Senior United States District [\[\\*\\*2\]](#) Judge.

**Opinion by:** Milton I. Shadur

## Opinion

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### [\*743] MEMORANDUM ORDER

North Jackson Pharmacy, Inc. and C & C, Inc. d/b/a Big C Discount Drugs, Inc. (collectively "North Jackson," treated for convenience as a singular noun) brought suit individually and on behalf of all other similarly situated independent pharmacies against Caremark Rx, Inc. and Caremark, Inc. (collectively "Caremark," also treated for convenience as a singular noun), charging violations of Section 1 of the Sherman Act, [15 U.S.C. §1](#) ("Section 1"). This Court originally inherited this action via a [28 U.S.C. §1404\(a\)](#) transfer from the United States District Court for the Northern District of Alabama, where it had been part of a three-case package of putative class actions.

Shortly after the transfer, Caremark filed a Fed. R. Civ. P. ("Rule") 12(b)(6) motion to dismiss the Second Amended Complaint ("SAC") with prejudice. North Jackson's responsive memorandum included a copy of the 25-page opinion issued by the transferor judge, Honorable Virginia Emerson Hopkins, that rejected a like Rule 12(b)(6) motion that had sought to dispatch the selfsame SAC [\[\\*\\*3\]](#) in the two cases that were retained in the Alabama District Court ([North Jackson Pharmacy, Inc. v. Express Scripts, Inc., 345 F. Supp. 2d 1279 \(N.D. Ala. 2004\)](#) ("Express Scripts")) Adopting the reasoning set out in *Express Scripts* without repeating Judge Hopkins' meticulous analysis, this Court summarily denied Caremark's Rule 12(b)(6) motion and ordered an answer to the SAC.

Caremark answered the SAC, and it has now filed a Rule 16 issue-narrowing motion that seeks an order from this Court establishing the rule of reason as the standard of analysis applicable to one of North Jackson's two Section 1 claims. For the reasons set out below, Caremark's motion is granted.

### Rule 16

**HN1** In part [Rule 16\(c\)](#) permits a court to take "appropriate action, with respect to (1) the formulation and simplification of the issues ... [and] (9) such other matters as may facilitate the just, speedy, and inexpensive disposition of the action." Resolution of issues as a matter of law under Rule 16 is analogous to a Rule 56(d)

proceeding as to those issues (but not as to the entire case) in the summary judgment area (see 6A Charles A. Wright, Arthur R. Miller & Mary Kay [<sup>\*\*4</sup>] Kane, *Federal Practice & Procedure: Civil* 2d §1529, at 299-301 (2d ed. 1990)). But there is at least one important difference: Rule 16 motions need not be accompanied by evidentiary statements called for by this District Court's LR 56.1, as is required for Rule 56 motions for summary judgment.

Such evidentiary statements, which serve to highlight which facts are disputed and which are agreed upon as an aid to determining whether the definitive disposition of a case or a discrete portion of a case is appropriate, are not called for when a party moves under Rule 16 only for an order narrowing the legal issues in a case--and none have been submitted here. Here the absence of such statements does not prevent this Court from ruling on the issue presented by Caremark's motion. That issue--the proper standard to be applied to North Jackson's Sherman Act claim--is one of law that can be resolved based on the allegations of the SAC and facts that neither party disputes. What follows then is a summary of the circumstances giving rise to this lawsuit, as set forth by the allegations of the SAC and the undisputed facts as set forth in the parties' submissions.

#### **[<sup>\*\*4</sup>] Background**

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[<sup>\*\*5</sup>] Caremark is a Pharmacy Benefits Manager ("PBM") that administers prescription drug benefit plans on behalf of employers, health insurers and other third-party payors of prescription drug costs ("Plan Sponsors") (SAC P14). Over 1,200 of such Plan Sponsors have hired Caremark to help control the cost of prescription drugs for their employees or members ("Plan Subscribers") (SAC PP15, 29). Caremark accomplishes that goal by performing a number of functions on Plan Sponsors' behalf, the most important of which for purposes of this motion is the creation of a network of retail pharmacies where Plan Subscribers can purchase discounted drugs (SAC P30). Caremark also lowers Plan Sponsors' costs by processing claims, maintaining patient records, creating and managing "formularies" (lists of drugs preferred by a given plan) and negotiating discounts or rebates with drug manufacturers that wish their drugs to be included on plan formularies (C. Mem. 4; C. Ex. 4 at 1-2).

North Jackson is an independent retail pharmacy that, like many retail pharmacies, has entered into an agreement with Caremark to dispense prescription drugs to Plan Subscribers (SAC PP9, 11). In return for inclusion in Caremark's [<sup>\*\*6</sup>] network and access to the large volume of business that such inclusion brings, North Jackson must agree to dispense drugs to Plan Subscribers at a discount from prices charged to its cash-paying customers (SAC P30). Such discounted prices, for which Caremark reimburses North Jackson, are set by agreement between Caremark and North Jackson, but are usually determined using a formula based on a drug's average wholesale price plus a dispensing fee (SAC P31).

North Jackson objects among other things to Caremark's creation of retail pharmacy networks and its negotiation of reimbursement rates on Plan Sponsors' behalf. When Caremark approaches independent pharmacies such as North Jackson for inclusion in Caremark's network, it presents such pharmacies with, as North Jackson would have it, a Hobson's choice between (1) being included in the network and accepting unconscionably low reimbursement rates for drugs dispensed to Plan Subscribers and (2) being left out of the network and thereby losing access to the large volume of business represented by Plan Subscribers who have an incentive to patronize network pharmacies. North Jackson's suit thus charges that Caremark's negotiation of those [<sup>\*\*7</sup>] low reimbursement rates is not a "negotiation" at all, but is instead a form of coercion that results from an illegal conspiracy to fix drug prices between and among Caremark and other PBMs and the Plan Sponsors they represent.

#### *North Jackson's Section 1 Claims*

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<sup>1</sup> This opinion uses "C." and "N.J." to identify documents respectively submitted by Caremark and North Jackson.

North Jackson's SAC alleges two per se violations of [Section 1](#). Claim I asserts a conspiracy between Plan Sponsors, using Caremark as their "common agent," to fix the prices paid independent pharmacies for dispensing prescription drugs to Plan Subscribers. Claim II charges a conspiracy between Caremark and PBMs with which it competes to fix those same prices. To establish that it is entitled to relief on either claim, North Jackson must demonstrate that Caremark took part in a "contract, combination...or conspiracy" that unreasonably restrains trade ([Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 768, 81 L. Ed. 2d 628, 104 S. Ct. 2731 \(1984\)](#)).

[\*745] [HN2](#)<sup>↑</sup> Two "complementary categories of antitrust analysis" may be applied to determine whether an alleged restraint of trade is unreasonable ([National Soc. of Professional Engineers v. United States, 435 U.S. 679, 692, 55 L. Ed. 2d 637, 98 S. Ct. 1355 \(1978\)](#)). Which applies depends on the nature and effects of the alleged [\*\*8] restraint ([Denny's Marina, Inc. v. Renfro Prods., Inc., 8 F.3d 1217, 1220 \(7th Cir. 1993\)](#)). Where the competitive effect of an alleged restraint is not readily apparent, the "rule of reason" supplies the standard of analysis. To that end the factfinder evaluates "the facts peculiar to the business, the history of the restraint, and the reasons why it was imposed" to form a judgment about the restraint's competitive significance ([Prof'l Eng'rs, 435 U.S. at 692](#)).

But in other cases a restraint's effect on competition is more obvious, so that the "per se" rule is applied instead. Per se treatment is appropriate for a restraint "that falls into the category of agreements or practices which because of their pernicious effect on competition and lack of any redeeming virtue are conclusively presumed to be unreasonable and therefore illegal without elaborate inquiry as to the precise harm caused or the business excuse for their use" ([N.W. Wholesale Stationers, Inc. v. Pac. Stationery & Printing Co., 472 U.S. 284, 289, 86 L. Ed. 2d 202, 105 S. Ct. 2613 \(1985\)](#) (internal quotation marks omitted)). Per se treatment, rather than being a distinct method of analysis, follows from [\*\*9] the rule of reason and is applied only "once experience with a particular restraint enables [courts] to predict with confidence that the rule of reason will condemn it" ([Ariz. v. Maricopa County Med. Soc., 457 U.S. 332, 344, 73 L. Ed. 2d 48, 102 S. Ct. 2466 \(1982\)](#)).

Caremark implicitly concedes that the conspiracy alleged in Claim II--that between Caremark and other PBMs to fix drug prices--would if proved constitute a naked horizontal price-fixing agreement subject to per se treatment. But it contests application of the per se rule to Claim I--the "common agent" claim--and seeks this Court's ruling that the rule of reason supplies the standard of analysis as to that claim. Such a ruling falls within Rule 16's purview, Caremark contends, because the choice between per se and rule of reason treatment will bear heavily on the conduct of discovery and, perhaps more importantly, on the propriety of class certification.

This Court of course reserves judgment as to how the standard chosen will affect North Jackson's inevitable class certification motion. But because the choice between per se and rule of reason treatment as to the common agent claim will plainly aid in the formulation of issues and will [\*\*10] facilitate the just, speedy and inexpensive disposition of this action, this opinion proceeds to a decision on the merits of Caremark's Rule 16 motion.

#### *Treatment of North Jackson's Common Agent Claim*

North Jackson urges that the alleged conspiracy between the Plan Sponsors and their use of Caremark as a common agent to effect that conspiracy's aim constitutes an illegal horizontal restraint of trade of the nature and type historically subject to per se treatment. Caremark challenges that assertion on two fronts. First it contends that the challenged arrangement between Caremark and the Plan Sponsors it represents is not properly viewed as a horizontal restraint between direct competitors, but is instead more accurately characterized as a series of vertical restraints. Such restraints are, as Caremark observes, generally subject to rule of reason rather than per se treatment and so should be in this case. Second, Caremark argues that even if the SAC is construed to allege a horizontal restraint, the [\*746] Plan Sponsors' use of Caremark as a common agent is not a "naked" restraint that should be presumed illegal, but is rather "ancillary" to a legitimate cooperative enterprise that [\*\*11] has the potential to increase productive efficiency. Consequently that ancillary restraint should be analyzed under the rule of reason. Those contentions will be dealt with in turn.

In support of its first argument, Caremark urges that the proper objects of analysis are the individual contracts between Caremark and the more than 1,200 Plan Sponsors it represents. Caremark is not a competitor of the Plan

385 F. Supp. 2d 740, \*746L 2005 U.S. Dist. LEXIS 17020, \*\*11

Sponsors, operating instead at a different level of the prescription drug purchasing chain, and so the argument goes that the contracts at issue are vertical restraints. And because [Business Elec. Corp. v. Sharp Elec. Corp., 485 U.S. 717, 724, 99 L. Ed. 2d 808, 108 S. Ct. 1515 \(1988\)](#) emphasized the Court's view that "the scope of *per se* illegality should be narrow in the context of vertical restraints," Caremark says that rule of reason treatment is proper as to those 1,200 individual contracts.

But that argument ignores the allegations of the SAC as construed by [Express Scripts, 345 F.Supp.2d at 1294](#):

The SAC implies that plan sponsors share, and are aware that they share, a common strategy--*i.e.*, the utilization of a PBM to combine purchasing power and drive down [\*\*12] pharmacy costs.

Under [United States v. Masonite Corp., 316 U.S. 265, 276, 86 L. Ed. 1461, 62 S. Ct. 1070, 1942 Dec. Comm'r Pat. 777 \(1942\)](#) the Plan Sponsors' knowledge of and acquiescence in that common strategy could reasonably support a finding of conspiracy under [Section 1](#). And as [Express Scripts, 345 F.Supp.2d at 1294-95](#) observed, if the Plan Sponsors have conspired to fix prices "a horizontal restraint is created even if PBMs are used to carry out the scheme."

Hence Caremark's assertion that the complained-of agreements are vertical restraints misses the mark. For purposes of Pharmacy's common agent claim, the relevant agreement is that alleged to exist among the Plan Sponsors. And that agreement, between firms that would normally compete with each other for the purchase of prescription drugs, may fairly be said to constitute a horizontal restraint.

But Caremark's alternative argument properly stresses that the SAC's allegation of horizontal price-fixing and its asserted attachment of the "*per se*" label do not, as North Jackson would have it, constrain this Court's ability to scrutinize the alleged agreement to determine whether *per se* treatment is indeed appropriate ([Car Carriers, Inc. v. Ford Motor Co., 745 F.2d 1101, 1108 \(7th Cir. 1984\)](#)). [\*\*13] This Court's obligation to do so exists because the Supreme Court has cautioned that [HN3](#)[<sup>↑</sup>] courts must avoid "formalistic line drawing" ([Continental T.V., Inc. v. GTE Sylvania Inc., 433 U.S. 36, 59, 53 L. Ed. 2d 568, 97 S. Ct. 2549 \(1977\)](#)) and must be hesitant to declare, as illegal *per se*, "restraints imposed in the context of business relationships where the economic impact of certain practices is not immediately obvious" ([State Oil Co. v. Khan, 522 U.S. 3, 10, 139 L. Ed. 2d 199, 118 S. Ct. 275 \(1997\)](#)). To see whether the challenged conduct falls within the *per se* category, it is thus necessary to consider the alleged agreement among Plan Sponsors in the larger context of the arrangement between them and Caremark.

By negotiating prescription drug reimbursement rates on behalf of the 1,200 Plan Sponsors it represents, Caremark acts on behalf of what is essentially a cooperative purchasing group. In support of its contention that a cooperative purchasing agreement among Plan Sponsors should not be presumed illegal, Caremark [\*747] makes much of the distinction made between buyers and sellers under the antitrust laws.

To be sure, that distinction does not carry the full significance Caremark attaches to it, because [HN4](#)[<sup>↑</sup>] "a horizontal [\*\*14] conspiracy among buyers to stifle competition is as unlawful as one among sellers" ([Todd v. Exxon Corp., 275 F.3d 191, 201 \(2nd Cir. 2001\)](#), citing [Mandeville Island Farms, Inc. v. Am. Crystal Sugar Co., 334 U.S. 219, 235, 92 L. Ed. 1328, 68 S. Ct. 996 \(1948\)](#)). But even so, a cooperative purchasing agreement among competing buyers does not necessarily stifle competition. Economists recognize that where buyers join to make purchases, any one of three economic models may exist (Roger D. Blair & Jeffrey L. Harrison, *Monopsony: Antitrust Law and Economics* 93-94 (1993)):

First, "cooperative buying" may be nothing more than a euphemism for collusive monopsony that drives prices below competitive levels and has negative economic effects on social welfare similar to those caused by price fixing sellers. Second, a cooperative buyer effort may not result in an aggregation of buying power at all and therefore, the use of this power cannot be the motivation. Instead, these joint ventures are formed for the purpose of exploiting the productive efficiencies that result from conducting business on a larger scale....A third possibility is to have elements of both monopsony, with the [\*\*15] attendant losses in allocative efficiency, and joint purchasing efficiency, resulting in productivity gains, at the same time.

Which of those models will stem from a given cooperative purchasing agreement will not always be apparent immediately, so that the question becomes how to analyze such agreements under [Section 1](#). Antitrust's "ancillary restraints" doctrine is well-suited to that task.

**HN5** Under the ancillary restraints doctrine, courts "must distinguish between 'naked' restraints, those in which the restriction on competition is unaccompanied by new production or products, and 'ancillary' restraints, those that are part of a larger endeavor whose success they promote" ([Polk Bros., Inc. v. Forest City Enters., Inc., 776 F.2d 185, 188-89 \(7th Cir. 1985\)](#)). Naked restraints are unlikely to have any redeeming value and so are usually accorded per se treatment. But ancillary restraints that "may contribute to the success of a cooperative venture that promises greater productivity and output" ([id. at 189](#)) demand the more thorough analysis provided by the rule of reason.

As *Polk Bros.*, *id.* observed, **HN6** "the evaluation of ancillary restraints [\*\*16] under the Rule of Reason does not imply that ancillary agreements are not real horizontal restraints. They are." But because "[antitrust law](#) is designed to ensure an appropriate blend of cooperation and competition, not to require all economic actors to compete full tilt every moment" ([id. at 188](#)), such restraints are excluded from per se treatment where they "contribute[] to productivity through integration of efforts" (*id.*).

[Broadcast Music, Inc. v. Columbia Broad. Sys., Inc., 441 U.S. 1, 60 L. Ed. 2d 1, 99 S. Ct. 1551 \(1979\)](#), a case upon which Caremark relies heavily, applied those principles to a licensing agent's issuance of "blanket licenses" for the performance of all of its client composers' musical compositions. Acknowledging that such a blanket license "involves 'price fixing' in the literal sense" because the composers had joined together in an organization that set the price for the blanket license it sold ([id. at 8](#)) the Court nonetheless held that per se treatment was inappropriate because rather than being a naked restraint, the blanket license "accompanied [\*748] the integration of sales, monitoring, and enforcement against unauthorized copyright use" [\*\*17] ([id. at 20](#)). And as the Court further explained, "a bulk license of some type is a necessary consequence of the integration necessary to achieve these efficiencies, and a necessary consequence of an aggregate license is that its price must be established" ([id. at 21](#)).

While there are few reported cases that apply [Section 1](#) and the ancillary restraints doctrine to cooperative purchasing arrangements, [Kartell v. Blue Shield of Mass., Inc., 749 F.2d 922, 925 \(2nd Cir. 1984\)](#) observed that courts had invalidated such arrangements only where "the buyer was typically a 'sham' organization seeking only to combine otherwise independent buyers in order to suppress their otherwise competitive instinct to bid up price." But where in contrast buyers join together in a productive venture, cooperative buying is rarely viewed as a per se unlawful restraint under [Section 1](#) so long as it contributes to the productive enterprise.

*N.W. Wholesale Stationers* thus held that a non-profit wholesale purchasing cooperative that allowed office-supply retailers to "achieve economies of scale in purchasing and warehousing that would be otherwise unavailable [\*\*18] to them" ([472 U.S. at 286-87](#)) was (*id. at 295* (internal quotation marks omitted)):

not a form of concerted activity characteristically likely to result in predominantly anticompetitive effects.  
Rather, such cooperative arrangements would seem to be designed to increase economic efficiency and render markets more, rather than less, competitive.

And [Addamax Corp. v. Open Software Found., Inc., 152 F.3d 48, 52 \(1st Cir. 1998\)](#) held that per se treatment was inappropriate where the alleged anticompetitive conduct--an agreement between a joint venture's constituent firms as to the price at which the venture would purchase inputs--was ancillary to the joint venture's productive contribution to the economy.

Caremark relies on *Broadcast Music*, *N.W. Wholesale* and *Addamax* to argue that its negotiation of reimbursement rates on behalf of Plan Sponsors, even if it were to be viewed as reflective of an otherwise anticompetitive horizontal restraint, is part and parcel of a larger cooperative enterprise whose purpose and effect is to *increase* competition in the insurance-reimbursed prescription drug market. Any alleged agreement [\*\*19] between Plan Sponsors to set the price paid for prescription drugs thus cannot be viewed in a vacuum, but must instead be looked at as a corollary of the cooperative arrangement between Caremark and the Plan Sponsors under which

Caremark performs a variety of functions in the administration of Plan Sponsors' drug benefit plans. Those functions include not only the negotiation of reimbursement rates with retail pharmacies but also the processing of reimbursement claims, maintenance of patient records, design and management of drug formularies, negotiation of manufacturer rebates and maintenance of a mail order pharmacy. According to Caremark, those functions contribute to increased efficiency and a reduction in the cost of prescription drugs delivered to Plan Subscribers.

For its part North Jackson argues that the designation of an agreement to lower prices as "ancillary" to a larger cooperative venture does not reflect the true nature of the arrangement between Plan Sponsors and Caremark, whose primary purpose is to lower the price of prescription drugs. But [HN7](#)<sup>1</sup> an agreement is not anticompetitive because it seeks to lower prices, and antitrust plaintiffs have to do more than complain [\[\\*\\*20\]](#) about their failure to make more money ([Brillhart v. Mut. Med. I](#)\*[749](#) Ins., Inc., 768 F.2d 196, 200 (7th Cir. 1985)). So the fact that the purpose of the cooperative relationship between Caremark and the Plan Sponsors is to affect drug prices (indeed, to lower them) begs the question whether it does so in a procompetitive, efficiency-enhancing manner that benefits consumers, or whether instead that goal is accomplished through unlawful collusion that drives prices below competitive levels and thereby reduces social welfare.

As described by the SAC and the parties' submissions on the current motion, the arrangement between Plan Sponsors and Caremark clearly has efficiency-enhancing potential. Caremark specializes in various functions of benefit plan administration and is likely able to achieve economies of scale in the performance of those functions that would otherwise be unavailable to Plan Sponsors. And the creation of retail pharmacy networks, which necessarily involves the setting of reimbursement rates, undoubtedly contributes to the success of that larger endeavor.

What is more, there is a real question whether, on the other side of the coin, the arrangement actually [\[\\*\\*21\]](#) has any countervailing anticompetitive consequences. Last year the FTC had occasion to consider Caremark's negotiation of reimbursement rates on behalf of Plan Sponsors when it investigated Caremark's acquisition of AdvancePCS, a former competitor. Addressing the question whether that acquisition would confer monopsony power on Caremark vis-a-vis retail pharmacies, the FTC explained in its Feb. 11, 2004 statement (*In re Caremark Rx, Inc./AdvancePCS*, FTC 031-0239, 2004 WL 318820):

A buyer has monopsony power--or a group of buyers has oligopsony power--when it can profitably reduce prices in a market below competitive levels by curtailing purchases of the relevant product or service. The exercise of this power causes competitive harm because the monopsonist or the group will shift some purchases to a less efficient source, supply too little output to the downstream market, or do both.

In the present case there is no reason to expect a monopsony or oligopsony outcome--i.e., one in which overall purchases from pharmacies are reduced--even if the acquisition enables the merged PBM (or PBMs as a group) to reduce the dispensing fees they pay to retail pharmacies. [\[\\*\\*22\]](#) Characteristics of the relevant market make monopsony or oligopsony power unlikely.

Rather than explaining how the arrangement purportedly reduces competition or responding to the potentially procompetitive aspects of the cooperative enterprise. North Jackson simply asserts that the alleged agreement between plan sponsors is a "naked restraint" on price, going on to list various allegations from the SAC that it says "establish per se violations" (N.J. Mem. 14-15). But none of the allegations listed there pertain to the alleged agreement between Plan Sponsors that is the subject of Claim I. Instead all of those allegations go to Claim II: the alleged horizontal conspiracy between Caremark and its competitor PBMs--a conspiracy that, if established, Caremark acknowledges would constitute a per se violation of [Section 1](#). Such allegations do not negate what has already been said: that the bundle of services provided by Caremark reflects a cooperative arrangement between Caremark and the Plan Sponsors that has efficiency-enhancing potential. And because the alleged anticompetitive agreement between Plan Sponsors is ancillary to that arrangement, it will be assessed under the more probing [\[\\*\\*23\]](#) analysis offered by the rule of reason.<sup>2</sup>

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<sup>2</sup> North Jackson's other principal argument in favor of per se treatment is that Caremark has "immense market power" and that its activities should therefore be judged under the per se rule. That argument has no merit. [HN8](#)<sup>1</sup> While it is clear that

[\*750] Application of the rule of reason to North Jackson's common agent claim is supported by two other related factors. First, the alleged anticompetitive agreement is one that might at least in the short term result in lower drug prices for consumers. According to a July 2004 joint [\*24] report of the Federal Trade Commission and the Department of Justice to which Caremark calls the Court's attention, "the empirical evidence suggests that consumers with prescription drug insurance administered by a PBM save substantially on their drug costs as compared to cash-paying customers" (*Improving Health Care: A Dose of Competition* 7:11, available at: [http://www.usdoj.gov/atr/public/health\\_care/204694.htm](http://www.usdoj.gov/atr/public/health_care/204694.htm)). As *Sanjuan v. Am. Bd. of Psychiatry & Neurology, Inc.*, 40 F.3d 247, 251 (7th Cir. 1994) puts it, the antitrust laws "are designed to drive producers' prices down rather than up." To hold an agreement that tends to lower consumer prices illegal per se, without careful examination of the agreement's true economic consequences, would seem at odds with the Sherman Act's purpose.<sup>3</sup>

[\*\*25] Another and related factor arises from a concern explained by *Kartell*, 749 F.2d at 931 (citation omitted):

The subject matter of the present agreement--medical costs--is an area of great complexity where more than solely economic values are at stake. How to provide affordable, high quality medical care is much debated. And, many different solutions--ranging from stricter regulation to greater reliance on competing service organizations--have been proposed. This fact, too, warrants judicial hesitancy to interfere.

That is of particular relevance here, where (as North Jackson itself alleges) PBMs such as Caremark administer the prescription drug benefits of "approximately 210 million Americans; 70% of the U.S. population" (SAC P3). Any premature ruling that one of the primary functions performed by PBMs is per se illegal would have particularly far-reaching consequences for the delivery of affordable prescription drugs to a large portion of the population, a consideration that further supports thorough rule of reason analysis.

What has been said to this point should not be read as expressing an ultimate view as to the lawfulness of the alleged conspiracy [\*26] between Plan Sponsors. If the required rule of reason inquiry were to reveal that the anticompetitive consequences of any such conspiracy sufficiently outweigh its procompetitive benefits so that the restraint is ultimately judged unreasonable under *Section 1*, this Court would not hesitate to rule accordingly. But because no authority even suggests that all [\*751] cooperative purchasing agreements run afoul of *Section 1*, and because the agreement at issue here is part of a larger and potentially procompetitive enterprise, the rule of reason must be applied to North Jackson's Claim I.

### *Conclusion*

As North Jackson would have it, the application of such pejorative labels as "horizontal restraint of trade" automatically triggers the application of a malum in se label--a per se violation of *Sherman Act §1*--that just as automatically renders illegal a group buying arrangement through an intermediary that *lowers* costs without restricting competition<sup>4</sup> or decreasing output. That universe, generated by an unthinking adherence to the tyranny of labels, may exist in North Jackson's corporate mind and the minds of its counsel, but it does not exist in the real

"substantial market power is an indispensable ingredient of every claim under the Rule of Reason" (*Digital Equip. Corp. v. Uniq Digital Tech., Inc.*, 73 F.3d 756, 761 (7th Cir. 1996)), there appears to be no authority (and indeed none is found in the cases North Jackson cites) to support the notion that substantial market power is a sufficient, rather than a necessary, basis for finding that a given restraint is per se unlawful under *Section 1*.

<sup>3</sup>It is true that the SAC alleges that consumers will ultimately be harmed by the alleged conspiracy, as "PBMs will bankrupt [independent] pharmacies, thereby capturing a larger segment of the insurance-paid prescription market for the PBMs' own prescription-dispensing business, [which will] allow[] the PBMs to charge higher prices for that service" (*Express Scripts*, 345 F.Supp.2d at 1292). Whether that is so, however, is a question better answered by a full rule of reason inquiry. What controls for present purposes is that the immediate and assured consequence of the alleged agreement appears to be lower prices for the consumers of insurance-reimbursed prescription drugs.

<sup>4</sup>For purposes of the current analysis, North Jackson's Claim II--that other aspects of Caremark's activities in conjunction with other PBMs assertedly restrict competition--is not implicated in the claim now under review.

world of antitrust jurisprudence. **[\*\*27]** Because rule-of-reason rather than per se treatment applies, Caremark's Rule 16 motion on that score is granted.<sup>5</sup>

**[\*\*28]** Milton I. Shadur

Senior United States District Judge

Date: August 12, 2005

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<sup>5</sup> Whether (as appears likely) this opinion proves to be the last major assignment of this Court's soon-to-depart law clerk Alex Pearce, it well exemplifies his outstanding work throughout his clerkship year. That high quality has marked all of Alex's tenure, whether in the production of draft opinions or in the performance of all the other duties that devolve upon this Court's clerks in what is akin to a three-lawyer law firm. As always it should be made clear, however, that any errors that may have found their way into the final opinions signed by this Court are its responsibility rather than that of its fine clerk, for every such work product has been the result of this Court's word by word and sentence by sentence vetting and recasting of the clerk's original draft.



## **Smith Wholesale Co. v. Philip Morris USA Inc.**

United States District Court for the Eastern District of Tennessee

August 16, 2005, Decided ; August 17, 2005, Filed

NO. 2:03-CV-221

### **Reporter**

2005 U.S. Dist. LEXIS 18078 \*; 2005 WL 1981452

SMITH WHOLESALE COMPANY, INC., et al. v. PHILIP MORRIS USA INC.

**Subsequent History:** Later proceeding at [Smith Wholesale Co. v. Philip Morris USA, Inc., 2005 U.S. Dist. LEXIS 18058 \(E.D. Tenn., Aug. 23, 2005\)](#)

Affirmed by [Smith Wholesale Co. v. Philip Morris USA, Inc., 2007 U.S. App. LEXIS 4754 \(6th Cir. Tenn., Feb. 27, 2007\)](#)

## **Core Terms**

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discount, cigarette, customers, plaintiffs', prices, competitors, market share, market power, buyer, sales, products, summary judgment, monopolize, anti-competitive, manufacturers, price discrimination, distributors, Wholesale, brands, purchasing, quantity, seller, tier, genuine issue of material fact, monopoly power, best price, practices, preliminary injunction, specific intent, anti trust law

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > Robinson-Patman Act > Remedies > Damages

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > Regulated Practices > Price Discrimination > Promotional Allowances & Services

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > Robinson-Patman Act > Remedies > Injunctions

Business & Corporate Law > Distributorships & Franchises > Causes of Action > Restraints of Trade

### **HN1 [down arrow] Remedies, Damages**

To establish a prima facie case under [§ 2\(a\)](#) of the Robinson-Patman Act, [15 U.S.C.S. § 13\(a\)](#), plaintiffs must prove that: (1) the defendant's product sales to the plaintiffs and their competitors are "in interstate commerce"; (2) the

sales involve products of "like grade and quality"; (3) the sales discriminate in prices among these competing distributors; and (4) the discrimination substantially lessens competition and causes antitrust injury to the plaintiffs.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

## **HN2** **Robinson-Patman Act, Claims**

If the best prices are available equally and functionally to all customers, then no price discrimination has occurred.

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

## **HN3** **Price Discrimination, Defenses**

The use of the functional availability theory to demonstrate the lack of an essential element of the plaintiffs' case, i.e. price discrimination, is technically not an affirmative defense, but the negation of an element of the plaintiff's case.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

## **HN4** **Summary Judgment, Entitlement as Matter of Law**

If an essential element of the plaintiff's case is negated, summary judgment is appropriate.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Business & Corporate Compliance > ... > Remedies > Seller's Damages & Remedies > General Overview

Antitrust & Trade Law > ... > Price Discrimination > Competitive Injuries > General Overview

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

## **HN5** **Robinson-Patman Act, Claims**

The practice of conditioning price concessions and allowances upon the customer's purchase of a specific quantity of goods will not give rise to a Robinson-Patman violation if the concessions are available equally and functionally

to all customers. Further, a claim of price discrimination will not lie if the buyer failed to take advantage of a price concession which was realistically and functionally available. The legislative history reveals that the aim of the Robinson-Patman Act is to prevent a large buyer from gaining discriminatory preferences over the small buyer solely because of the large buyer's greater purchasing power.

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

#### **HN6** Price Discrimination, Defenses

To the extent that there is an "availability" defense, it will fail if the lower price is not "practically" available to all competing customers. Discounts must be available not only in theory but in fact to be practically available. "Equal opportunity" is required; even when a seller has a dual pricing system, if the lower price is available to all purchasers, not only in theory but in fact, there is no violation of [§ 2\(a\)](#) of the Robinson-Patman Act, [15 U.S.C.S. § 13\(a\)](#).

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

#### **HN7** Price Discrimination, Defenses

Discounts that have been held to not be functionally available because they were discounts in theory but not in fact are: (1) Quantity discounts, which are not functionally available to many small buyers; (2) When the purchaser was not told about the discount; and (3) When the purchaser was not permitted to participate in the program.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

#### **HN8** Private Actions, Remedies

The antitrust laws were never intended to protect individual competitors.

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > ... > Price Discrimination > Defenses > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

#### **HN9** Robinson-Patman Act, Claims

Case law does not support the conclusion that the demands of a purchaser's customer can render a discount functionally unavailable for purposes of the Robinson-Patman Act. Courts have refused to find discrimination when the buyer's inability to take advantage of the best discount was within the control of the buyer, such as poor credit, management choices, decisions not to hold inventory, or particular marketing strategies.

Antitrust & Trade Law > Sherman Act > Claims

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > Robinson-Patman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > Claims

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

#### **HN10** [blue download icon] **Sherman Act, Claims**

A claim for attempted monopolization under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), requires: (1) a specific intent to monopolize; (2) anti-competitive conduct; and (3) a dangerous probability of success.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

#### **HN11** [blue download icon] **Monopolies & Monopolization, Attempts to Monopolize**

Market power is a necessary element for showing a dangerous probability of achieving monopoly power in an attempt to monopolize case. In determining whether there is a dangerous probability of monopolization, courts have considered the relevant market and the defendant's ability to lessen or to destroy competition in that market.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### **HN12** [blue download icon] **Monopolies & Monopolization, Attempts to Monopolize**

An attempt to monopolize claim requires "proof of market power." An analysis of market power requires that the court, focus on the ability of a single seller to unilaterally raise prices and restrict output.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

#### **HN13** [blue download icon] **Monopolies & Monopolization, Attempts to Monopolize**

On an attempt to monopolize claim, an analysis of market power requires that the court, focus on the ability of a single seller to unilaterally raise prices and restrict output.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

## [HN14](#) [blue download icon] Monopolies & Monopolization, Attempts to Monopolize

For purposes of an attempt to monopolize analysis, market share, standing alone, is insufficient to establish market power as a matter of law and is only the starting point for determining whether monopoly power exists. The inference of monopoly power does not automatically follow from the possession of a commanding market share.

Antitrust & Trade Law > Sherman Act > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > Robinson-Patman Act > General Overview

## [HN15](#) [blue download icon] Antitrust & Trade Law, Sherman Act

Competition is a ruthless process and the anti-trust laws are not a balm for the rivals' wounds.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

## [HN16](#) [blue download icon] Antitrust & Trade Law, Sherman Act

It is well established that the anti-trust laws are designed to protect competition, not individual competitors.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

## [HN17](#) [blue download icon] Regulated Practices, Market Definition

A firm lacks market power when its competitors have excess capacity. Excess capacity is the ability of existing competitors to expand output to counteract a reduction in output by a provider with a large market share. Excess capacity inhibits monopoly pricing because consumers can obtain the product or service at competitive pricing from another provider. Excess capacity deprives a relatively large "market share" of its normal "market power."

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Robinson-Patman Act > General Overview

## [HN18](#) [blue download icon] Antitrust & Trade Law, Sherman Act

Anticompetitive conduct is conduct designed to destroy competition, not just to eliminate a competitor. Lively legal competition will result in the efficient and shrewd businessman routing the inefficient and imprudent from the field. The anti-trust laws must be administered in such a way that they do not restrain such vigorous competition in order to protect inefficient competitors. The successful competitor, having been urged to compete, must not be turned on when he wins. Merely to attempt to succeed in business is not anti-competitive conduct.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN19** [ ] **Monopolies & Monopolization, Actual Monopolization**

Specific intent to monopolize may be inferred from evidence of anti-competitive conduct, but not from legitimate business practices aimed only at succeeding in competition. **Antitrust law** protects competition, not particular competitors. Whether conduct is anti-competitive for purposes of [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), depends on whether valid business reasons can explain defendants' actions.

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For A D Bedell Company, Inc., Andalusia Distributing Company, Inc., Axton Candy & Tobacco Co., Buyers Wholesale Distributors, Inc., Dixie Tobacco & Candy Co., Inc., Forest City Grocery Co., Inc., Home Folks Wholesale Co., Inc., Independent Wholesale, Inc., Macon Cigar & Tobacco Co., Inc., Mydad, LLC doing business as Hardec's, Pittman Brothers Co., Inc., Renfro Supply Co., Inc., Rice Wholesale Company, Inc., Robert's Cigar & Tobacco Co., Inc., C T Jewell, Co., Inc, Derigo Sales, Plaintiffs: Kyle M Keegan, Chris D Kiesel, David A Lowe, Roy, Kiesel, Keegan & DeNicola, Baton Rouge, LA.

For A B Coker Co., Inc., Affiliated Foods INC., Ashland Specialty Co, Eby Brown Co., Huntsville Wholesale Grocery, Jackson Wholesale, LAG, Inc., M-K Grocery Co. doing business as Bates Distributing Co., Market Grocery Co. doing business as Modern Grocery Co., Novelart Manufacturing Co., Inc. doing business as TOPICZ, Park City Tobacco, Reidsville Grocery Company, Inc., R.C. Taylor Distributing, Triple C Wholesale, Wichita [\*2] Tobacco & Candy Co., Plaintiffs: Earl R Booze, Herrin, Booze, Rambo, Jenkins & Wheeler, Johnson City, TN; Kyle M Keegan, Chris D Kiesel, David A Lowe, Roy, Kiesel, Keegan & DeNicola, Baton Rouge, LA.

For William Brockman Co., Plaintiff: Kyle M Keegan, Chris D Kiesel, Roy, Kiesel, Keegan & DeNicola, Baton Rouge, LA.

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For State of Mississippi, Intervenor Plaintiff: Sondra S McLemore, Attorney General of Mississippi, Office of Consumer Protection, Jackson, MS. David A Lowe, Roy, Kiesel, Keegan & DeNicola, Baton Rouge, LA.

**Judges:** J. RONNIE GREER, UNITED STATES DISTRICT JUDGE.

**Opinion by:** Greer

## **Opinion**

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### **MEMORANDUM OPINION**

[\*3] This [Robinson-Patman Act/Sherman Act](#) complaint is before the Court to consider the Motion for Summary Judgment filed by the defendant, Philip Morris USA Inc. ("PM"), on the basis that the defendant's discounts are functionally available to all distributors and because the defendant's market share incentive program is lawful under the [Sherman Act](#). [Doc. 176].

On June 11, 2003, sixteen plaintiffs filed suit against PM alleging that PM's Wholesale Leaders ("WL") program, a market share based discount program, constituted illegal price discrimination and an attempt to monopolize under federal antitrust laws. [15 U.S.C. § 1 et seq.](#) On July 14, 2003, the State of Mississippi filed an Intervenor's Complaint after obtaining leave of this Court. Seventeen new plaintiffs were added in an amended complaint filed with this Court on November 14, 2003.

On August 6, 2003, this Court granted a preliminary injunction which enjoined PM from providing lower price discounts and /or rebates to the plaintiffs than are provided to the plaintiffs' competitors as proposed in the new 2003 WL. PM appealed this Court's order granting the preliminary injunction to the Court of [\*\*4] Appeals for the Sixth Circuit and a Stay of the Preliminary Injunction was granted on September 18, 2003. PM's appeal of this injunction was argued and is currently pending before the Sixth Circuit.<sup>1</sup> Discovery is now closed. PM has filed its motion for summary judgment on all of the plaintiffs' claims and the claims of the State of Mississippi. After careful consideration of the record as a whole, this Court makes the following findings of fact and conclusions of law. For the purpose of deciding this motion for summary judgment, the Court will adopt the facts as submitted by the plaintiffs.

## **FACTUAL BACKGROUND SUBMITTED BY THE PLAINTIFF**

### **A. Cigarette Industry**

The U.S. cigarette industry is highly concentrated and oligopolistic. Philip Morris is the unchallenged market leader with 56% of sales by dollar volume and [\*5] the two largest manufacturers, PM and R.J. Reynolds (RJR), now control more than 80% of the market. Like most oligopolies, the cigarette industry exhibits little price competition and shows lock-step pricing among manufacturers of premium cigarettes. Producers of low price 4th tier cigarettes have entered the market since the Master Settlement Agreement of 1998 and their entry has captured less than 15% of the market but has not caused a decrease in premium cigarette prices.

### **B. Plaintiffs' Business**

Plaintiffs sell tobacco and other products at wholesale to grocery and convenience stores and other retail outlets in various states. Tobacco products constitute 50% or more of their sales and most plaintiffs have purchased, directly from PM for more than 50 years. As full service wholesalers, plaintiffs supply their retailer customers with products they request, including all major manufacturers' cigarettes as well as 4th tier and other non-PM cigarettes. The retailers base their purchases on customer demand which is influenced by advertising, product promotions and retail store programs, all controlled by the manufacturer.

### **C. PM's Wholesale Leaders Programs [\*6] -- 1999 To Present**

From 1999 through 2nd Quarter 2003, PM's Wholesale Leaders ("WL") program gave a 2.75% gross discount on PM products to direct distributors. It also paid back-end money (i.e., quarterly rebates) conditioned on the wholesaler's achieving market share-based sales quotas of PM brands. Thus, a distributor's sales of PM brands compared with non-PM brands determined its rebate, and the best back-end monies were paid for achieving PM share percentages which could go as high as 58.9%. In other words, PM's WL program rewards distributors based on their sales of PM cigarettes as a percentage of their total cigarette sales.

Effective 3rd Quarter 2003, PM unilaterally revised its wholesale pricing structure by establishing a three-level pricing system, ranging from Level 1 (the least favored) to Level 3 (the most favored), that based both price discounts and back-end monies on a market share comparison. A share-based component also remains part of WL 2004. WL's per carton price differences between the worst and best price from 2nd Quarter 1999 to present were as follows:

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<sup>1</sup> Given this Court's conclusion that PM's WL program violates neither the [Robinson-Patman Act](#) nor the [Sherman Act](#), the preliminary injunction was improvidently granted.

<b>Effective Date</b>	<b>Maximum Price Difference</b>
2nd Quarter 1999 -- 2nd Quarter 2000	\$ 0.23
3rd Quarter 2000 -- 1st Quarter 2002	\$ 0.30
2nd Quarter 2002 -- 2nd Quarter 2003	\$ 0.32
3rd Quarter 2003	\$ 0.81
4th Quarter 2003	\$ 0.55 (post injunction)
1st Quarter 2004 -- present	\$ 0.24

[\*7]

PM's highest share (Level 3) quotas and its most favored prices have never been achieved by the plaintiffs.

### **ROBINSON PATMAN/ACT CONCLUSIONS OF LAW**

Plaintiffs' price discrimination claim is brought under Section 2(a) of the Robinson-Patman Act, [15 U.S.C. § 13\(a\)](#). **HN1** To establish a *prima facie* case under [Section 2\(a\)](#), plaintiffs must prove that: (1) PM's cigarette sales to plaintiffs and their competitors are "in interstate commerce"; (2) the sales involve PM cigarettes of "like grade and quality"; (3) the sales discriminate in prices <sup>2</sup> among these competing distributors; and (4) the discrimination substantially lessens competition and causes antitrust injury to plaintiffs. [Schwartz v. Sun Co., Inc., 276 F. 3d 900, 903-904 \(6th Cir.2002\)](#). Plaintiffs seek damages for claimed loss of profit, customers, sales, goodwill and business value that resulted from PM's allegedly discriminatory pricing. Plaintiffs further seek permanent injunctive relief against this alleged discrimination. The State of Mississippi is seeking injunctive relief on behalf of its consumers, wholesalers, and manufacturers and to prevent alleged injury [\*8] to the economy of the state.

PM contends that summary judgment on plaintiffs' [Robinson- Patman Act](#) claims is appropriate in this case because PM's discounts are functionally available to the plaintiffs. **HN2** If the best prices are "available equally and functionally to all customers", then no price discrimination has occurred. [Federal Trade Commission v. Morton Salt Co., 334 U.S. 37, 68 S. Ct. 822, 92 L. Ed. 1196, 44 F.T.C. 1499 \(1948\)](#); [Bouldis v. U.S. Suzuki Motor Corp., 711 F.2d 1319 \(6th Cir. 1983\)](#). The plaintiffs contend that summary judgment is inappropriate in this case because issues of material fact remain in regard to whether or not the defendant's discounts are functionally available for several reasons:

1. PM's data demonstrate that its best price is not available to all or most distributors,
2. PM's best price is unattainable because distributors do not control consumer demand,
3. Plaintiffs do everything asked of them to sell PM [\*9] products,
4. PM's share quotas are inherently unachievable, and
5. Plaintiffs must sell 4th tier and other competitor cigarettes to retain their business.

Plaintiffs appear to concede that PM's discounts are theoretically available to them but argue that the "choices" they must make to take advantage of PM's best prices "could potentially destroy their businesses". They argue that [Section 2\(a\)](#) does not require them "to change their business structure, reconfigure their customer base, or adopt an expensive and risky business plan in an effort" to achieve the best prices.<sup>3</sup>

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<sup>2</sup> Simply put, this means a difference in price.

<sup>3</sup> The Court notes that such is the essence of a competitive economic system. Businesses that wish to succeed and gain market advantage over their competitors must make such choices everyday. Some flourish, some fail, but such is the nature of competition.

**HN3**[] The use of the functional availability theory to demonstrate the lack of an essential element of the plaintiffs' case, i.e. price discrimination, is technically not an affirmative [\*10] defense, but the negation of an element of the plaintiff's case. See [\*Metro Ford Truck Sales, Inc. v. Ford Motor Co.\*, 145 F.3d 320, n. 17 \(5th Cir.1998\)](#). **HN4**[] If an essential element of the plaintiff's case is negated, summary judgment is appropriate.

The theory of "functional availability" is explained by the Sixth Circuit in [\*Bouldis v. U.S. Suzuki Motor Corp.\*, 711 F.2d 1319, 1326 \(6th Cir. 1983\)](#):

**HN5**[] The practice of conditioning price concessions and allowances upon the customer's purchase of a specific quantity of goods will not give rise to a Robinson-Patman violation if the concessions are available equally and functionally to all customers. See [\*Federal Trade Comm. v. Morton Salt Co.\*, 334 U.S. 37, 42, 68 S. Ct. 822, 826, 92 L. Ed. 1196, 44 F.T.C. 1499 \(1948\)](#); [\*Shreve Equipment, Inc. v. Clay Equipment Corp.\*, 650 F.2d 101, 105 \(6th Cir.\)](#), cert. denied, 454 U.S. 897, 102 S. Ct. 397, 70 L. Ed. 2d 213 (1981); [\*Mowery v. Standard Oil Company of Ohio\*, 463 F. Supp. 762, 775-76 n. 17 \(N.D.Ohio 1976\)](#), aff'd without opinion, 590 F.2d 335 (6th Cir.1978). See generally 16C Von Kalinowski, BUSINESS [\*11] ORGANIZATIONS § 27.04 (1982). Further, a claim of price discrimination will not lie if the buyer failed to take advantage of a price concession which was realistically and functionally available. See [\*Shreve Equipment, Inc., supra\*, 650 F.2d at 105](#). The legislative history reveals that the aim of the Act is to prevent a large buyer from gaining discriminatory preferences over the small buyer solely because of the large buyer's greater purchasing power. See [\*Federal Trade Comm. v. Henry Broch & Co.\*, 363 U.S. 166, 168-69, 80 S.Ct. 1158, 1160-61, 4 L. Ed. 2d 1124 \(1960\)](#); [\*Morton Salt Co.\*, \*supra\*, 334 U.S. at 43, 68 S. Ct. at 826](#).

In *Bouldis*, the district court found that Suzuki's various promotional concessions and allowances were practically and realistically available to Bold-Morr, Inc., a former Suzuki motorcycle dealership whose officers and sole stockholders were Pete Bouldis and Norman Morris. In addition, the testimony of Bouldis revealed that he had cash flow and inventory problems at times which prevented him from participating in the promotional sales. Therefore, the Sixth Circuit found that, by his own admission, there [\*12] was no causal link between Suzuki's practices and Bouldis' alleged injuries but rather his inability to participate was attributable to his own business problems. The Sixth Circuit concluded that conditioning price concessions and allowances on the purchase of a specific quantity of goods is allowed if concessions were made available equally and functionally to all customers. *Id.*

Several other circuits have addressed the "availability" theory as well. In [\*Edward J. Sweeney & Sons Co. v. Texaco, Inc.\*, 637 F.2d 105 \(3d Cir. 1980\)](#), the Third Circuit found that customer pickup allowances from the seller's uniform zone delivered pricing system based upon the distance from the seller's delivery point was nondiscriminatory because it was available to all customers using a nondiscriminatory formula, even though different customers paid different prices. The Fifth Circuit found, in [\*Metro Ford Truck Sales\*, 145 F.3d at 326](#), that price discrimination did not exist, and that no violation of the *Robinson-Patman Act* occurred, because Metro was treated the same as all other Ford dealers with respect to the CPA program for the same customer and products of like [\*13] grade and quality. In [\*Comcoa, Inc. v. NEC Tel., Inc.\*, 931 F.2d 655 \(10th Cir. 1991\)](#), the Tenth Circuit found that there could be no recovery if the challenged discount was functionally available to the plaintiff and the program was evenly administered.

**HN6**[] To the extent that there is an "availability" defense, it will fail if the lower price is not "practically" available to all competing customers. Discounts must be available not only in theory but in fact to be practically available. See [\*FLM Collision Parts, Inc. v. Ford Motor Co.\*, 543 F.2d 1019, 1025-26 \(2d Cir. 1976\)](#). ("equal opportunity" is required; "even when a seller has a dual pricing system, if the lower price is available to all purchasers, not only in theory but in fact, there is no violation of [§ 2\(a\)](#)")

**HN7**[] Discounts that have been held to not be functionally available because they were discounts in theory but not in fact are:

1. Quantity discounts. See [\*FTC v. Morton Salt Co.\*, 334 U.S. 37, 92 L. Ed. 1196, 44 F.T.C. 1499 \(1948\)](#) (holding that quantity discounts are not functionally available to many small buyers);

2. When the purchaser was not told about the discount. See [\*Caribe BMW, Inc. v. Bayerische Motoren Werke, 19 F.3d 745 \(1st Cir. 1994\)\*](#) [\*14] (favorable prices not practically available if the buyer was not told that it would receive the same prices as customers purchasing from different facility of supplier should buyer agree to purchase from that facility); and

3. When the purchaser was not permitted to participate in the program. See [\*DeLong Equip. Co. v. Washington Mills Abrasive Co., 887 F.2d 1499 \(11th Cir. 1989\)\*](#) (recognizing the validity of the availability defense, but finding it inapplicable because the plaintiff was not given the opportunity to buy the lower-priced item).

None of these examples apply to the plaintiffs' situation because this case does not involve a quantity discount, the plaintiffs were told about the discount, and the plaintiffs were permitted to participate in the program. The Court FINDS that PM's discount is available to all customers using a nondiscriminatory formula, even though different customers may pay different prices, and that there is no evidence that the program was not evenly administered. Therefore, the Court FINDS that PM's discount was functionally available to the plaintiffs in both theory and in fact. That plaintiffs may be faced with difficult business choices, [\*15] and even that some may go out of business, makes little difference and does not create a genuine issue of material fact in this case. [HN8](#) ↑ The antitrust laws were never intended to protect individual competitors. See [\*Conwood Co., L.P. v. U.S. Tobacco Co., 290 F.3d 768, 769 \(6th Cir. 2002\)\*](#), cert. denied, 537 U.S. 1148, 123 S. Ct. 876, 154 L. Ed. 2d 850 (2003). Each of the individual plaintiffs may choose to make these difficult decisions or to do nothing at all; nevertheless, the choice is theirs. PM does not dictate the choices these wholesalers make.

The plaintiffs cite [\*Caribe, 19 F.3d at 752\*](#), for the proposition that "plaintiff need not give up the advantages of its importer's contract in order to obtain the most favorable price." However, *Caribe* really states:

The emphasized language says that Caribe did not know that its competitors were receiving favored treatment. And, we do not see how ordinarily one could say that a seller has made favored treatment "available" to a disfavored customer if the disfavored customer does not know about the favored treatment. See, e.g., [\*Alterman Foods, Inc. v. F.T.C., 497 F.2d 993, 1001 \(5th Cir. 1974\)\*](#); [\*16] [\*Mueller Co. v. F.T.C., 323 F.2d 44, 46-47 \(7th Cir. 1963\)\*](#), cert. denied, 377 U.S. 923, 84 S. Ct. 1219, 12 L. Ed. 2d 215 (1964); [\*Century Hardware Corp. v. Acme United Corp., 467 F. Supp. 350, 355-56 \(E.D. Wis. 1979\)\*](#).

Caribe also argues that the favored treatment, as a practical matter, was not "available" because BMW AG insisted that it give up various advantages of its importer's contract in order to obtain it. We cannot tell from the complaint, however, just what those advantages were and how they related to the practical "availability" of the favorable treatment given other retailers. Thus, we cannot say, at this time, whether or not Caribe will be able to prove that the favorable price and terms, as a practical matter, were not available. At this stage, however, Caribe has sufficiently alleged that they were not.

Our conclusion is that Caribe's complaint states a valid [\*Robinson-Patman Act\*](#) claim, in respect to price discrimination under [\*Robinson-Patman Act § 2\(a\)\*](#), and for similar reasons, under the [\*Robinson-Patman Act\*](#) sections that deal with payments for services, furnishing services, and brokerage payments. [15 U.S.C. § 13](#) [\*17] [\*\(b\), \(d\)-\(e\)\*](#). Although Caribe's pleadings regarding these other [\*Robinson-Patman Act\*](#) sections are rather sparse, they are sufficient to give BMW AG and BMW NA notice of the substance of Caribe's complaint. (emphasis added)

*Id. at 752*. Therefore, Caribe does not hold what the plaintiffs assert but merely addresses the sufficiency of the complaint.

The plaintiffs also cite [\*National Dairy Products Corp. v. F.T.C., 395 F.2d 517, 523 \(7th Cir. 1968\)\*](#) for the proposition that "the [\*Robinson-Patman Act\*](#) does not force [plaintiffs] to sacrifice their independence' in order to receive the highest discounts." *National Dairy* was a proceeding on a petition of a dairy product distributor to set aside an order and decision of the Federal Trade Commission. The Seventh Circuit held that where a dairy product distributor operated in 35 states and it was typical to have volume discount schedules in effect at various operations, the order of the Federal Trade Commission requiring it to cease from unlawful price practices was not an abuse of discretion

in view of the showing that the practices had occurred in widespread areas over a long period of time. The Seventh [\*18] Circuit concluded:

We also cannot accept National's argument that the disfavored independents should have joined voluntary or cooperative groups and thus obtained higher discounts. *The Robinson-Patman Act* does not force them to sacrifice their independence. One of the reasons for its enactment was to protect the independents from the chains and other large buying groups. *Federal Trade Commission v. Anheuser-Busch, Inc.*, 363 U.S. 536, 543-544, 80 S. Ct. 1267, 4 L. Ed. 2d 1385; Rowe, Price Discrimination Under the Robinson-Patman Act (1962), pp. 11-23.

*Id. at 523.*

The Court FINDS that *National Dairy* is not on point with this case because that case involved volume discounts and there has been no suggestion or requirement by PM that these plaintiffs join voluntary or cooperative groups and sacrifice their independence.

In addition, the plaintiffs cite *Calumet Breweries, Inc. v. G. Heileman Brewing Co., Inc.*, 951 F. Supp. 749 (N.D.Ind. 1994), in which a beer wholesaler brought an action challenging the legality of a brewer's quantity discount program. The Court in *Calumet* stated:

Moreover, the evidence tends [\*19] to discount Heileman's contention that it would be a reasonable business decision for Calumet, because of its physical storage capacities and economic resources, to purchase enough beer to obtain the maximum discount. Heileman argues that Calumet does not do so because it has decided to maximize sales of competing brands, such as Anheuser-Busch, rather than aggressively promoting sales of Heileman products. According to Heileman, Calumet should compete with Central by structuring its purchases: obtaining the maximum discount by buying more than a month's supply of beer, warehousing it, and then selling from inventory in the following month(s). Nothing in the *Robinson-Patman Act* or the cases interpreting it suggests that Calumet's decision to emphasize other brands and remain a (relatively) small seller of Heileman products ipso facto means Heileman may charge Calumet a higher price:

The legislative history of the *Robinson-Patman Act* makes it abundantly clear that Congress considered it to be an evil that a large buyer could secure a competitive advantage over a small buyer solely because of the large buyer's quantity purchasing ability. *The Robinson-Patman Act* was passed [\*20] to deprive a large buyer of such advantages except to the extent that a lower price could be justified by reason of a seller's diminished costs due to quantity manufacture, delivery or sale, or by reason of a seller's good faith effort to meet a competitor's equally low price. *Morton Salt*, 334 U.S. at 43, 68 S. Ct. at 826. (emphasis added)

*Id. at 755.*

*Calumet* is also not on point with this case because this case does not involve volume discounts which permit a large buyer to secure a competitive advantage over a small buyer because of the large buyer's quantity purchasing ability.

Therefore, the cases cited by the plaintiffs stand for the proposition that the plaintiffs do not have to alter their independent purchasing status to receive the discount. Not one of the cases cited by the plaintiffs addresses plaintiffs' selling status nor supports plaintiffs' assertion that Section 2(a) does not require plaintiffs to change their business structure, reconfigure their customer base, or undertake an expensive and risky business plan.

Although the plaintiffs contend that PM's discounts are not functionally available to them because of the [\*21] demands of their customers, applicable HNG[] case law does not support the plaintiffs' conclusion that the demands of a purchaser's customer can render a discount functionally unavailable. Courts have refused to find discrimination when the buyer's inability to take advantage of the best discount was within the control of the buyer,

such as poor credit, management choices, decisions not to hold inventory, or particular marketing strategies. See *Bouldis*, 711 F.2d at 1327; *Shreve*, 650 F.2d at 105; *Edward J. Sweeney*, 637 F.2d at 121; *Chapman v. Rudd Paint & Varnish Co.*, 409 F.2d 635, 643 (9th Cir. 1969).

The Court FINDS that the undisputed fact that an outside influence, not in the control of PM, i.e. plaintiffs' customer demands, frustrated their performance does not render the discounts under PM's WL program functionally unavailable. Therefore, because PM's discount is functionally available under the undisputed facts of this case, the defendant has demonstrated the lack of an essential element of the plaintiffs' case, i.e. price discrimination, and PM is entitled to summary judgment on plaintiffs' *Robinson-Patman Act* claims.

[\*22] In this case, the Court also FINDS that there is no causal link between PM's practices and the plaintiffs' alleged injuries. Plaintiffs contend that they did not make a voluntary choice to emphasize fourth-tier or other non-PM brand over PM's products, but that they have simply responded to the demands of their customers. Therefore, by their own admission, the plaintiffs' inability to participate in WL is attributable to an outside influence over which PM had no control. In effect, the plaintiffs seek to reap the rewards of the WL without furthering the purpose of that program, i.e., increasing the demand for PM products.

The Court FINDS that, because the plaintiffs did not take advantage of a lower price or discount which was functionally available on an equal basis, no price discrimination has occurred. In the alternative, the Court FINDS that any alleged discrimination was not the proximate cause of the plaintiffs' complained of injuries.

## **SHERMAN ACT/CONCLUSIONS OF LAW**

In addition to their claims under the *Robinson-Patman Act*, plaintiffs also allege that PM has engaged in an actionable attempt to monopolize in violation of the *Sherman Act*. HN10[] A claim for attempted [\*23] monopolization under § 2 of the Sherman Act, *15 U.S.C. § 2*, requires: (1) a specific intent to monopolize; (2) anti-competitive conduct; and (3) a dangerous probability of success. *Tarrant Service Agency, Inc. v. American Standard, Inc.*, 12 F.3d 609 (6th Cir. 1993) Because plaintiffs cannot show genuine issues of material fact as to these three necessary elements, summary judgment will also be granted to defendant on plaintiffs' *Sherman Act* claim.

## **DANGEROUS PROBABILITY OF SUCCESS**

### **Market Power**

The United States Supreme Court has held that HN11[] market power is a necessary element for showing a dangerous probability of achieving monopoly power in an attempt to monopolize case. *Spectrum Sports v. McQuillan*, 506 U.S. 447, 457, 113 S. Ct. 884, 891, 122 L. Ed. 2d 247 (1993). In determining whether there is a dangerous probability of monopolization, courts have considered the relevant market and the defendant's ability to lessen or to destroy competition in that market. *Id.*

HN12[] An attempt to monopolize claim requires "proof of market power", *Id. at 457*, and market power is "the power [\*24] to control prices or exclude competition." *United States v. Grinnell Corp.*, 384 U.S. 563, 571, 16 L. Ed. 2d 778, 86 S. Ct. 1698 (quoting *United States v. E. I. du Pont De Nemours & Co.*, 351 U.S. 377, 391, 100 L. Ed. 1264, 76 S. Ct. 994 (1956)) HN13[] An analysis of market power requires that the court, focus on the ability of a single seller to unilaterally raise prices and restrict output. *Spectrum Sports at 457*; *Virgin Atlantic Airways, LTD. v. British Airways*, 257 F.3d 256 (2nd Cir. 2001); *Rebel Oil Co., Inc. v. Atlantic Richfield Co.*, 51 F.3d 1421 (9th Cir. 1995)

Plaintiffs assert that PM's "high market share is strong evidence of monopoly power" and argue that PM's dollar share of the cigarette market (56%) makes it the dominant company in the United States cigarette industry. This

alone, according to plaintiffs, is sufficient to defeat summary judgment. PM's market share based on units sold has been calculated by plaintiffs at 49.6%.

Plaintiffs' position, however, has been expressly rejected by the Sixth Circuit Court of Appeals. [HN14](#)[] Market share, standing alone, is insufficient to establish market power as a matter of law and is only the starting [\*25] point for determining whether monopoly power exists. "The inference of monopoly power does not automatically follow from the possession of a commanding market share." [\*American Counsel of Certified Podiatric Physicians and Surgeons v. American Board of Podiatric Surgery, Inc.\*, 185 F.3d 606, 623 \(6th Cir. 1999\)](#) (quoting [\*Byars v. Bluff City News Co.\*, 609 F.2d 843, 850-851 \(6th Cir. 1979\)](#)). See also [\*Richter Concrete Corp. v. Hilltop Concrete Corp.\*, 691 F.2d 818 \(6th Cir. 1982\)](#) PM's market share, standing alone, is therefore insufficient to establish market power as a matter of law.

Plaintiffs also suggest that PM's market share "likely understates its market power" since PM and RJR have a combined market share of about 83% and have very similar "exclusionary" programs. It is improper, however, to combine PM's market share with RJR's market share in determining whether or not PM has market power. [\*Arthur S. Langenderfer, Inc. v. S.E. Johnson Co.\*, 917 F.2d 1413 \(6th Cir. 1990\)](#) Plaintiffs have alleged no facts in this case which would suggest, and have not established, that PM and RJR have entered into any conspiracy [\*26] such as would justify a combined share approach to determining market power. In short, plaintiffs have produced no evidence to show that PM's market share translates into market power.

Plaintiffs also assert that there is direct evidence that PM has monopoly power "as shown by its ability to exclude rivals and control price." In support of their assertion, plaintiffs point to certain affidavits and exhibits in which plaintiffs contend that PM's WL program has undermined their competitiveness and increased their costs of distribution. Plaintiffs also assert that PM's ability to control prices is "demonstrated by the pricing of its premium cigarettes at almost five times the level of 4th tier products, its high product margins and inelastic demand for its products." This Court has already found that PM's conduct with respect to its WL program of market share discounts is not illegal or anti-competitive but is rather a valid business reaction to market pressures. Also, as pointed out by PM, the fact that PM prices its cigarettes at almost five times the level of 4th tier brands does not demonstrate PM's ability to unilaterally control the price. While this Court has considerable sympathy [\*27] with the plaintiffs in this case and the effects the WL program may have on their businesses, it is well established that [HN15](#)[] "competition is a ruthless process . . . and the anti-trust laws are not a balm for the rivals' wounds." [\*Tennessee Truck Stop, Inc. v. NTS, Inc.\*, 875 F.2d 86, 90 \(6th Cir. 1989\)](#) (quoting [\*Ball Memorial Hospital, Inc. v. Mutual Hosp. Ins., Inc.\*, 784 F.2d 1325, 1338 \(7th Cir. 1986\)](#)) [HN16](#)[] It is also well established that the anti-trust laws are designed to protect competition, not individual competitors. [\*Conwood\*, 290 F.3d at 788](#). Simply put, there is no evidence, direct or indirect, in this record that PM has monopoly power.

#### **Low barriers to entry**

The parties in this case apparently agree that entry into the U. S. cigarette market is relatively easy and that numerous new manufacturers and brands have entered the industry and successfully captured market share over the last few years.<sup>4</sup> "The difficulty of entry into the market is relevant because if entry is easy, even a firm holding a commanding percentage of the market cannot charge a price above the competitive price, for once it does, competitors [\*28] will enter the market and undercut the firm's price." [\*American Counsel of Certified Podiatric Physicians and Surgeons at 623\*](#). Plaintiffs respond to PM's argument that such actual entry "is a strong indicator" that PM lacks market power by arguing that such entry "has not constrained premium cigarette pricing" and asserts that "the fringe 4th tier manufacturers have been limited by punitive state legislation and restricted access to efficient distribution channels as spearheaded by PM and RJR." This Court fails to see how such arguments by the plaintiffs can overcome the undisputed evidence of ease of entry by competitors into the U. S. cigarette market, and both parties agree that the relevant market at issue in this case is the United States cigarette market, not just the market for premium cigarettes.

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<sup>4</sup> Since the Master Settlement Agreement of 1998, dozens of new cigarette manufacturers have entered the market and have captured approximately 15% of the market despite an overall significant decline in U.S. cigarette sales over the last 20 years.

[\*29] **Excess capacity**

**HN17** [↑] A firm also lacks market power when its competitors have excess capacity. Excess capacity is the ability of existing competitors to expand output to counteract a reduction in output by a provider with a large market share. Excess capacity inhibits monopoly pricing because consumers can obtain the product or service at competitive pricing from another provider. Excess capacity deprives a relatively large "market share" of its normal "market power." [Rebel Oil Co. at 1441](#). Two of PM's competitors, RJR and Lorillard, with a combined market share of less than 30%, together have the capacity to produce nearly 50% of the 400 billion cigarettes consumed in the United States in 2003. Plaintiffs respond to PM's argument by arguing that the excess capacity "resides primarily in PM and RJR" who have an "oligopoly strategy" of "supracompetitive" pricing. Plaintiffs ignore the fact that two of PM's competitors have nearly one-half of all excess capacity and that, as discussed by the Court above, market power is the ability of a single seller to raise prices and restrict output. Plaintiffs have presented no evidence that PM has the ability to control any [\*30] other firm's production capacity or that PM can raise prices above competitive levels without rival manufacturers simply increasing output.

In summary, after examining barriers to entry, excess capacity, and PM's market share, plaintiffs have not established that there is a genuine issue of material fact as to whether or not PM has sufficient market power to establish a dangerous probability of success. See *Ford v. Stroup*, 113 F.3d 1234, 1997 WL 201560 (6th Cir. (Tenn.)) PM is, therefore, entitled to summary judgment for this reason alone.

**ANTI-COMPETITIVE CONDUCT WITH THE SPECIFIC INTENT TO MONOPOLIZE**

As the Sixth Circuit has observed:

**HN18** [↑] Anticompetitive conduct is conduct designed to destroy competition, not just to eliminate a competitor. Lively legal competition will result in the efficient and shrewd businessman routing the inefficient and imprudent from the field. The anti-trust laws must be administered in such a way that they do not restrain such vigorous competition in order to protect inefficient competitors. As Judge Learned Hand has pointed out, "The successful competitor, having been urged to compete, must not be turned on [\*31] when he wins" [United States v. Aluminum Co. of America](#), 148 F.2d 416, 430 (2nd Cir. 1945). Merely to attempt to succeed in business is not anti-competitive conduct.

[Richter Concrete Corp. at 823](#).

Plaintiffs argue that PM's WL programs are exclusionary and anti- competitive and that specific intent to monopolize "can be inferred from the defendant's anti-competitive practices." Plaintiffs are correct that **HN19** [↑] specific intent to monopolize may be inferred from evidence of anti-competitive conduct, see [Lorain Journal Co. v. United States](#), 342 U.S. 143, 153, 96 L. Ed. 162, 72 S. Ct. 181 (1951), but not from legitimate business practices aimed only at succeeding in competition. [Times-Picayune Publishing Co. v. United States](#), 345 U.S. 594, 626, 97 L. Ed. 1277, 73 S. Ct. 872 (1952). **Antitrust law** protects competition, not particular competitors. [Spectrum Sports at 458-459](#). Whether conduct is anti-competitive for purposes of Section 2 of the Sherman Act, [15 U.S.C. § 2](#), depends on "whether 'valid business reasons' can explain [defendants'] actions." [Eastman Kodak Co. v. Image Technical Servs.](#), 504 U.S. 451, 483, 119 L. Ed. 2d 265, 112 S. Ct. 2072 (1992). [\*32]

The inference claimed by plaintiffs here, however, is unavailable to them because they have been unable to establish that PM's WL program has anti-competitive effect. In fact, plaintiffs have been unable to establish that WL decreases rather than increases competition. At best, plaintiffs' proof establishes only harm to individual competitors, not harm to competition. Plaintiffs have failed to present evidence that creates a genuine issue of material fact to support their allegation that WL has foreclosed any cigarette manufacturer from access to the relevant market.

The relative lack of difficulty of entry into the U.S. cigarette industry likewise negates plaintiffs' claim of anti-competitive conduct. Were PM to charge a price above the competitive price for its products, this record establishes

that either existing competitors (RJR and Lorillard) or new competitors would enter the market (or increase production) and undercut PM's price. As indicated above, RJR and Lorillard together possess about fifty percent (50%) of the excess capacity for production of cigarettes and dozens of new manufacturers have entered the market since 1998. PM's WL program is a valid business reaction [\*33] to market pressure brought about by increased competition for a declining cigarette market. Moreover, these plaintiffs admit that, were they to choose to discontinue sales of fourth tier brands altogether in order to achieve PM's best discounts, those brands would immediately be picked up by a competing distributor.

Thus, not only have plaintiffs not established a genuine issue of material fact on the issue of whether PM possesses sufficient market power to establish a dangerous probability of monopolization, no genuine issue of material fact exists on the issues of whether or not PM has engaged in anti-competitive conduct with the specific intent to monopolize. PM is likewise entitled to summary judgment on these grounds.

### **Antitrust Injury**

As set forth throughout this memorandum opinion, plaintiffs also cannot establish an "injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendant's acts unlawful." [Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701\(1977\)](#). Plaintiffs surely have suffered harm but such harm does not result from a decrease in competition [\*34] rather than some other consequences of PM's WL program. Their injuries, therefore, are not injuries which the antitrust laws were intended to prevent.

An appropriate order shall issue.

ENTER:

Date: 8/16/05

s/ J. RONNIE GREER

UNITED STATES DISTRICT JUDGE

### **ORDER**

For the reasons set out in the Memorandum Opinion that accompanies this order, it is hereby **ORDERED** that that the Motion for Summary Judgment filed by the defendant, Philip Morris USA, Inc., is **GRANTED**, [Doc. 176], and the plaintiffs' complaint as well as the intervening complaint if the State of Mississippi is **DISMISSED**.

On August 6, 2003, this Court entered a preliminary injunction on behalf of the plaintiffs, the entry of which was appealed by Philip Morris USA and which is the subject of Court of Appeals Docket No. 03-6025 in the United States Court of Appeals for the Sixth Circuit. This Court's order provided that this injunction would remain in effect during the pendency of this lawsuit. In view of the dismissal of the plaintiffs' complaint by this order, it is also hereby **ORDERED** that the preliminary injunction entered by the Court on August 6, 2003 is **VACATED**. [Doc. [\*35] 67]. The defendant's motion for a hearing and request for oral argument is **DENIED**. [Doc. 178].

ENTER:

Date: 8/16/05

s/ J. RONNIE GREER

UNITED STATES DISTRICT JUDGE



## **Guichard v. Mandalay Pictures, LLC**

United States District Court for the Northern District of California

August 22, 2005, Decided; August 22, 2005, Filed

No. C 04-4363 JSW

### **Reporter**

2005 U.S. Dist. LEXIS 45410 \*; 2005 WL 2007883

ROBERT GUICHARD, Plaintiff, v. MANDALAY PICTURES, LLC. d/b/a MANDALAY ENTERTAINMENT, METRO-GOLDWYN-MAYER STUDIOS, INC., et al., Defendants.

**Subsequent History:** Subsequent appeal at [\*Guichard v. Mandalay Pictures LLC, 143 Fed. Appx. 818, 2005 U.S. App. LEXIS 19784 \(9th Cir. Cal., 2005\)\*](#)

## **Core Terms**

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motion picture, antitrust, Studio, Defendants', Pictures, pleadings, registration, trademark, alleges, Sherman Act, registered, screenplay, producing, rights, amend, motion for judgment, motion to dismiss, relevant market, contends, film

**Counsel:** [\*1] Robert Guichard, Plaintiff, Pro se, San Francisco, CA.

For Mandalay Pictures, LLC, doing business as Mandalay Entertainment, Defendant: David Aaron Grossman, LEAD ATTORNEY, Jacques M. Rimokh, Loeb & Loeb LLP, Los Angeles, CA.

For Metro-Goldwyn-Mayer Studios, Inc., Defendant: David Aaron Grossman, LEAD ATTORNEY, Jacques M. Rimokh, Loeb & Loeb LLP, Los Angeles, CA; Thomas R. Burke, Davis Wright Tremaine LLP, San Francisco, CA.

For Motion Picture Association of America, Paramount Pictures Corporation, Sony Pictures Entertainment Inc., Twentieth Century Fox Film Corporation, Universal City Studios LLP, Walt Disney Pictures and Television Inc., Warner Bros. Entertainment, Inc., Defendants: Henry James Tashman, Thomas R. Burke, LEAD ATTORNEYS, Davis Wright Tremaine LLP, Los Angeles, CA.

**Judges:** JEFFREY S. WHITE, UNITED STATES DISTRICT JUDGE.

**Opinion by:** JEFFREY S. WHITE

## **Opinion**

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### **ORDER GRANTING MPAA DEFENDANTS' MOTION TO DISMISS AND STUDIO DEFENDANTS' MOTION FOR JUDGMENT ON THE PLEADINGS**

Now before the Court is the motion by Defendants Motion Picture Association of America, Inc., erroneously named as MPAA; Sony Pictures Entertainment Inc.; Warner Bros. Entertainment, Inc.; Walt Disney Pictures and Television, erroneously named [\*2] as Buena Vista Pictures Distribution; Paramount Pictures Corporation; Twentieth Century Fox Film Corporation; and Universal Studios LLLP (collectively "MPAA Defendants") to dismiss Plaintiff's First Amended Complaint ("FAC") for failure to state a claim under [\*Federal Rule of Civil Procedure 12\(b\)\(6\)\*](#).

Also before the Court is the motion by Defendants Metro-Goldwyn-Mayer Studios, Inc. ("MGM") and Mandalay Pictures LLC ("Mandalay") (collectively "Studio Defendants") for judgment on the pleadings on the fifth sixth, seventh and eighth claims pursuant to [Federal Rule of Civil Procedure 12\(c\)](#).

Having carefully read the parties' papers and considered the arguments and the relevant legal authority, the Court hereby GRANTS the MPAA Defendants' motion to dismiss without leave to amend on all claims pending against them and GRANTS the Studio Defendants' motion for judgment on the pleadings on the fifth sixth, seventh and eighth claims against them.

## BACKGROUND

In his initial complaint filed on October 15, 2004, Plaintiff named only the Studio Defendants and asserted claims for trademark infringement under the Lanham Act, [15 U.S.C. § 1125\(a\)](#), for breach of confidentiality, common law misappropriation, [\*3] and violations of [California Business and Professions Code § 17200](#). In his amended complaint filed December 13, 2004, Plaintiff named the MPAA Defendants for the first time and added claims against them and the Studio Defendants for violation of the Sherman and Cartwright Acts, as well as for violation of the [California Business and Professions Code § 17200](#). Plaintiff alleges that Defendant Motion Picture Association of America is a "trade association of the American film industry" and the other MPAA Defendants are six of the seven members of the Association. (FAC, P 30.) Plaintiff alleges that MPAA members constitute a majority of the United States theatrical motion picture production and distribution markets. (FAC, PP 31, 43.)

Plaintiff alleges that in 1925 the MPAA established the Title Registration Bureau ("TRB") that functions as the central registration bureau for titles of motion pictures in the United States. (FAC, P 32.) The TRB promulgates a set of rules ("TRB Rules") which require all members to register their titles for theatrical motion pictures prior to their release. (FAC, P 32; TRB Rules §§ 2.2.3, 3.1 (attached to Motion Brief as Appendix 1).) TRB members are prohibited [\*4] from using a particular title unless they have priority granted by prior registration. (FAC, P 36; TRB Rules § 5.1.2.) Once a title is registered, an identical title cannot be used for a theatrical motion picture by any other MPAA member or signatory without a waiver from the initial title registrant. (FAC, P 36, TRB Rules § 4.3.) The MPAA members all participate in the TRB, although the TRB is open to non-members if they sign an agreement to join, agree to follow the TRB Rules, and pay an annual fee. (FAC, P 30; TRB Rules §§ 2.2.4, 2.4.1.)

Plaintiff contends that he wrote a screenplay in 1993 called "Into The Blue," an underwater action and adventure story about searching the waters off Florida and the Bahamas for a sunken ship and treasure. (FAC, PP 21-22.) Plaintiff contends that in 1997 he submitted his screenplay to Mandalay who declined to pursue its production. (FAC, PP 24-25.) Plaintiff claims that the Studio Defendants misappropriated his title, ideas, and elements of the screenplay by making a similar motion picture and improperly registered the title with the TRB when they knew, or should have known, that the title belonged to Plaintiff. (FAC, PP 60-61.) In 1999, Plaintiff [\*5] changed the title of his screenplay to "In2Blue" and claims still to be developing and producing his theatrical motion picture based on his original script. (FAC, P 21, 5.)

According to Plaintiffs complaint, Defendant Mandalay registered the title "Into The Blue" with the TRB in June 2002 and on MGM registered the identical title in May 2003. (FAC, PP 34, 35.) Also, in 2003, Mandalay waived its rights to the title with the TRB, thereby putting MGM in priority position. (FAC, P 36.) Plaintiff contends that the prior registrations of the motion picture title preclude Plaintiff from having the member studios produce his screenplay without receiving a waiver from MGM. (FAC, P 37.) He claims that the TRB Rules function as a monopoly and unreasonable restraint of trade in violation of the Sherman Act, as well as the Cartwright Act and [California Business and Professions Code § 17200](#).

## ANALYSIS

### A. Legal Standard on Motion to Dismiss.

A motion to dismiss for failure to state a claim will be denied unless it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him or her to relief. [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#). All allegations of material fact are [\*6] taken as true and construed in the light most favorable to the nonmoving party. [Cahill v. Liberty Mut. Ins. Co., 80 F.3d 336, 337-38 \(9th Cir. 1996\)](#). Dismissal is proper only where there is no cognizable legal theory or an absence of sufficient facts alleged to support a cognizable legal theory. [Navarro v. Block, 250 F.3d 729, 732 \(9th Cir. 2001\)](#). The Court is not, however, bound to accept as true conclusory allegations of law or legal conclusions couched as a factual allegation. [Papasan v. Allain, 478 U.S. 265, 286, 106 S. Ct. 2932, 92 L. Ed. 2d 209 \(1986\); Arpin v. Santa Clara Transp. Agency, 261 F.3d 912, 923 \(9th Cir. 2001\)](#) (internal quotation omitted). For private antitrust claims, if the facts "do not at least outline or adumbrate a violation of the Sherman Act, the plaintiffs will get nowhere merely by dressing them up in the language of antitrust." [Rutman Wine Co. v. E&J Gallo Winery, 829 F.2d 729, 736 \(9th Cir. 1987\)](#). A claimant must, at a minimum, sketch the outline of the antitrust violation with allegations of supporting factual detail. [Les Shockley Racing, Inc. v. National Hot Rod Ass'n, 884 F.2d 504, 508 \(9th Cir. 1989\)](#).

### B. Plaintiff Has Failed to State a Claim Under the Sherman Act.

In order to plead a [\*7] claim under the Sherman Act, Plaintiff must allege a restraint on competition that harms competition in the relevant market. See [McClinchy v. Shell Chem. Co., 845 F.2d 802, 812-13 \(9th Cir. 1988\)](#) ("It is the impact upon competitive conditions in a definable market which distinguishes the antitrust violation from the ordinary business tort. [The] failure to allege injury to competition is a proper ground for dismissal by judgment on the pleadings.")

The essence of Plaintiff's claims against the MPAA Defendants is that the TRB Rules serve as a monopolistic structure precluding the production and distribution of motion pictures by small, independent film makers. However, the uncontested facts are that the TRB Rules do not prevent members (or non-members) from distributing Plaintiff's, or any other independent film maker's, motion picture. At most the rules restrict MPAA members from producing a motion picture with a title identical to one accorded priority under the TRB Rules. (FAC, P 36, TRB Rules §§ 2.2.3, 3.1, 5.1.2.) Restricting the use of a title does not harm competition in the relevant markets alleged by Plaintiff, the United States motion picture production or distribution markets. [\*8] (FAC, PP 73, 91.)

The TRB Rules effectively manage, among its members, the priority of rights given to the users of various titles for motion pictures. Such mechanism for priority of rights is similar (although not identical) to the assertion of trademark rights.<sup>1</sup> As a matter of law, possessing and asserting priority of trademark rights does not harm competition in the market associated with the mark. See [Clorox Co. v. Sterling Winthrop, Inc., 117 F.3d 50, 56 \(2nd Cir. 1997\)](#) (holding that a trademark is, by its nature, non-exclusionary, and "does not confer a legal monopoly on any good or idea; it confers rights to a name only.") Because a trademark, or in this case, a priority to use of a motion picture title, "merely enables the owner to bar others from use of the mark, . . . the opportunity for effective antitrust misuse of a trademark, as distinguished from collateral anti-competitive activities on the part of the manufacturer or seller of the goods bearing the mark, is so limited that it poses a far less serious threat to the economic health of the nation." *Id.* (citing [Carl](#)

<sup>1</sup> In his written submissions as well as at oral argument on the motion, Plaintiff asserts that the TRB Rules effectively create a private Patent and Trademark Office and grant a "language monopoly" or a "monopoly of words from the dictionary." (Opp. Br. at 7; FAC, P 85.) The MPAA's private arrangement to prioritize the use of motion picture titles, as Plaintiff concedes in his complaint, is designed "to avoid confusion in the marketplace between competing projects with identical or similar marks." (FAC, P 84.) Such private arrangement serves its members by prioritizing the right to use a certain title among its members; [\*10] it does not constitute a private PTO and such prioritizing does not constitute a monopoly in the relevant market. There is no relevant market made up of words, or titles, and the relevant market designated by Plaintiff -- the United States motion picture production and distribution -- is not affected by the restrictions imposed by the TRB Rules, as discussed above.

Zeiss Stiftung v. V.E.B. Carl Zeiss, Jena, 298 F. Supp. 1309, 1314 (S.D.N.Y. 1969).) [\*9] A trademark agreement does no more than regulate how a certain name may be used and does not in any way restrict competition in the production or sale of a competing good with a different name. Id. at 57; see also California Packing Corp. v. Sun-Maid Raisin Growers of California, 165 F. Supp. 245, 250-51 (S.D. Cal. 1958) (holding that private agreement limiting the use of a certain mark does not prevent competitor from engaging in competitive production and sales in the market, but only restricts the use of the name, and therefore does not raise antitrust concerns).

Restrictions on the use of a title do not ultimately bear on the production or distribution of the motion picture associated with that title. Even accepting as true all of Plaintiff's assertions, the TRB Rules do not function to restrict its members from producing or distributing Plaintiff's motion picture project and do not prevent Plaintiff from selling his motion picture project to member or non-member producers or distributors or from entering those markets himself. As Plaintiff contends, the TRB Rules are apparently designed to avoid confusion in the marketplace as to those motion pictures its members or signatories decide to market or distribute. (FAC, P 84.) The TRB Rules, therefore, have no effect on the motion picture production or distribution markets.

Having failed to demonstrate that the rules harm competition [\*11] in the relevant market, Plaintiff cannot state a claim under the Sherman Act. Because Plaintiff cannot allege facts sufficient to demonstrate that the MPAA Defendants' rules harm competition, leave to amend would be futile and is denied. See Rutman Wine, 829 F.2d at 738 (request for leave to amend should be denied if amendment would be futile).

### C. Plaintiff Lacks Antitrust Standing.

The fact that Plaintiff lacks antitrust standing serves as an alternate basis for dismissal of Plaintiff's claims against the MPAA Defendants. The Clayton Act authorizes a private individual to bring suit under the antitrust laws if that individual has been "injured in his business or property by reason of anything forbidden in the antitrust laws." 15 U.S.C. § 15. Only individuals who possess antitrust standing by virtue of having suffered such injury may sue to redress an antitrust violation. Associated General Contractors of California, Inc. v. California State Council of Carpenters, 459 U.S. 519, 529-535, 103 S. Ct. 897, 74 L. Ed. 2d 723 (1983); see also Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 113, 107 S. Ct. 484, 93 L. Ed. 2d 427 (1986) ("a private plaintiff must allege threatened loss or damage `of the type the antitrust laws were designed to prevent [\*12] and that flows from that which makes defendants' acts unlawful.'") (citing Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc., 429 U.S. 477, 489, 97 S. Ct. 690, 50 L. Ed. 2d 701 (1977))).

First, as addressed above, restrictions on the use of any particular title do not prevent Plaintiff, or any other screenwriter, from entering the market for motion picture production or distribution, and therefore do not restrain competition in those relevant markets. See Clorox, 117 F.3d at 56. Second, Plaintiff cannot allege any specific injury he has suffered as a result of the MPAA Defendants' conduct. Plaintiff alleges that he wrote his screenplay nine years before Mandalay registered "Into The Blue" with the TRB and did not meet with any success producing or distributing his motion picture project during that time period. (FAC, PP 21, 34.) Further, although Plaintiff contends that film projects often take years to come to successful fruition, he has not alleged, and cannot allege, that since Mandalay's registration in 2002 or MGM's registration in 2003, any motion picture producer or distributor has rejected Plaintiff's project on the basis that a similar title has been granted priority among MPAA members by virtue of prior title registration. [\*13] Therefore, there is no factual support for a claim for direct injury as a result of the MPAA Defendants' conduct.<sup>2</sup>

Plaintiff has not alleged, and cannot in good faith allege, facts sufficient to demonstrate that he has the requisite standing for his federal antitrust claims against the MPAA Defendants. Because Plaintiff cannot allege facts

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<sup>2</sup> In addition, Plaintiff has not alleged in his complaint that he attempted to register his title with the TRB and only represented at oral argument that his attempt to register was frustrated by his own refusal to abide by the terms required for registration. Without having tried to benefit from the TRB's registration process, Plaintiff cannot contend that he has suffered from rejection of the registration of his own title.

demonstrating injury as a result of anticompetitive conduct by defendants, leave to amend on this basis would also be futile and is denied. See [Rutman Wine, 829 F.2d at 738](#) (request for leave to amend should be denied if amendment would be futile).

#### **D. Other California Causes of Action.**

Plaintiff has also alleged two California state law claims against the MPAA Defendants, under the Cartwright Act and [California Business and Professions Code § 17200](#). [\*14] In the absence of anticompetitive conduct capable of harming competition in the relevant market, Plaintiff's Cartwright Act claim fails. See, e.g., [Dimidowich v. Bell & Howell, 803 F.2d 1473, 1476-77 \(9th Cir. 1986\)](#). In addition, the claim falters due to Plaintiff's lack of standing to assert antitrust injury. Furthermore, Plaintiff's state unfair competition claim fails because it is not based upon "conduct that threatens an incipient violation of an **antitrust law**, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition." [Cel-Tech Communications, Inc. v. Los Angeles Cellular Tel. Co., 20 Cal. 4th 163, 187, 83 Cal. Rptr. 2d 548, 973 P.2d 527 \(1999\)](#); see also [Kentmaster Mfg. Co. v. Jarvis Products Corp., 146 F.3d 691, 695](#) (holding that plaintiff's failure to allege harm to competition was fatal to [Section 17200](#) just as it was to Sherman Act, [Section 2](#) claims).

#### **E. Studio Defendants' Motion for Judgment on the Pleadings.**

The Studio Defendants join the arguments of the MPAA Defendants and move for judgment on the pleadings as to the fifth, sixth, seventh and eighth causes of action pending against [\*15] them. Judgment on the pleadings is appropriate where, even if all the material facts in the complaint are true, the moving party is entitled to judgment as a matter of law. [Hal Roach Studios, Inc. v. Richard Feiner & Co., 896 F.2d 1542, 1550 \(9th Cir. 1989\)](#). For the same reasons discussed herein, Plaintiff has failed to state a claim upon which relief can be granted and lacks antitrust standing as to those same claims pending against the Studio Defendants. Therefore, the Studio Defendants' motion for judgment on the pleadings is granted.

### **CONCLUSION**

For the foregoing reasons, the Court hereby GRANTS the MPAA Defendants' motion to dismiss without leave to amend on all claims pending against them and GRANTS the Studio Defendants' motion for judgment on the pleadings on the fifth sixth, seventh and eighth claims against them.

IT IS SO ORDERED.

Dated: August 22, 2005

JEFFREY S. WHITE

UNITED STATES DISTRICT JUDGE

## Wilson Learning Corp. v. Schlechte

United States District Court for the District of Minnesota

August 24, 2005, Decided

Civil No. 04-4703(DSD/SRN)

**Reporter**

2005 U.S. Dist. LEXIS 39631 \*; 2005-2 Trade Cas. (CCH) P74,997

Wilson Learning Corporation, a Delaware corporation, Plaintiff v. David W. Schlechte, a Missouri resident, Norman H. Evans, A Missouri resident, and Douglas M. Schlechte, a Missouri resident (d/b/a Personal Skills Development, a Missouri fictitious business name), Defendants

### **Core Terms**

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defendants', counterdefendants, counterclaims, antitrust, motion to dismiss, damages, statute of limitations, summary judgment, claimant, alleges, conspiracy, products, sales, anticompetitive, civil conspiracy, overt act, distributors, speculative, genuine

### **LexisNexis® Headnotes**

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Civil Procedure > ... > Pleadings > Counterclaims > General Overview

#### **HN1[] Pleadings, Counterclaims**

Parties joined by a defendant to answer a counterclaim along with a party plaintiff are referred to as counter-defendants rather than third-party defendants.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN2[] Summary Judgment, Entitlement as Matter of Law**

Fed. R. Civ. P. 56(c) provides that summary judgment is appropriate if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

#### **HN3[] Burdens of Proof, Movant Persuasion & Proof**

For a party moving for summary judgment to prevail, it must demonstrate to the court that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c). A

fact is material only when its resolution affects the outcome of the case. A dispute is genuine if the evidence is such that it could cause a reasonable jury to return a verdict for either party.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

#### **HN4** **Burdens of Proof, Nonmovant Persuasion & Proof**

On a motion for summary judgment, all evidence and inferences are to be viewed in a light most favorable to the non-moving party. The non-moving party, however, may not rest upon mere denials or allegations in the pleadings, but must set forth specific facts sufficient to raise a genuine issue for trial. Moreover, if a plaintiff cannot support each essential element of its claim, summary judgment must be granted, because a complete failure of proof regarding an essential element necessarily renders all other facts immaterial.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

#### **HN5** **Motions to Dismiss, Failure to State Claim**

When considering a motion to dismiss for failure to state a claim, a court takes all the facts alleged in support of the claim being attacked as true and construed in the light most favorable to the claimant. However, a court is free to ignore legal conclusions, unsupported conclusions, unwarranted inferences and sweeping legal conclusions cast in the form of factual allegations. The motion should not be granted unless the claimant can prove no set of facts entitling him to relief.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Governments > Legislation > Statute of Limitations > Pleadings & Proof

#### **HN6** **Motions to Dismiss, Failure to State Claim**

Where it appears from the face of the pleading that the statute of limitations has run, a limitations defense may properly be invoked in a motion to dismiss pursuant to [\*Fed. R. Civ. P. 12\(b\)\(6\)\*](#). If the claimant then wishes to avail himself of an exception to the statute of limitations, he bears the burden to plead and prove that he is entitled to it.

Antitrust & Trade Law > Clayton Act > General Overview

Governments > Legislation > Statute of Limitations > Pleadings & Proof

#### **HN7** **Antitrust & Trade Law, Clayton Act**

Section 4B of the Clayton Act provides that any action for damages under the federal antitrust laws must be commenced within four years after the cause of action accrued. [15 U.S.C.S. § 15b](#). Generally, such a cause of action accrues and the statute begins to run when a defendant commits an act that injures a plaintiff's business.

Antitrust & Trade Law > Clayton Act > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

## [\*\*HN8\*\*](#) [blue download icon] Antitrust & Trade Law, Clayton Act

Generally, where a claimant complains of an anticompetitive agreement, the statute of limitations begins to run when the claimant becomes subject to the terms of the agreement. Later acts in performance of the agreement do not restart the limitations period.

Governments > Legislation > Statute of Limitations > Tolling

## [\*\*HN9\*\*](#) [blue download icon] Statute of Limitations, Tolling

The speculative damages exception holds that a cause of action for an antitrust violation does not accrue until the claimant's damages become ascertainable.

Governments > Legislation > Statute of Limitations > Tolling

## [\*\*HN10\*\*](#) [blue download icon] Statute of Limitations, Tolling

A statute of limitations will not be tolled merely because the unlawful act of an antitrust defendant will inflict damages continuing into the future.

Governments > Legislation > Statute of Limitations > Tolling

## [\*\*HN11\*\*](#) [blue download icon] Statute of Limitations, Tolling

The speculative damages exception will only delay accrual of a cause of action when future damages are not susceptible of proof at the time of the antitrust defendant's unlawful act.

Governments > Legislation > Statute of Limitations > Tolling

## [\*\*HN12\*\*](#) [blue download icon] Statute of Limitations, Tolling

Federal courts have distinguished uncertain damages from uncertain extent of damages. The former constitutes a plaintiff's inability to establish an injury and, thus, a cause of action. The latter constitutes mere imprecision in the calculation of damages, which may be settled by the jury's reasonable estimation.

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Governments > Legislation > Statute of Limitations > Tolling

## [\*\*HN13\*\*](#) [blue download icon] Statute of Limitations, Extensions & Revivals

A continuing violation is one in which the claimant's interests are repeatedly invaded and a cause of action arises each time the claimant is injured. When a claimant alleges a continuing violation, an overt act by the defendant is required to restart the statute of limitations and the statute runs from the last overt act. An overt act has two elements: (1) it must be a new and independent act that is not merely a reaffirmation of a previous act, and (2) it

must inflict new and accumulating injury on the plaintiff. If an act is merely the unabated inertial consequence of a previous act, the subsequent act will not restart the statute of limitations.

Governments > Legislation > Statute of Limitations > Extensions & Revivals

#### **HN14** [L] **Statute of Limitations, Extensions & Revivals**

Performance of an alleged anticompetitive contract is not sufficient to restart the limitations period.

Torts > ... > Concerted Action > Civil Conspiracy > General Overview

#### **HN15** [L] **Concerted Action, Civil Conspiracy**

Under Missouri law, civil conspiracy is a theory of joint liability for a tortious act. If a party fails to state a claim for an underlying tort, his conspiracy claim fails of necessity.

Antitrust & Trade Law > Sherman Act > Claims

#### **HN16** [L] **Sherman Act, Claims**

The Sherman Act's prohibition of trade restraints implemented by contract, combination, or conspiracy, is aimed at the inherent anticompetitive risk posed by the consolidation of efforts by actors that previously pursued their own interests separately.

Antitrust & Trade Law > Sherman Act > Claims

#### **HN17** [L] **Sherman Act, Claims**

Because the officers of a single firm are not separate economic actors pursuing separate economic interests, they do not provide the plurality of actors imperative for a conspiracy under [15 U.S.C.S. § 1](#).

**Counsel:** [\*1] For plaintiff: Edward T. Matthews, Esq., Nathan J. Hartshorn, Esq., Richard J. Wegener, Esq., Todd A. Wind, Esq. and Fredrikson & Byron, P.A., Minneapolis, MN; Heidi G. Welsch, Esq. and Welsch Law Offices, Bloomington, MN

For defendants: Arthur G. Muegler, Jr., Esq., Louis, MO; James P. Cullen, Esq., Minneapolis, MN; Alan I Silver, Esq., Todd J. Thun, Esq. and Bassford Remele, Minneapolis, MN

**Judges:** David S. Doty, Judge, United States District Court

**Opinion by:** David S. Doty

## **Opinion**

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**ORDER**

This matter is before the court upon defendant Douglas M. Schlechte's motion for summary judgment, plaintiff's motion to dismiss defendants' <sup>1</sup> counterclaims and counterdefendants' motion to dismiss defendants' counterclaims. <sup>2</sup> Based upon a review of the file, record and proceedings herein, and for the reasons stated, the court denies the motion for summary judgment and grants the motions to dismiss.

## [\*2] BACKGROUND

In one view, this is a rather run-of-the-mill breach of contract action arising from defendants' alleged failure to pay an amount owing on a promissory note. In another view, it is a complicated antitrust case. Wilson Learning Corporation ("WLC") develops and sells what it terms "human performance improvement solutions," that is "how-to" books, outlines and other training materials meant to increase individuals' business performance. Defendants David W. Schlechte, Norman H. Evans and Douglas M. Schlechte are former distributors of WLC's products who conducted their business under the fictitious name of Personal Skills Development ("PSD").

For its claim against defendants, WLC alleges that defendants purchased products from it for resale without paying for them. Subsequently, PSD executed a promissory note in WLC's favor in the amount of \$ 114,321.58 of which \$ 78,377 is now due and owing.<sup>3</sup> WLC sues to recover that money under breach of contract and unjust enrichment theories. WLC also seeks a declaration that the termination of its distributor agreement with defendants was proper and that the termination does not bar collection of PSD's debt. Douglas M. Schlechte [\*3] moves for summary judgment upon the ground that he was not an owner, partner or joint venturer in PSD. WLC opposes the motion by submitting evidence that Douglas Schlechte is listed as a one-third owner of PSD on a "registration of fictitious name" document filed with the Missouri Secretary of State pursuant to state statute. Schlechte's signature also appears on the document next to the instruction "Individual Owners Sign Here."

For their counterclaims against WLC, defendants David Schlechte and Norman Evans allege various violations of federal and Missouri state **antitrust law** and civil conspiracy under Missouri state law. Defendants also join as counterdefendants several officers, directors and employees of WLC and several unknown fellow distributors of WLC products. Defendants allege that they, WLC and counterdefendants:

voluntarily joined together in concert with each other and agreed, conspired and combined to illegally [\*4] restrain trade and commerce and to lessen competition within the [market for how-to products] through horizontal competitor price fixing, vertical price fixing, horizontal competitor allocation of exclusive markets, horizontal competitor allocation of exclusive customers, group boycotts, price discrimination and other illegal anticompetitive restraints. . . .

(1st Am. Countercl. P 34.) Among other things, defendants assert that WLC and its officers, directors and employees coerced defendants and other distributors to enter into a "Wilson Learning Corporation Standard Representative Agreement" which "contained and implemented the [conspiracy's illegal restraints]." (1st Am. Countercl. P 69(a).) The contract was executed on October 16, 1999. WLC and the counterdefendants, excluding the John Doe distributors, now move to dismiss defendants' counterclaims.

## DISCUSSION

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<sup>1</sup> Defendant Douglas M. Schlechte does not join in the counterclaims. Nevertheless, for ease of reference, the court refers to the counterclaims throughout as "defendants' counterclaims."

<sup>2</sup> The counterdefendants characterize themselves as "third-party defendants." However, no third-party claim has been asserted against them because defendants do not allege that they are liable "to [defendants] for all or part of the plaintiff's claim against the [defendants]." *Fed. R. Civ. P. 14 (a)*. Rather, **HN1** parties joined by a defendant to answer a counterclaim along with a party plaintiff are referred to as "counterdefendants." See, ironically, *Independence Tube Corp. v. Copperweld Corp.*, 74 F.R.D. 462, 468 (N.D. 111. 1977).

<sup>3</sup> The complaint also alleges that David W. Schlechte personally guaranteed the debt.

## I. Defendant Douglas Schlechte's Motion for Summary Judgment

### A. Summary Judgment Standard

**HN2** [↑] [Rule 56\(c\) of the Federal Rules of Civil Procedure](#) provides that summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories, [\*5] and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." **HN3** [↑] In order for the moving party to prevail, it must demonstrate to the court that "there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." [Celotex Corp. v. Catrett](#), 477 U.S. 317, 322, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986)(quoting [Fed. R. Civ. P. 56\(c\)](#)). A fact is material only when its resolution affects the outcome of the case. [Anderson v. Liberty Lobby, Inc.](#), 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986). A dispute is genuine if the evidence is such that it could cause a reasonable jury to return a verdict for either party. See [id. at 252](#).

**HN4** [↑] On a motion for summary judgment, all evidence and inferences are to be viewed in a light most favorable to the non-moving party. See [id. at 255](#). The non-moving party, however, may not rest upon mere denials or allegations in the pleadings, but must set forth specific facts sufficient to raise a genuine issue for trial. See [Celotex](#), 477 U.S. at 324. [\*6] Moreover, if a plaintiff cannot support each essential element of its claim, summary judgment must be granted because a complete failure of proof regarding an essential element necessarily renders all other facts immaterial. [Id. at 322-23](#).

### B. Merits of the Motion

The court finds that a genuine issue of material fact exists which precludes summary judgment in defendant Douglas Schlechte's favor. His motion is therefore denied.

## II. Motions to Dismiss

### A. Standard on Motion to Dismiss

**HN5** [↑] When considering a motion to dismiss for failure to state a claim, all the facts alleged in support of the claim being attacked are taken as true and construed in the light most favorable to the claimant. [Varner v. Peterson Farms](#), 371 F.3d 1011, 1016 (8th Cir. 2004)(quoting [Kottschade v. City of Rochester](#), 319 F.3d 1038, 1040 (8th Cir. 2003)). However, the court is "free to ignore legal conclusions, unsupported conclusions, unwarranted inferences and sweeping legal conclusions cast in the form of factual allegations." [Id. at 1016](#) (quoting [Wiles v. Capitol Indem. Corp.](#), 280 F.3d 868, 870 (8th Cir. 2002)). [\*7] The motion should not be granted unless the claimant can prove no set of facts entitling him to relief. [Kottschade](#), 319 F.3d at 1040.

**HN6** [↑] When it appears from the face of the pleading that the statute of limitations has run, a limitations defense may properly be invoked in a motion to dismiss pursuant to [Rule 12 \(b\)\(6\) of the Federal Rules of Civil Procedure](#). [Varner](#), 371 F.3d at 1016. If the claimant then wishes to avail himself of an exception to the statute of limitations, he bears the burden to plead and prove that he is entitled to it. See [Wollman v. Gross](#), 637 F.2d 544, 549 (8th Cir. 1980); [Coleman v. Kansas City, Mo.](#), 173 S.W.2d 572, 578, 351 Mo. 254 (Mo. 1943)(Missouri law).

### B. Plaintiff's Motion to Dismiss

## 1. Antitrust Claims

WLC argues that all of defendants' antitrust claims are barred by the relevant statute of limitations. [HN7](#) Section 4B of the Clayton Act provides that any action for damages under the federal antitrust laws must be commenced within four years after the cause of action accrued.<sup>4</sup> [\*9] [15 U.S.C. § 15b](#). "Generally, a cause of action accrues [\*8] and the statute begins to run when a defendant commits an act that injures a plaintiff's business." [Zenith Radio Corp. v. Hazeltine Research, Inc., 401 U.S. 321, 338, 91 S. Ct. 795, 28 L. Ed. 2d 77 \(1971\)](#). Here, the principal act of which defendants complain is that WLC and others "intimidated and caused WLC representatives, including [defendants], to execute a Wilson Learning Corporation Standard Representative Agreement" which imposed a number of anticompetitive restrictions on defendants' participation in the market for training materials. (1st Am. Countercl. P 69 (a); see also PP 37.) This contract was executed on October 16, 1999.<sup>5</sup> (*Id.* P 69 (a).) Defendants did not file their counterclaim until December 20, 2004. [HN8](#) Generally, where a claimant complains of an anti-competitive agreement, the statute of limitations begins to run when the claimant becomes subject to the terms of the agreement. See [Varner, 371 F.3d at 1020](#). Later acts in performance of the agreement do not restart the limitations period. See [id. at 1020](#). Therefore, on the face of the pleading, defendants' federal antitrust claims are outside the statute of limitations.

Defendants invoke two separate exceptions to the statute of limitations in a bid to buoy their claims. First, defendants allege that their damages from WLC's anti-competitive conduct were speculative for a time due to a phenomenon which they refer to as "sales delay." (1st Am. Countercl. PP 31-33.) [HN9](#) The speculative damages exception holds that a cause of action for an antitrust violation does not accrue until the claimant's damages become ascertainable. See [Kaiser Aluminum & Chem. Sales, Inc. v. Avondale Shipyards, Inc., 677 F.2d 1045, 1051 \(5th Cir. 1982\)](#) (citing [Zenith, 401 U.S. at 339-40](#), cited in [Varner, 371 F.3d at 1019 n.6](#)). Defendants allege that, to sell products in the marketplace, they had [\*10] to undertake a laborious, multiple-step process including targeting the decisionmaker within a potential customer organization, determining the restrictions on the decisionmaker's authority, developing a personal relationship with the decisionmaker, identifying appropriate products to pitch to the decisionmaker, preparing a sales presentation and so forth. (*Id.* P 31.) Defendants allege that this "sales delay" would have prevented them from realizing a first sale of market products until December 22, 2000. (*Id.* P 31.) Defendants further allege that, until that date, their damages were speculative and incapable of proof. (*Id.* P 31.)

Defendants' "sales delay" allegations are unavailing. [HN10](#) The statute of limitations will not be tolled merely because the unlawful act of an antitrust defendant will inflict damages continuing into the future. See [Zenith, 401 U.S. at 338-39](#) (antitrust plaintiffs may recover future damages). [HN11](#) The speculative damages exception will only delay accrual of a cause of action when future damages are not susceptible of proof at the time of the antitrust defendant's unlawful act. See [id. at 339](#).<sup>6</sup> Here, defendants' pleading [\*11] offers no factual basis from which the court can conclude that "sales delay" rendered their damages insusceptible of proof. That is, defendants' allegations, taken as true, fail to offer any factual support for the proposition that realization of actual sales, or even the hypothetical realization of sales, was a necessary pre-condition to their ability to prove injury resulting from

<sup>4</sup> Defendants do not dispute that their claim for violations of Missouri antitrust law is governed by federal antitrust law. (See Mem. Opp'n at 10.)

<sup>5</sup> Elsewhere, defendants allege that certain of the offending terms had been in effect since as early as 1998 as part of a conspiracy between WLC and its authorized sales representatives. (See, e.g., 1st Am. Countercl. PP 39-42.) Because 1998 is even earlier than 1999, those allegations do not impact the court's statute of limitations analysis.

<sup>6</sup> Thus, [HN12](#) federal courts have distinguished "uncertain damages" from "uncertain extent of damages." [Pace Indus., Inc. v. Three Phoenix Co., 813 F.2d 234, 240 \(9th Cir. 1987\)](#) (citing [In re Multidistrict Vehicle Air Pollution, 591 F.2d 68, 73 \(9th Cir. 1979\)](#)). The former constitutes a plaintiff's inability to establish an injury and, thus, a cause of action. See [id. at 240](#). The latter constitutes mere imprecision in the calculation of damages, which may be settled by the jury's reasonable estimation. See [id. at 240](#).

WLC's conduct. In the absence of such a factual basis, the court must conclude that defendants could have substantiated their damages, through expert testimony or otherwise, prior to December 2000. See, e.g., *Mir v. Little Co. of Mary Hosp.*, 844 F.2d 646, 650 (9th Cir. 1988) (statute not tolled where plaintiff could have presented evidence of projected lost income); *Brunswick Corp. v. Riegel Textile Corp.*, 752 F.2d 261, 271 (7th Cir. 1984). Therefore, the speculative damages exception does not apply.

[\*12] Defendants also argue that they have alleged a continuing violation of the antitrust laws. [HN13](#) [↑] "A continuing violation is one in which the [claimant's] interests are repeatedly invaded and a cause of action arises each time the [claimant] is injured." *Pace Indus.*, 813 F.2d at 237 (citing *Hennegan v. Pacifico Creative Serv., Inc.*, 787 F.2d 1299 (9th Cir. 1986)). When a claimant alleges a continuing violation, "an overt act by the defendant is required to restart the statute of limitations and the statute runs from the last overt act." *Varner*, 371 F.3d at 1019 (quoting *Peck v. General Motors Corp.*, 894 F.2d 844, 849 (6th Cir. 1990)). "An overt act has two elements: (1) it must be a new and independent act that is not merely a reaffirmation of a previous act, and (2) it must inflict new and accumulating injury on the plaintiff." *Id. at 1019* (citing *Pace Indus.*, 813 F.2d at 238). If an act is merely the unabated inertial consequence of a previous act, the subsequent act will not restart the statute of limitations. See *id. at 1019*. Defendants argue that paragraph sixty-nine of the counterclaim [\*13] alleges a host of independent overt acts.

Defendants' counterclaim is insufficient to invoke the continuing violation doctrine. As the court has observed, [HN14](#) [↑] performance of an alleged anticompetitive contract is not sufficient to restart the limitations period. *Varner*, 371 F.3d at 1020. Defendants admit in the pleading itself that the October 16, 1999, contract "contained and implemented" the illegal conduct which forms the basis of their counterclaim: (1st Am. Countercl. P 69 (a).) Furthermore, in response to WLC's motion to dismiss, defendants fail to explain how any of the various acts they allege depart from what was contemplated in the contract or were otherwise new and independent. Therefore, the continuing violation doctrine does not apply. Defendants' antitrust counterclaims, counts one through five, are dismissed.

## 2. Civil Conspiracy Claim

Count six of defendants' counterclaim alleges a "civil conspiracy" claim under Missouri state law. No such cause of action exists. See *Bockover v. Stemmerman*, 708 S.W.2d 179, 182 (Mo. Ct. App. 1986), abrogated on other grounds by *Roth v. La Societe Anonyme Turbomeca France*, 120 S.W.3d 764 (Mo. Ct. App. 2003). [\*14] Rather, [HN15](#) [↑] in Missouri, civil conspiracy is a theory of joint liability for a tortious act. See *id. at 182*. If a party fails to state a claim for an underlying tort, his conspiracy claim fails of necessity. See *Rice v. Hodapp*, 919 S.W.2d 240, 245 (Mo. 1996) (citing *Williams v. Mercantile Bank of St. Louis*, 845 S.W.2d 78, 85 (Mo. Ct. App. 1993)). Here, because of the applicable statute of limitations, defendants have failed to state any substantive claim. Therefore, their conspiracy claim must fail as well. Defendants' counterclaim against WLC is dismissed.

## C. Counterdefendants' Motion to Dismiss

### 1. Sherman Act and Clayton Act Claims

Counterdefendants Iizuka, Roth, Kielley, Leveille, Magnuson, Gillem and Skon, each an officer, director or employee of WLC, also move to dismiss defendants' counterclaims. At the outset, because defendants allege that counterdefendants' participation in the conspiracy was accomplished through WLC's contract with defendants, it is doubtful that the claims survive the statute of limitations for the reasons stated above. (1st Am. Countercl. P 69(a).) Nevertheless, counterdefendants have identified an additional [\*15] fundamental problem with defendants' counterclaims.

Defendants' claims against counterdefendants must be dismissed because, as WLC's officers, directors and employees, counterdefendants cannot have conspired with WLC. [HN16](#)[<sup>16</sup>] The Sherman Act's prohibition of trade restraints implemented by "contract, combination . . . or conspiracy" is aimed at the inherent anticompetitive risk posed by the consolidation of efforts by actors "that previously pursued their own interests separately." [\*Copperweld Corp. v. Independence Tube Corp.\*, 467 U.S. 752, 768-69, 104 S. Ct. 2731, 81 L. Ed. 2d 628 \(1984\)](#). [HN17](#)[<sup>17</sup>] Because "the officers of a single firm are not separate economic actors pursuing separate economic interests," they "do not provide the plurality of actors imperative for a § 1 conspiracy." [\*Id. at 769\*](#). Furthermore, counterdefendants persuasively argue, and defendants do not deny, that the holding of *Copperweld* should also apply to defendants' claim under section three of the Clayton Act because its elements are identical to a Sherman Act section one claim. Cf. [\*Advanced Health-Care Servs., Inc. v. Radford Cnty. Hosp.\*, 910 F.2d 139, 152 \(4th Cir. 1990\)](#). Defendants have neither pleaded [\*16] in their counterclaim nor argued in response to counterdefendants' motion that the counterdefendants' economic interests diverged from those of WLC or that their acts in furtherance of the alleged conspiracy were separate from those of WLC. In fact, in each instance where the counterclaim alleges an "overt act" by counterdefendants, WLC is included as a co-actor. (See, e.g., 1st Am. Countercl. PP 69(a), (b), (c), (d), (e), (g) & (h) .) Because defendants have failed to allege an actionable antitrust conspiracy with respect to counterdefendants, defendants' claims must be dismissed.

## 2. Other Claims

Defendants have not responded to counterdefendants' arguments that defendants' Robinson-Patman Act claim against them is fatally flawed. The court dismisses those claims for the reasons cited by counterdefendants. Furthermore, because defendants' Missouri antitrust claim is governed by principles of federal law, it too is dismissed. Finally, as defendants have failed to state any actionable claim against counterdefendants, defendants' civil conspiracy claim is dismissed for the same reason expressed in section II.B.2. of this order.

## CONCLUSION

Accordingly, **IT IS HEREBY [\*17] ORDERED** that:

1. Defendant Douglas M. Schlechte's motion for summary judgment [Doc. No. 24] is denied.
2. Counterdefendants' motion to dismiss defendants' counterclaims [Doc. No. 30] is granted.
3. Plaintiff's motion to dismiss defendants' counterclaims [Doc. No. 34] is granted.

Dated: August 24, 2005

David S. Doty, Judge

United States District Court



## **Adeduntan v. Hosp. Auth. of Clarke County**

United States District Court for the Middle District of Georgia, Athens Division

August 25, 2005, Decided

Case No. 3:04-CV-65 (CDL)

### **Reporter**

2005 U.S. Dist. LEXIS 18281 \*; 2005-2 Trade Cas. (CCH) P74,956

AZEEZ P. ADEDUNTAN, VICTORY VASCULAR & GENERAL SURGERY OF GEORGIA, P.C. Plaintiffs, v. HOSPITAL AUTHORITY OF CLARKE COUNTY d/b/a ATHENS REGIONAL MEDICAL CENTER, ATHENS REGIONAL MEDICAL CENTER, INC., ATHENS REGIONAL HEALTH SERVICES, INC., ATHENS VASCULAR SURGERY, P.C., DAVID M. SAILORS, MARK J. CONSTANTINO, Defendants.

**Subsequent History:** Costs and fees proceeding at [Adeduntan v. Hosp. Auth., 2006 U.S. Dist. LEXIS 46846 \(M.D. Ga., July 11, 2006\)](#)

## **Core Terms**

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peer review, Plaintiffs', summary judgment, Vascular, privileges, Defendants', antitrust, peer review process, discovery, patient, surgery, performing, immunity, immunity defense, antitrust claim, recommendation, rights, direct observation, anti trust law, medical staff, nonmoving, proceedings, competence, written opinion, Sherman Act, anticompetitive, Credentials, courts, rebut, terms

## **LexisNexis® Headnotes**

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Civil Procedure > Judgments > Summary Judgment > Partial Summary Judgment

Healthcare Law > Business Administration & Organization > Hospital Privileges > General Overview

Civil Rights Law > Protection of Rights > Immunity From Liability > Private Parties

Healthcare Law > ... > Actions Against Facilities > Defenses > General Overview

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Healthcare Law > Business Administration & Organization > Employment Issues > Employment Discrimination

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

Public Health & Welfare Law > Healthcare > General Overview

**[HN1\[](#) Summary Judgment, Partial Summary Judgment**

The Health Care Quality Improvement Act, [42 U.S.C.S. § 11111 et seq.](#), expressly excludes federal civil rights claims from its immunity provisions. [42 U.S.C.S. § 11111\(a\)\(1\)](#).

Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Legal Entitlement

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

## [HN2](#) Discovery, Methods of Discovery

[Fed. R. Civ. P. 56\(c\)](#) provides that summary judgment shall be granted if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. An issue of fact is material if, under the applicable substantive law, it might affect the outcome of the case. An issue of fact is genuine if the record taken as a whole could lead a rational trier of fact to find for the nonmoving party.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

## [HN3](#) Summary Judgment, Entitlement as Matter of Law

A court must decide at summary judgment whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must prevail as a matter of law.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

## [HN4](#) Entitlement as Matter of Law, Genuine Disputes

The moving party at summary judgment bears the initial responsibility of informing the court of the basis for its motion, and identifying those portions of the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, which it believes demonstrate the absence of a genuine issue of material fact. Where the nonmoving party bears the burden of proof at trial, the moving party at summary judgment may discharge this initial responsibility by showing that there is an absence of evidence to support the nonmoving party's case or by showing that the nonmoving party will be unable to prove its case at trial.

Civil Procedure > Trials > Judgment as Matter of Law > Directed Verdicts

Evidence > Burdens of Proof > Ultimate Burden of Persuasion

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > Trials > Judgment as Matter of Law > General Overview

#### **HN5** Judgment as Matter of Law, Directed Verdicts

To survive summary judgment, the nonmoving party bearing the ultimate burden of proof at trial must come forward with evidence sufficient to withstand a directed verdict motion.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN6** Summary Judgment, Entitlement as Matter of Law

On summary judgment, the evidence of the nonmovant is to be believed.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN7** Summary Judgment, Entitlement as Matter of Law

A district court should resolve all reasonable doubts about the facts at summary judgment in favor of the nonmovant, and draw all justifiable inferences in his favor.

Contracts Law > Contract Interpretation > General Overview

#### **HN8** Contracts Law, Contract Interpretation

The starting point in contract construction under Georgia law is to look at the four corners of an instrument to determine the intention of the parties from the language employed. In making this determination, all the attendant and surrounding circumstances may be proved, but not explained. O.C.G.A. § 13-2-3. If the language of the agreement is clear, unambiguous, and capable of only one reasonable interpretation, no construction is necessary or even permissible by the court.

Contracts Law > Contract Interpretation > Ambiguities & Contra Proferentem > General Overview

Contracts Law > Defenses > Ambiguities & Mistakes > General Overview

#### **HN9** Contract Interpretation, Ambiguities & Contra Proferentem

An ambiguity in a contract is defined as duplicity, indistinctness, or an uncertainty of meaning or expression. A mere lack of clarity on casual reading is not the criterion for determining whether a contract is afflicted with ambiguity.

Contracts Law > Defenses > Ambiguities & Mistakes > General Overview

Evidence > Types of Evidence > Documentary Evidence > Parol Evidence

Governments > Legislation > Effect & Operation > Prospective Operation

Contracts Law > Contract Interpretation > Ambiguities & Contra Proferentem > General Overview

Contracts Law > Contract Interpretation > Parol Evidence > General Overview

## **HN10**[ **Defenses, Ambiguities & Mistakes**

Under Georgia law, if an ambiguity exists in an agreement, a court should attempt to resolve the ambiguity by applying the statutory rules of contract construction. If the ambiguity cannot be negated by applying the rules of construction, then parol evidence may be introduced, and the issue of what was intended by the parties is a matter for a jury to decide.

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

## **HN11**[ **Pleadings, Amendment of Pleadings**

Plaintiffs may not amend their complaint through argument opposing summary judgment.

Antitrust & Trade Law > Sherman Act > General Overview

Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > State Regulation

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > State Regulation

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

## **HN12**[ **Antitrust & Trade Law, Sherman Act**

The Sherman Act, [15 U.S.C.S. § 1 et seq.](#), declares every contract, combination, or conspiracy in restraint of trade or commerce among the several states to be illegal, [15 U.S.C.S. § 1](#), and also prohibits the monopoly of, or attempt to monopolize, or combine and conspire with any other person or persons, to monopolize any part of trade or commerce among the several states. [15 U.S.C.S. § 2](#).

Antitrust & Trade Law > Sherman Act > Remedies > Damages

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > Damages

Antitrust & Trade Law > Regulated Practices > Private Actions > Prioritizing Resources & Organization for Intellectual Property Act

Antitrust & Trade Law > Regulated Practices > Private Actions > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Sherman Act > Remedies > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

#### [HN13](#) [ ] Remedies, Damages

Private enforcement suits for damages caused by violations of the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), are permitted under the Clayton Act, [15 U.S.C.S. § 15](#). The Clayton Act allows successful plaintiffs to recover treble damages. [15 U.S.C.S. § 15](#).

Antitrust & Trade Law > ... > Private Actions > Standing > Clayton Act

Civil Procedure > ... > Justiciability > Standing > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Clayton Act > Claims

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

#### [HN14](#) [ ] Standing, Clayton Act

Standing under the Clayton Act, [15 U.S.C.S. § 15](#), has been described by the United States Court of Appeals for the Eleventh Circuit as a search for the proper plaintiff to enforce the [antitrust law](#). As a result, the courts have developed a two-step inquiry to evaluate whether a plaintiff has antitrust standing: (1) a court should determine whether the plaintiff suffered antitrust injury; and then, (2) the court should determine whether the plaintiff is an efficient enforcer of the antitrust laws.

Antitrust & Trade Law > Clayton Act > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

#### **HN15** [blue icon] Antitrust & Trade Law, Clayton Act

An antitrust injury has been defined by the United States Supreme Court as injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation. It should, in short, be the type of loss that the claimed violations would be likely to cause. This requires the antitrust plaintiff to show that his own injury coincides with the public detriment tending to result from the alleged violation increasing the likelihood that public and private enforcement of the antitrust laws will further the same goal of increased competition.

Antitrust & Trade Law > Sherman Act > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

Antitrust & Trade Law > Clayton Act > General Overview

#### **HN16** [blue icon] Antitrust & Trade Law, Sherman Act

The antitrust laws were not enacted to permit one person to profit from the anticompetitive behavior of another.

Antitrust & Trade Law > Clayton Act > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

Antitrust & Trade Law > Sherman Act > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

#### **HN17** [blue icon] Antitrust & Trade Law, Clayton Act

The legislative intent behind the antitrust statutes was the protection of competition, not competitors.

Antitrust & Trade Law > Sherman Act > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

#### **HN18** [blue icon] Antitrust & Trade Law, Sherman Act

The aim of the Sherman Act, [15 U.S.C.S. § 1 et seq.](#), is not to protect businesses from the working of the market; it is to protect the public from the failure of the market. For that reason, the law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself.

Civil Procedure > ... > Justiciability > Standing > General Overview

Constitutional Law > ... > Case or Controversy > Standing > General Overview

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Judgments > Enforcement & Execution > General Overview

Healthcare Law > Healthcare Litigation > Antitrust Actions > Physicians

## [HN19](#) [+] Justiciability, Standing

Even if plaintiffs are able to establish that they suffered antitrust injury, they still must demonstrate that they are efficient enforcers of the antitrust laws. This analysis requires consideration of several factors that might be useful in determining whether a party is a proper plaintiff in a particular antitrust suit. These factors include: (1) the directness of the injury and whether there exists an identifiable class of persons whose self-interest would motivate them to vindicate the public interest in antitrust enforcement; (2) the nature of the damages; (3) the importance of avoiding duplicative recoveries; and (4) whether the plaintiff can enforce an antitrust judgment efficiently and effectively.

Civil Rights Law > Protection of Rights > Immunity From Liability > Private Parties

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Public Health & Welfare Law > Healthcare > General Overview

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

## [HN20](#) [+] Immunity From Liability, Private Parties

Pursuant to [42 U.S.C.S. § 11111\(a\)](#), individuals associated with a medical professional review action - including a professional review body, members or staff of the body, persons under contract with the body, and persons who participate or assist with the review action - are entitled to immunity from damages under federal and state law under the Health Care Quality Improvement Act, [42 U.S.C.S. § 11111 et seq.](#)

Civil Rights Law > Protection of Rights > Public Versus Private Discrimination

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Healthcare Law > Business Administration & Organization > Hospital Privileges > Professional Review

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

## [HN21](#) [blue document icon] Protection of Rights, Public Versus Private Discrimination

A "professional review action" is defined as an action or recommendation of a professional review body which is based on the competence or professional conduct of an individual physician (which conduct affects or could affect adversely the health or welfare of a patient or patients) and which affects (or may affect) adversely the clinical privileges, or membership in a professional society, of the physician. Such term includes a formal decision of a professional review body not to take an action or make a recommendation and also includes professional review activities relating to a professional review action. [42 U.S.C.S. § 11151\(9\)](#).

Civil Rights Law > Protection of Rights > Public Versus Private Discrimination

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

Torts > ... > Types of Negligence Actions > Negligent Infliction of Emotional Distress > General Overview

Civil Rights Law > Protection of Rights > Immunity From Liability > Private Parties

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Torts > Intentional Torts > Intentional Infliction of Emotional Distress > General Overview

## [HN22](#) [blue document icon] Protection of Rights, Public Versus Private Discrimination

[42 U.S.C.S. § 11111\(a\)\(1\)](#) excludes civil rights actions brought under state or federal law.

Civil Rights Law > Protection of Rights > Immunity From Liability > Private Parties

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Rights Law > Protection of Rights > Public Versus Private Discrimination

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

Healthcare Law > Business Administration & Organization > Peer Review > Peer Review Statutes

## [HN23](#) [blue document icon] Immunity From Liability, Private Parties

For immunity to apply, a professional review action must have been pursued: (1) in the reasonable belief that the action was in furtherance of quality health care, (2) after a reasonable effort to obtain the facts of the matter, (3) after adequate notice and hearing procedures are afforded to the physician involved or after such other procedures as are fair to the physician under the circumstances, and (4) in the reasonable belief that the action was warranted by the facts known after such reasonable effort to obtain facts and after meeting the requirement of paragraph (3). [42 U.S.C.S. § 11112\(a\)](#). A professional review action is presumed to have met these standards, but the presumption is rebuttable by a preponderance of the evidence. The standard for resolving this issue at summary judgment is therefore: Might a reasonable jury, viewing the facts in the best light for the plaintiff, conclude that he has shown, by a preponderance of the evidence, that the defendants' actions are outside the scope of [§ 11112\(a\)](#)?

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > Business Administration & Organization > Peer Review > Peer Review Statutes

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

#### **HN24** [blue] Discovery, Privileged Communications

Georgia has codified its peer review and medical review privileges. [O.C.G.A. §§ 31-7-133](#) and [31-7-143](#).

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

#### **HN25** [blue] Discovery, Privileged Communications

See [O.C.G.A. § 31-7-133](#).

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > Business Administration & Organization > Peer Review > Organizations

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

Healthcare Law > Business Administration & Organization > Peer Review > Peer Review Statutes

#### **HN26** [blue] Official Information Privilege, Reports Privilege

The language of [O.C.G.A. § 31-7-143](#) is substantially the same as [O.C.G.A. § 31-7-133](#), substituting "medical review committee" for "peer review organization."

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

#### **HN27** [blue] Discovery, Privileged Communications

In enacting the peer review and medical review privileges statutes, the Georgia General Assembly has placed an absolute embargo upon the discovery and use of all proceedings, records, findings, and recommendations of peer review groups and medical review committees in civil litigation.

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Governments > Courts > Rule Application & Interpretation

Evidence > Privileges > General Overview

### **HN28** [blue document icon] **Official Information Privilege, Reports Privilege**

*Fed. R. Evid. 501* sets forth the rules of evidentiary privilege as they are applied in federal court.

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

### **HN29** [blue document icon] **Official Information Privilege, Reports Privilege**

See *Fed. R. Evid. 501*.

Evidence > Privileges > General Overview

Governments > Courts > Authority to Adjudicate

Governments > Courts > Rule Application & Interpretation

### **HN30** [blue document icon] **Evidence, Privileges**

*Fed. R. Evid. 501* clearly provides federal courts with the statutory power to recognize new or novel evidentiary privileges. However, courts do not create and apply an evidentiary privilege unless it promotes sufficiently important interests to outweigh the need for probative evidence.

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

### **HN31** [blue document icon] **Business Administration & Organization, Peer Review**

Peer review, the process by which physicians and hospitals evaluate and discipline staff doctors, has become an integral component of the health care system in the United States.

Civil Rights Law > Protection of Rights > Immunity From Liability > Private Parties

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Torts > Malpractice & Professional Liability > Healthcare Providers

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

### **HN32** [blue icon] Immunity From Liability, Private Parties

The enactment of peer review and medical review privileges statutes represents a proper legislative choice between the competing public concerns of fostering medical staff candor, on the one hand, and impairing medical malpractice plaintiffs' access to evidence, on the other hand. However, when a state law privilege would essentially prevent a plaintiff from rebutting a federal immunity defense or would defeat a federal claim which bears little relation to the type of claim the privilege was designed to address, the need for probative evidence sufficiently outweighs the interests protected by the privilege.

Evidence > ... > Government Privileges > Official Information Privilege > Reports Privilege

Healthcare Law > ... > Actions Against Facilities > Governmental & Nonprofit Liability > Health Care Quality Improvement Act

Evidence > ... > Government Privileges > Official Information Privilege > Self-Critical Analysis Privilege

Healthcare Law > Business Administration & Organization > Peer Review > General Overview

### **HN33** [blue icon] Official Information Privilege, Reports Privilege

While the Health Care Quality Improvement Act, [42 U.S.C.S. § 11111 et seq.](#), is certainly intended to promote the peer review process, it does not, by its terms, completely bar confidential peer review information from disclosure, particularly in cases where the peer review process itself is at issue.

Civil Procedure > ... > Discovery > Privileged Communications > General Overview

Evidence > ... > Government Privileges > Official Information Privilege > Self-Critical Analysis Privilege

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

### **HN34** [blue icon] Discovery, Privileged Communications

As a matter of federal common law, the self-critical analysis privilege does not exist.

**Counsel:** [\*1] For Azeez P. Adeduntan, M.D., Victory Vascular & General Surgery of Georgia, P.C., Plaintiffs: Lawrence Edwards Newlin, Atlanta, GA.

For Athens Vascular Surgery, P.C., David M. Sailors, M.D., Mark J. Costantino, M.D., Defendants: Benton J. Mathis, Jr., Atlanta, GA; Gary Bryan Blasingame, Athens, GA; J. Ralph Beard, Athens, GA; Bradley T. Adler, Atlanta, GA.

For M.D. Azeez P. Adeduntan, Counter Defendant: Lawrence Edwards Newlin, Atlanta, GA.

**Judges:** CLAY D. LAND, UNITED STATES DISTRICT JUDGE.

**Opinion by:** CLAY D. LAND

## Opinion

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### ORDER

#### I. INTRODUCTION

This lawsuit arises from the medical peer review of Plaintiff Dr. Azeez P. Adeduntan conducted after a patient of Dr. Adeduntan died at the Athens Regional Medical Center (ARMC). The peer review was allegedly conducted and directed by the Defendants. Dr. Adeduntan, along with his professional corporation, Victory Vascular & General Surgery of Georgia, P.C., assert various federal and state claims based upon Defendants' peer review conduct. Those claims include federal civil rights claims pursuant to [42 U.S.C. §§ 1981, 1985, 1983](#), and [Title VII](#); federal antitrust claims under the Sherman Act, [15 U.S.C. §§ 1, \[\\*2\] 2](#); and state law claims for the negligent and intentional infliction of emotional distress and for attorney's fees.

Defendants have filed motions for summary judgment and partial summary judgment. Defendants Hospital Authority of Clarke County (doing business as Athens Regional Medical Center), Athens Regional Medical Center, Inc., and Athens Regional Health Services, Inc. (collectively referred to as the "ARMC Defendants") have moved for summary judgment as to all of Plaintiffs' claims based upon a release executed by Dr. Adeduntan. In addition to their release defense, the ARMC Defendants also contend that they are entitled to summary judgment on: (1) Dr. Adeduntan's Title VII claim because they were not his employer; (2) Plaintiffs' peer review related claims, excluding the federal civil rights claims,<sup>1</sup> based upon immunity under the Health Care Quality Improvement Act (HCQIA), [42 U.S.C. § 11111, et seq.](#); and (3) Plaintiffs' antitrust claims based upon Plaintiffs' alleged lack of standing to assert those claims.

[\*3] Defendants Athens Vascular Surgery, P.C., Dr. David M. Sailors, and Dr. Mark J. Costantino (collectively referred to as the "Athens Vascular Defendants") seek partial summary judgment as to Plaintiffs' peer review related claims, except for Plaintiffs' federal civil rights claims, based upon immunity under the HCQIA. The Athens Vascular Defendants also seek summary judgment on Plaintiffs' antitrust claims based upon Plaintiffs' lack of standing.

Having reviewed the motions and responses and having heard oral argument on the motions, the Court grants summary judgment in favor of the ARMC Defendants as to all of Plaintiffs' claims and grants partial summary judgment to the Athens Vascular Defendants as to Plaintiffs' antitrust claims against them. The Court defers ruling on the Athens Vascular Defendants' Motion for Summary Judgment as to Plaintiffs' peer review related claims based upon HCQIA immunity until Plaintiffs are provided with the opportunity to conduct additional limited discovery regarding Defendants' peer review of Dr. Adeduntan.<sup>2</sup>

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<sup>1</sup> [HN1](#) [↑] The HCQIA expressly excludes federal civil rights claims from its immunity provisions. [42 U.S.C. § 11111 \(a\) \(1\)](#).

<sup>2</sup> To overcome Defendants' immunity defense and to prove their federal discrimination claims, Plaintiffs contend that they need to review peer review materials. Defendants take the position that those materials are protected by the Georgia peer review privilege and are not subject to discovery. The ARMC Defendants, who have custody and control of the peer review materials, have filed a Motion for Protective Order, and therefore, those materials have not been produced to Plaintiffs. In light of the Court's grant of summary judgment to the ARMC Defendants and the fact that the Athens Vascular Defendants do not seek summary judgment as to Plaintiffs' federal discrimination claims, a question exists as to whether the peer review privilege issue, which had been presented by the ARMC Defendants in their motion for a protective order, is now necessary to resolve. The Court, as explained in further detail in this Order, finds that the issue must be decided since it is relevant to the Athens Vascular Defendants' summary judgment motion based upon HCQIA immunity and because those peer review materials are relevant to Plaintiffs' federal discrimination claims against the Athens Vascular Defendants, for which no summary judgment motion has been filed.

## [\*4] II. BACKGROUND

Dr. Adeduntan is a physician and surgeon with his own professional medical practice, Victory Vascular & General Surgery of Georgia, P.C., in Athens, Georgia. Dr. Adeduntan is black; his national origin is Nigerian. He first applied for and was granted medical staff privileges at ARMC, a local hospital, on August 28, 1996. These privileges allowed Dr. Adeduntan to admit and treat his patients in the hospital, so that ARMC could provide care for those patients during their stays. Dr. Adeduntan also maintained medical staff privileges at other Athens area hospitals, including St. Mary's Hospital.

ARMC requires that surgeons reapply for medical staff privileges on a regular basis. Dr. Adeduntan did as required, and his privileges were renewed on four separate occasions. In February 2002, Dr. Adeduntan performed an emergency abdominal aortic aneurysm (AAA) surgery in ARMC's operating room. The patient did not survive; the ARMC Defendants state that the patient died during the procedure, while Dr. Adeduntan contends that the patient was "clinically dead" before he was ever contacted for surgery.

Afterwards, ARMC's Surgical Case Review Committee conducted a peer [\*5] review of the procedure and recommended to the credentialing committee that Dr. Adeduntan complete a continuing education course or arrange for a local proctor before performing the same procedure again at ARMC. Dr. Adeduntan appealed this recommendation and agreed to refrain from performing the procedure while the matter was unresolved. He still maintained all other medical staff privileges at ARMC at that time.<sup>3</sup>

On September 3 and October 6, 2003, Dr. Adeduntan filed two charges of discrimination with the EEOC regarding ARMC's peer review process.<sup>4</sup> Dr. Adeduntan applied for reappointment to the medical staff at ARMC on March 24, 2003, and ARMC granted him a six-month extension pending resolution of the peer review process on April 23, 2003. A second extension was granted in October 2003. On February 9, 2004, Dr. Adeduntan and the ARMC Defendants [\*6] executed a Peer Review Resolution Agreement (PRRA), intended to encompass all issues and claims related to the peer review process. Dr. Adeduntan's privileges lapsed at the end of April 2004.<sup>5</sup> He commenced this proceeding on July 1, 2004.

## III. SUMMARY JUDGMENT STANDARD

[HN2](#) [Federal Rule of Civil Procedure 56\(c\)](#) [\*7] provides that summary judgment shall be granted "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law."

An issue of fact is "material" if, under the applicable substantive law, it might affect the outcome of the case. [Allen v. Tyson Foods](#) 121 F.3d 642, 646 (11th Cir. 1997). An issue of fact is "genuine" if the record taken as a whole could lead a rational trier of fact to find for the nonmoving party. *Id.* [HN3](#) A court must decide "whether the evidence presents a sufficient disagreement to require submission to a jury or whether it is so one-sided that one party must

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<sup>3</sup> It appears that until April 30, 2004, when all of his staff privileges lapsed, Dr. Adeduntan maintained all privileges except for permission to perform AAA surgeries.

<sup>4</sup> The first charge of discrimination alleged that Dr. Adeduntan was subjected to peer review, had limited hospital privileges, and faced future loss of his hospital privileges because of his race and national origin. His second charge stated that he was subject to retaliation for filing the first charge.

<sup>5</sup> The ARMC Defendants state that Dr. Adeduntan's privileges lapsed because his application to renew them was incomplete in three ways: (1) he did not provide an appropriate written opinion from Dr. Vittimberga in accordance with the PRRA (discussed in more detail *infra*); (2) the reference from St. Mary's Hospital was not timely received; and (3) the reference from Elberton Hospital was never received.

prevail as a matter of law." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 251, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986).

**HN4** The moving party bears "the initial responsibility of informing the . . . court of the basis for its motion, and identifying those portions of the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any,' which it believes demonstrate the absence of [\*8] a genuine issue of material fact." *Celotex Corp. v. Catrett* 477 U.S. 317, 323, 91 L. Ed. 2d 265, 106 S. Ct. 2548 (1986). Where the nonmoving party bears the burden of proof at trial, the moving party may discharge this "initial responsibility" by showing that there is an absence of evidence to support the nonmoving party's case or by showing that the nonmoving party will be unable to prove its case at trial. *United States v. Four Parcels of Real Property* 941 F.2d 1428, 1437-38 (11th Cir. 1991). **HN5** To survive summary judgment, the nonmoving party bearing the ultimate burden of proof at trial must come forward with evidence sufficient to withstand a directed verdict motion. *Fitzpatrick v. City of Atlanta* 2 F.3d 1112, 1116 (11th Cir. 1993).

**HN6** On summary judgment, "the evidence of the non-movant is to be believed." *Anderson* 477 U.S. at 255. **HN7** "The district court should resolve all reasonable doubts about the facts in favor of the non-movant, and draw all justifiable inferences . . . in his favor." *Four Parcels*, 941 F.2d at 1437 (internal quotations and citations omitted).

## IV. DISCUSSION

### A. The ARMC Defendants and the PRRA Release

[\*9] Dr. Adeduntan and the ARMC Defendants entered into the PRRA as a means of resolving the peer review process without resorting to a formal medical staff hearing. The PRRA acknowledges that Dr. Adeduntan had voluntarily discontinued performing AAA procedures during the peer review process and set forth the recommendation of the credentialing committee to which Dr. Adeduntan had objected (namely, that he receive additional instruction in performing the procedure or arrange for local proctoring). The substantive terms of the agreement set forth that

Based upon direct observation of Dr. Adeduntan performing AAA procedure(s) (exact number to be determined by Dr. Vittimberga, but more than one), Dr. Vittimberga will provide a written opinion to the Credentials Committee that Dr. Adeduntan has the requisite clinical skills to perform the AAA procedure consistent with the standard of care. Further, Dr. Adeduntan agrees to a retrospective review of his next five (5) AAA surgeries at ARMC.

The Credentials Committee will deem Dr. Vittimberga's opinion and certification as sufficient evidence of Dr. Adeduntan's competence and qualification in performing AAA procedures, and his agreement to [\*10] refrain from performing AAA surgery will no longer be necessary. In the event Dr. Vittimberga fails to certify Dr. Adeduntan's competence and qualifications in performing these procedures, this matter will be referred back to the Credentials Committee for consideration, with input, as requested, from Dr. Adeduntan and Dr. Vittimberga.

The release of the PRRA provided that

Each party hereto unconditionally releases, remises, discharges, and acquits the other party from each, every, and all claims, both in law and in equity, and all expenses, debts, covenants, liabilities, or responsibilities in any way relating to or arising from said claims, which either party had or now has against the other party, whether known or unknown, and whether foreseen or unforeseen arising from, or in any way connected directly or indirectly with, or otherwise related to the peer review investigation of Case No. 10-63-13 and the hearing regarding the same. The release of ARMC is limited only to ARMC, Athens Regional Health Services, Inc., Athens Regional Medical Center, Inc., Hospital Authority of Clarke County, Georgia, Athens Regional Foundation, Inc., Athens Regional Health Resources, Inc., Athens [\*11] Area Health Plan Select, Inc., Athens Regional Physician Services, Inc., Regional FirstCare, Inc., Athens Regional Health Ventures, Inc., Athens Area Health Plan Governance Committee and Athens Regional Home Health.

Dr. Adeduntan further acknowledges and agrees that with respect to the rights and claims he is waiving, to [sic] he is not only waiving his right to recover money or any other relief in any action he might commence, but also his right to file and recover in any action brought on his behalf against ARMC by any other party, including, but not limited to the United States Equal Employment Opportunity Commission or any other federal, state or local government agency or department.

ARMC and Dr. Adeduntan expressly agree that this release does not preclude Dr. Adeduntan from bringing any and all claims, demands, rights, causes of action and/or seeking evidence arising out of any other matter or against any other party, including, but not limited to, any claims, demands, rights, or causes of action that are presently pending in the State Court of Clarke County.

The ARMC Defendants contend that this release bars all of Plaintiffs' claims arising out of the peer review [\*12] process before February 9, 2004, the effective date of the PRRA. In response, Plaintiffs argue that the PRRA is unenforceable as a whole because the agreement lacks consideration or, in the alternative, the release is unenforceable because the ARMC Defendants materially breached the terms of the agreement.

## **1. Enforceability of Release**

### **a. Consideration**

The Court finds Plaintiffs' argument that the agreement lacks consideration to be without merit. If Dr. Adeduntan complied with the conditions set forth in the agreement, the ARMC Defendants agreed to reinstate his privileges in full and to discontinue any further peer review process. The PRRA also provides that any individual or entity inquiring into Dr. Adeduntan's standing at ARMC would be informed that he had no pending disciplinary actions and that he maintained privileges in good standing. The PRRA also contained a mutual release of claims arising from the peer review process. The agreement therefore was supported by more than adequate consideration.

### **b. Breach of Contract**

Plaintiffs contend that the ARMC Defendants breached the terms of the PRRA, rendering any release of claims contained in the agreement unenforceable. [\*13] The breach occurred, according to Plaintiffs, when ARMC refused to accept the written opinion of Dr. Vittimberga certifying Dr. Adeduntan's competence. In response, the ARMC Defendants contend that the written opinion of Dr. Vittimberga did not comply with the terms of the PRRA.

Plaintiffs' allegation of breach of contract requires a review of additional facts regarding the procurement of Dr. Vittimberga's written opinion. After entering into the PRRA, Dr. Adeduntan sent a letter to Dr. Vittimberga dated March 8, 2004, requesting that Dr. Vittimberga send a letter to ARMC regarding Dr. Adeduntan's qualifications to perform the AAA procedure. Dr. Adeduntan essentially dictated the letter's content to Dr. Vittimberga, instructing that it should read: "Based on direct observations; I hereby certify that Dr. Azeez Adeduntan; is a well trained Surgeon who is highly qualified & competent in performing Abdominal Aortic Aneurysms (AAA) procedures consistent with the standard of Care."<sup>6</sup> On March 17, 2004, Dr. Vittimberga sent a one-sentence letter to ARMC containing language that was nearly the verbatim language requested by Dr. Adeduntan. Dr. Vittemberga included with his letter a copy [\*14] of Dr. Adeduntan's March 8 letter to him.

Dr. Cecil Hudson, Chief Medical Officer at ARMC, contacted Dr. Vittimberga to follow up on the letters he received. When asked the date of his observation of Dr. Adeduntan's performance of AAA procedures, Dr. Vittimberga responded that he had observed Dr. Adeduntan performing the procedure eight years prior, while Dr. Adeduntan was in a training program for residents and fellows in vascular surgery under Dr. Vittimberga's supervision. This additional information led Dr. Hudson to subsequently inform Dr. Adeduntan that the written opinion of Dr. Vittimberga did not satisfy the requirement of direct observation in the PRRA.

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<sup>6</sup> Punctuation and capitalization as in original.

The issue for the Court is the meaning of the direct observation requirement in the PRRA. [HN8](#)<sup>↑</sup> The starting point in contract construction under Georgia law is "to look at the four corners of the instrument to determine the intention of the parties from the language employed." [Livoti v. Aycock, 263 Ga. App. 897, 901-02, 590 S.E.2d 159, 164 \(2003\)](#). [\*15] In making this determination, "all the attendant and surrounding circumstances may be proved, but not explained." *Id.*; see also [O.C.G.A. § 13-2-3](#). If the language of the agreement is "clear, unambiguous, and capable of only one reasonable interpretation, no construction is necessary or even permissible by the court." [Estate of Sam Farkas, Inc. v. Clark, 238 Ga. App. 115, 119-20, 517 S.E.2d 826, 830 \(1999\)](#) (quoting [Reahard v. Ivester, 188 Ga. App. 17, 19, 371 S.E.2d 905, 907 \(1988\)](#)). [HN9](#)<sup>↑</sup> An "[a]mbiguity in a contract is defined as duplicity, indistinctness, or an uncertainty of meaning or expression." [Thomas v. B&I Lending, LLC, 261 Ga. App. 39, 41, 581 S.E.2d 631, 634 \(2003\)](#). "[A] mere lack of clarity on casual reading is not the criterion for determining whether a contract is afflicted with ambiguity." [McCann v. Glynn Lumber Co., 199 Ga. 669, 679, 34 S.E.2d 839, 845 \(1945\)](#).

Plaintiffs assert that the language of the PRRA is silent as to whether the direct observation requirement is prospective or retrospective, so that Dr. Vittimberga's previous observation of Dr. Adeduntan satisfies [\*16] its terms.<sup>7</sup> The plain language of the PRRA does not support Plaintiffs' argument. The language of the agreement is in the present tense and written in a way that contemplates future action: the number of procedures observed is "to be determined" by Dr. Vittimberga; Dr. Vittimberga is to determine whether Dr. Adeduntan "has" the competency to perform AAA procedures. The language regarding the number of procedures to be observed by Dr. Vittimberga is particularly awkward when attempting to interpret it in Plaintiffs' suggested manner; the provision that the number of procedures observed is "to be determined by Dr. Vittimberga" is rendered meaningless if viewed retrospectively, considering that Dr. Vittimberga has apparently already observed Dr. Adeduntan perform a finite number of AAA procedures under his previous supervision. Plaintiffs' interpretation of the language of the direct observation requirement is tortured and overreaching. The clear and unambiguous language of the agreement clearly evinces the parties' intention that the direct observation requirement is prospective in nature, and the Court finds that it is the only reasonable interpretation of that provision.

[\*17] For that reason, Plaintiffs have not demonstrated that Defendants breached the terms of the PRRA, nor have they offered any other legal basis supporting their contention that the PRRA is not enforceable. The Court finds as a matter of law that the release contained in the PRRA is enforceable. The next issue is whether Plaintiffs released the claims that they assert in this lawsuit.

## 2. Scope of Release

Plaintiffs have asserted federal claims against the ARMC Defendants under [42 U.S.C. §§ 1981, 1983, and 1985](#); Title VII; and the Sherman Act. The Court finds, that according to the terms of the release, it encompasses all of Plaintiffs' claims in this suit:

Each party hereto unconditionally releases, remises, discharges, and acquits the other party from each, every, and all claims, both in law and in equity, and all expenses, debts, covenants, liabilities, or responsibilities in any way relating to or arising from said claims, which either party had or now has against the other party, whether known or unknown, and whether foreseen or unforeseen arising from, or in any way connected directly or

<sup>7</sup> Plaintiffs' logic is inconsistent with the law in that they seem to argue that because the direct observation requirement was ambiguous as to whether it was prospective or retrospective in nature, they have satisfied the requirement by fulfilling it according to their interpretation. [HN10](#)<sup>↑</sup> Under Georgia law, if an ambiguity exists in an agreement, the court should attempt to resolve the ambiguity by applying the statutory rules of contract construction. [Atlanta Dev., Inc. v. Emerald Capital, 258 Ga. App. 472, 476, 574 S.E.2d 585, 589 \(2002\)](#). If the ambiguity cannot be negated by applying the rules of construction, then parol evidence may be introduced, and the issue of what was intended by the parties is a matter for a jury to decide. [Livoti, 263 Ga. App. at 903, 590 S.E.2d at 164](#). Simply establishing that an ambiguity exists does not mean that Plaintiffs' interpretation must prevail.

indirectly with, or otherwise related to the peer review [\*18] investigation of Case No. 10-63-13 and the hearing regarding the same.

All of the federal claims Plaintiffs have asserted are related to the peer review process. Moreover, since Plaintiffs' state law claims of negligent and intentional infliction of emotional distress arise from the peer review process, they are also covered by the release in the PRRA.

During the hearing on Defendants' motion, Plaintiffs attempted to identify other instances of discriminatory conduct that occurred outside the peer review process, giving rise to independent and discrete causes of action. Plaintiffs stated that the ARMC Defendants: (1) sent the police to Dr. Adeduntan's home on one occasion; (2) encouraged an employee to file a sexual harassment complaint against Dr. Adeduntan; (3) sent Dr. Adeduntan more uninsured patients than other doctors; (4) referred a patient complaint to the State Medical Board rather than handling it internally; (5) posted a confidential letter written by Dr. Adeduntan in the doctors' lounge; (6) made unnecessary chart reviews of Dr. Adeduntan's cases; and (7) placed observers in the operating room.

While these alleged acts may be probative of Dr. Adeduntan's clearly [\*19] asserted discrimination claims, Plaintiffs have failed to demonstrate that each separate instance of conduct alleged is actionable. First, Plaintiffs failed to allege specifically in their Complaint any facts relating to the complaint of alleged sexual harassment against Dr. Adeduntan; the inclusion of observers in Dr. Adeduntan's operating room; or the excessive review of Dr. Adeduntan's patient charts. [HN11](#)[<sup>↑</sup>] Plaintiffs may not amend their Complaint "through argument . . . opposing summary judgment." [\*Gilmour v. Gates, McDonald & Co., 382 F.3d 1312, 1315 \(11th Cir. 2004\)\*](#). The remaining incidents, which were raised by Plaintiffs in the Complaint, either do not constitute actionable discriminatory conduct or are part of the peer review process and covered by the PRRA.

Because all of Plaintiffs' viable claims against the ARMC Defendants are encompassed and therefore barred by the release in the PRRA, the Court grants summary judgment to the ARMC Defendants on all of Plaintiffs' federal and state law claims.<sup>8</sup>

## [\*20] B. Antitrust Claims

Plaintiffs have brought a private suit for alleged restraint of trade and monopoly under the federal antitrust statutes against the ARMC Defendants and the Athens Vascular Defendants.<sup>9</sup> [HN12](#)[<sup>↑</sup>] The Sherman Act declares "[e]very contract, combination . . . or conspiracy, in restraint of trade or commerce among the several States . . . to be illegal," [15 U.S.C. § 1](#), and also prohibits the monopoly of, "or attempt to monopolize, or combine and conspire with any other person or persons, to monopolize any part of trade or commerce among the several States. . . ." [15 U.S.C. § 2](#). [HN13](#)[<sup>↑</sup>] Private enforcement suits for damages caused by violations of the Sherman Act are permitted under the Clayton Act, [15 U.S.C. § 15](#). The Clayton Act allows successful plaintiffs to recover treble damages. *Id.*

[\*21] Defendants argue that they are entitled to summary judgment on Plaintiffs' antitrust claims because Plaintiffs do not have legal standing to assert those claims. [HN14](#)[<sup>↑</sup>] Standing under the Clayton Act has been described by the Eleventh Circuit "as a search for the proper plaintiff to enforce the **antitrust law**." [\*Todorov v. DCH Healthcare Auth., 921 F.2d 1438, 1448 \(11th Cir. 1991\)\*](#). As a result, the courts have developed a two-step inquiry to evaluate whether a plaintiff has antitrust standing: (1) "a court should determine whether the plaintiff suffered antitrust

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<sup>8</sup>In light of this ruling, it is unnecessary to address the ARMC Defendants' Motion for Partial Summary Judgment on Dr. Adeduntan's Title VII claim based upon their contention that they were not his employer.

<sup>9</sup>The only remaining antitrust claims are those asserted against the Athens Vascular Defendants. The release in the PRRA bars Plaintiffs' antitrust claims against the ARMC Defendants. The Court notes that Defendant Hospital Authority of Athens-Clarke County is not in any event subject to Plaintiffs' antitrust claims as an instrumentality, agency, or political subdivision of Athens-Clarke County, which Plaintiffs concede in their Complaint. (Compl. at PP 64, 69.) Even if the PRRA did not operate to bar Plaintiffs' antitrust claims against the ARMC Defendants, they would still be entitled to summary judgment for the reasons stated herein.

injury"; and then, (2) "the court should determine whether the plaintiff is an efficient enforcer of the antitrust laws." *Id. at 1449.*

**HN15**[<sup>15</sup>] An antitrust injury has been defined by the Supreme Court as injury of the type the antitrust laws were intended to prevent and that flows from that which makes the defendants' acts unlawful. The injury should reflect the anticompetitive effect either of the violation or of anticompetitive acts made possible by the violation. It should, in short, be "the type of loss that the claimed violations . . . would be likely to cause."

*Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 489, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977) [\*22] (quoting *Zenith Radio Corp. v. Hazeltine Research*, 395 U.S. 100, 125, 23 L. Ed. 2d 129, 89 S. Ct. 1562 (1969)). This "requires the antitrust plaintiff to show that his own injury coincides with the public detriment tending to result from the alleged violation . . . increas[ing] the likelihood that public and private enforcement of the antitrust laws will further the same goal of increased competition." *Todorov*, 921 F.2d at 1450 (quoting *Austin v. Blue Cross & Blue Shield of Ala.*, 903 F.2d 1385, 1389 (11th Cir. 1990)).

Plaintiffs allege in their Complaint that the Defendants "have conspired to impose and have imposed an unreasonable restraint on the vascular surgery market in and around Athens-Clarke County, Georgia" and "have engaged in predatory or anticompetitive conduct with the specific intent to monopolize the Athens-Clarke County area vascular surgery market." The effect of this conduct, Plaintiffs allege, has been economic injury caused by the Defendants' attempt to drive Plaintiffs out of the vascular surgery market.

In *Todorov* the Eleventh Circuit denied antitrust standing to a physician who did not receive the staff privileges he requested because [\*23] it found that the doctor had shown only that he had been deprived of "the profits he would have garnered had he been able to share a part of the . . . supercompetitive, or monopoly, profits." *Id. at 1453-54.* This injury clearly did not fall within the definition of an antitrust injury because **HN16**[<sup>16</sup>] "the antitrust laws were not enacted to permit one person to profit from the anticompetitive behavior of another." *Id. at 1454.*

The type of harm complained of by Plaintiffs in this case is of the type deemed insufficient for antitrust standing in *Todorov*. As the Supreme Court has noted, **HN17**[<sup>17</sup>] the legislative intent behind the antitrust statutes was "the protection of competition, not competitors." *Brown Shoe Co. v. United States* 370 U.S. 294, 320, 8 L. Ed. 2d 510, 82 S. Ct. 1502 (1962). The harm alleged in the Complaint is harm to the individual doctor, not to competition within the marketplace. **HN18**[<sup>18</sup>] The aim of the Sherman Act "is not to protect businesses from the working of the market; it is to protect the public from the failure of the market."<sup>10</sup> *Spanish Broad. Sys. of Fla., Inc. v. Clear Channel Communications, Inc.*, 376 F.3d 1065, 1069 (11th Cir. 2004) (quoting *Spectrum Sports v. McQuillan*, 506 U.S. 447, 459, 122 L. Ed. 2d 247, 113 S. Ct. 884 (1993)). [\*24] For that reason, "the law directs itself not against conduct which is competitive, even severely so, but against conduct which unfairly tends to destroy competition itself." *Id.* Plaintiffs have failed to demonstrate that they have suffered the type of antitrust injury contemplated under the Sherman Act.

[\*25] **HN19**[<sup>19</sup>] Even if Plaintiffs were able to establish that they suffered antitrust injury, they still must demonstrate that they are efficient enforcers of the antitrust laws. This analysis requires consideration of several factors "that might be useful in determining whether a party is a proper plaintiff in a particular [antitrust] suit." *Todorov*, 921 F.2d at 1451. These factors include: (1) the directness of the injury and whether there "exists an identifiable class of persons whose self-interest would motivate them to vindicate the public interest in antitrust

<sup>10</sup> The Athens Vascular Defendants also provide numerous citations to cases outside the Eleventh Circuit that have similarly found that denial of a doctor's hospital privileges does not satisfy the requirement of antitrust injury. See, e.g., *Patel v. Midland Mem'l Hosp. & Med. Ctr.*, 298 F.3d 333, 346 (5th Cir. 2002) (finding suspension of privileges at one hospital did not eliminate plaintiff as competitor when he continued to treat patients at another facility); *BCB Anesthesia Care, Ltd. v. Passavant Mem'l Area Hosp. Ass'n*, 36 F.3d 664, 667, 668-69 (7th Cir. 1994) (holding anesthetists failed to show impact on competition, rather than themselves and also collecting federal cases that have reached same conclusion on antitrust claims); *Austin v. McNamara*, 979 F.2d 728, 739 (9th Cir. 1992) (noting that "[e]ven the elimination of a single competitor, standing alone, does not prove anticompetitive effect. . . . [I]njury to competition, beyond the impact on the claimant" is required).

enforcement"; (2) the nature of the damages; (3) the importance of avoiding duplicative recoveries; and (4) whether the plaintiff can enforce an antitrust judgment efficiently and effectively. *Id. at 1451-52*. Considering those factors, Plaintiffs are not appropriate enforcers. All of Plaintiffs' allegations relate to the economic harm suffered by Plaintiffs, and there are no allegations regarding the effect of the alleged anticompetitive behavior on the consumers in the market. Parties who "have a stronger interest in ensuring that prices and services remain at competitive levels" are the appropriate [\*26] enforcers of antitrust laws. *Robles v. Humana Hosp. Cartersville*, 785 F. Supp. 989, 999. Plaintiffs' interest "is that [they] be allowed to compete . . . not that patients receive quality services at competitive prices." <sup>11</sup> *Id.*

Plaintiffs [\*27] have therefore failed to show that they meet either prong of the two-step inquiry into antitrust standing. Because they lack antitrust standing, the Court grants summary judgment in favor of the Athens Vascular Defendants as to Plaintiffs' antitrust claims.

### C. HCQIA Immunity

The Athens Vascular Defendants seek summary judgment as to Plaintiffs' state law claims based upon HCQIA immunity. [HN20](#)[] Individuals associated with a medical "professional review action"-including a professional review body, members or staff of the body, persons under contract with the body, and persons who participate or assist with the review action-are entitled to immunity from damages under federal and state law under the HCQIA. <sup>12</sup> [42 U.S.C. § 11111\(a\)](#). [HN21](#)[] A "professional review action" is defined as:

[A]n action or recommendation of a professional review body . . . which is based on the competence or professional conduct of an individual physician (which conduct affects or could affect adversely the health or welfare of a patient or patients) and which affects (or may affect) adversely the clinical privileges, or membership in a professional society, of the physician. Such [\*28] term includes a formal decision of a professional review body not to take an action or make a recommendation . . . and also includes professional review activities relating to a professional review action.

[42 U.S.C. § 11151\(9\)](#).

If the action at issue meets this definition, the HCQIA also sets forth precise standards for such actions that must be fulfilled for the immunity provision to apply. [HN23](#)[] For immunity to apply, the review action must have been pursued:

(1) in the reasonable belief that the action was in furtherance of quality health care, (2) after a reasonable effort to obtain the [\*29] facts of the matter, (3) after adequate notice and hearing procedures are afforded to the physician involved or after such other procedures as are fair to the physician under the circumstances, and (4) in the reasonable belief that the action was warranted by the facts known after such reasonable effort to obtain facts and after meeting the requirement of paragraph (3).

<sup>11</sup> Plaintiffs note that St. Mary's Hospital, where Dr. Adeduntan also maintains privileges, lacks open heart and dedicated angioplasty facilities. Although these are not facilities needed for Dr. Adeduntan to perform his surgeries, Plaintiffs submit that they may be needed for some of his patients, who often suffer from heart-related problems. Plaintiffs contend that the limited facilities at St. Mary's therefore impact Dr. Adeduntan's ability to treat patients there because patients may require a transfer from St. Mary's to ARMC, resulting in financial impact on those patients. However, the Court finds that this connection between vascular surgery and cardiac procedures is still insufficient to establish antitrust injury to the competition for vascular surgery in the Athens-Clarke area.

<sup>12</sup> [HN22](#)[] The statute excludes civil rights actions brought under state or federal law. [42 U.S.C. § 11111\(a\)\(1\)](#). Accordingly, the immunity sought would apply to Plaintiffs' antitrust claims-which the Court has already disposed of on other grounds-and their state law claims of intentional infliction of emotional distress and negligent infliction of emotional distress.

42 U.S.C. § 11112 (a). A professional review action is presumed to have met these standards, but the presumption is rebuttable by a preponderance of the evidence. *Id.* The standard for resolving this issue at summary judgment is therefore: "Might a reasonable jury, viewing the facts in the best light for [the plaintiff], conclude that he has shown, by a preponderance of the evidence, that the defendants' actions are outside the scope of § 11112 (a)?" Bryan v. James E. Holmes Reg'l Med. Ctr., 33 F.3d 1318, 1333 (11th Cir. 1994) (quoting Austin v. McNamara, 979 F.2d 728, 735 (9th Cir. 1992)).

It is clear that the peer review process undertaken by ARMC of Dr. Adeduntan fits within the statutory definition of a professional review action. However, Plaintiffs [\*30] have been denied a full opportunity to rebut the presumption of immunity because they have been denied access to the peer review materials that may show that Defendants' actions were outside the scope of activity protected by HCQIA immunity.<sup>13</sup> The Athens Vascular Defendants seek to invoke a federal law peer review immunity defense while at the same time indirectly finding refuge in a state law peer review privilege asserted by a fellow Defendant that has the effect of denying Plaintiffs the opportunity to rebut the immunity defense. The Court therefore must determine whether the peer review materials sought by Plaintiffs are protected from discovery under federal law based upon Georgia's peer review statute. If they are privileged and thus not discoverable, then no evidence exists (and none would be forthcoming) to rebut the HCQIA immunity defense, and the Athens Vascular Defendants would be entitled to summary judgment. However, if those materials are not privileged, then Plaintiffs should be given the opportunity to conduct limited discovery regarding those materials before being subjected to summary judgment.

#### [\*31] 1. Georgia's Peer Review/Medical Review Committee Privileges

HN24[<sup>↑</sup>] Georgia has codified its peer review and medical review privileges. O.C.G.A. §§ 31-7-133, 31-7-143. The peer review statute provides that

HN25[<sup>↑</sup>] [T]he proceedings and records of a review organization shall be held in confidence and shall not be subject to discovery or introduction into evidence in any civil action; and no person who was in attendance at a meeting of such organization shall be permitted or required to testify in any such civil action as to any evidence or other matters produced or presented during the proceedings or activities of such organization or as to any findings, recommendations, evaluations, opinions, or other actions of such organization or any members thereof. The confidentiality provisions of this article shall also apply to any proceedings, records, actions, activities, evidence, findings, recommendations, evaluations, opinions, data, or other information shared between review organizations who are performing a peer review function or disclosed to a government agency as required by law. However, information, documents, or records otherwise available from original [\*32] sources are not to be construed as immune from discovery or use in any such civil action merely because they were presented during proceedings of such organization, nor should any person who testifies before such organization or who is a member of such organization be prevented from testifying as to matters within the person's knowledge; but such witness cannot be asked about such witness's testimony before such organization or about opinions formed by such witness as a result of organization hearings.

O.C.G.A. § 31-7-133. HN26[<sup>↑</sup>] The language of O.C.G.A. § 31-7-143 is substantially the same, substituting "medical review committee" for peer review organization. At least one federal district court within Georgia has described the effect of the peer review statutes as "confer[ring] upon peer review organizations the qualities of a black hole; what goes in does not come out, and, unless the information exists in duplicate in the surrounding orbit, nothing that went in is discoverable." Doe v. UNUM Life Ins. Co. of Am., 891 F. Supp. 607, 610 (N.D. Ga. 1995). The Georgia Supreme Court has recognized that HN27[<sup>↑</sup>] in enacting [\*33] these statutes, "the General Assembly has placed an absolute embargo upon the discovery and use of all proceedings, records, findings, and recommendations of peer review groups and medical review committees in civil litigation." Emory Clinic v. Houston, 258 Ga. 434, 434-35, 369 S.E.2d 913, 913 (1988) (per curiam).

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<sup>13</sup> As noted previously, the ARMC Defendants have refused to produce any peer review materials based upon their contention that such materials are not discoverable because of the Georgia peer review privilege.

Defendants urge the Court to adopt this state law privilege and apply it in this case pursuant to [Rule 501 of the Federal Rules of Evidence](#). [HN28](#)<sup>14</sup> [Rule 501](#) sets forth the rules of evidentiary privilege as they are applied in federal court, providing that

[HN29](#)<sup>15</sup> Except as otherwise required by the Constitution of the United States or provided by Act of Congress or in rules prescribed by the Supreme Court pursuant to statutory authority, the privilege of a witness, person, government, State, or political subdivision thereof shall be governed by principles of the common law as they may be interpreted by the courts of the United States in the light of reason and experience. However, in civil actions and proceedings, with respect to an element of a claim or defense as to which State law supplies the rule of decision, the privilege [\*34] . . . shall be determined in accordance with State law.

[Fed. R. Evid. 501](#). [HN30](#)<sup>16</sup> The rule "clearly provides federal courts with the statutory power to recognize new or novel" evidentiary privileges." [In re Int'l Horizons, Inc.](#) 689 F.2d 996, 1003 (11th Cir. 1982). However, courts do not "create and apply an evidentiary privilege unless it promotes sufficiently important interests to outweigh the need for probative evidence." [Univ. of Pa. v. EEOC](#), 493 U.S. 182, 189, 107 L. Ed. 2d 571, 110 S. Ct. 577 (1990) (quoting [Trammel v. United States](#) 445 U.S. 40, 51, 63 L. Ed. 2d 186, 100 S. Ct. 906 (1980)).

[HN31](#)<sup>17</sup> "Peer review, the process by which physicians and hospitals evaluate and discipline staff doctors, has become an integral component of the health care system in the United States." [Bryan v. James E. Holmes Reg'l Med. Ctr.](#) 33 F.3d 1318, 1321 (11th Cir. 1994). While the peer review privilege has been upheld in a few cases within the Eleventh Circuit, those cases are distinguishable from the instant action on the basis that they did not involve the HCQIA immunity defense; nor did they involve federal civil rights claims. See [Somer v. Johnson](#) 704 F.2d 1473, 1479 (11th Cir. 1983) [\*35] (upholding similar privilege under Florida law in medical malpractice diversity action); [Doe](#), 891 F. Supp. at 609 (upholding privilege under Georgia law where insurance company sought information regarding physician's suspended privileges due to alleged drug abuse). There is no Eleventh Circuit authority addressing application of the peer review privilege in a federal question case, particularly in a case involving the HCQIA immunity defense or civil rights claims of discrimination.<sup>14</sup> The Court understands the decision the Georgia legislature has made in adopting its peer review privilege: [HN32](#)<sup>18</sup> "[T]he enactment of such statutes represents a proper legislative choice between the competing public concerns of fostering medical staff candor, on the one hand, and impairing medical malpractice plaintiffs' access to evidence, on the other hand." [Eubanks v. Ferrier](#) 245 Ga. 763, 765, 267 S.E.2d 230, 232 (1980). However, when a state law privilege would essentially prevent a plaintiff from rebutting a federal immunity defense or would defeat a federal claim which bears little relation to the type of claim the privilege was designed to address, the need for probative [\*36] evidence sufficiently outweighs the interests protected by the privilege.<sup>15</sup> The Court therefore finds that the Georgia peer review privilege cannot be used to prevent Plaintiffs from discovering peer review materials that may be relevant to rebut the Athens Vascular Defendants' HCQIA immunity defense.

## [\*37] 2. Federal Self-Critical Analysis Privilege

Defendants also urge the Court to adopt the federal self-critical analysis privilege, which offers substantially the same protections as the Georgia statutory peer review privilege. The Court has located no Eleventh Circuit decision applying this privilege in the HCQIA immunity context. District courts within the Eleventh Circuit have divided on the

<sup>14</sup> Other circuits have rejected the application of the peer review privilege in federal question or civil rights cases, despite the widespread adoption of such statutory privileges throughout the United States. See [Virmani v. Novant Health, Inc.](#), 259 F.3d 284, 293 (4th Cir. 2001); [Mem'l Hosp. v. Shadur](#), 664 F.2d 1058, 1063 (7th Cir. 1981) (per curiam).

<sup>15</sup> Furthermore, the Court notes that Congress, in enacting the HCQIA and providing immunity from civil damages to individuals who participate in medical peer review proceedings, specifically excluded immunity from suits brought for violations of civil rights. [42 U.S.C. § 11111\(a\)\(1\)](#). [HN33](#)<sup>19</sup> While the HCQIA is certainly intended to promote the peer review process, it does not, by its terms, completely bar confidential peer review information from disclosure, particularly in cases where the peer review process itself is at issue.

issue of whether the privilege should be applied in discrimination cases. Compare *Reid v. Lockheed Martin Aeronautics Co.*, 199 F.R.D. 379, 384-385 (N.D. Ga. 2001) with *Johnson v. United Parcel Serv., Inc.*, 206 F.R.D. 686, 690 (M.D. Ala. 2002). The Supreme Court has rejected the application of the privilege to peer review materials associated with a professor's denial of tenure. *Univ. of Pa.* 493 U.S. at 189.

The Eleventh Circuit has not explicitly recognized the self-critical analysis privilege, joining other federal Courts of Appeal in failing to do so. See *Dowling v. Am. Haw. Cruises, Inc.*, 971 F.2d 423, 425-26 & n.1 (9th Cir. 1992); *FTC v. TRW, Inc.* 202 U.S. App. D.C. 207, 628 F.2d 207, 210 (D.C. Cir. 1980); *Emerson Elec. Co. v. Schlesinger* 609 F.2d 898, 907 (8th Cir. 1979). [\*38] <sup>16</sup> **HN34**<sup>↑</sup> As a matter of federal common law, the self-critical analysis privilege does not exist. The Court finds that under the circumstances of this case such privilege cannot be applied to prevent the discovery of limited peer review materials.

Based on the foregoing, the Court finds that limited peer review materials are discoverable in this case. Therefore, the Court defers ruling on the Athens Vascular Defendants' summary judgment motion based on the HCQIA immunity defense, until this discovery has been completed.

#### **D. The ARMC Defendants' Motion for Protective Order**

As previously mentioned, the ARMC Defendants have filed a Motion for Protective Order to avoid having to produce the peer review materials sought by Plaintiffs in their discovery requests. For the reasons stated in this Order, the Court has concluded that those materials are not absolutely [\*39] protected under the circumstances of this case. However, the Court also finds that Plaintiffs' discovery requests are overly broad. The Court finds that Plaintiffs' discovery should be limited to those materials that pertain to the peer review specifically undertaken of Dr. Adeduntan arising from the emergency AAA surgery that precipitated the peer review in the first place. The Court therefore denies the ARMC Defendants' motion for a protective order to the extent they seek to prohibit Plaintiffs' access to Dr. Adeduntan's peer review materials, as described hereinabove. Accordingly, the ARMC Defendants are ordered to produce those peer review materials to Plaintiffs within thirty days of the date of this Order.<sup>17</sup>

#### **[\*40] V. CONCLUSION**

The ARMC Defendants' Motion for Summary Judgment is granted as to all of Plaintiffs' claims. The Athens Vascular Defendants' Motion for Partial Summary Judgment is granted as to Plaintiffs' antitrust claims. The Court defers ruling on the Athens Vascular Defendants' Motion for Summary Judgment as to Plaintiffs' other claims based upon the HCQIA immunity defense until Plaintiffs have had a reasonable opportunity to complete their limited discovery regarding the peer review materials that the Court has ordered are discoverable. The ARMC Defendants' Motion for Protective Order is denied to the extent described in this Order.<sup>18</sup>

**[\*41] IT IS SO ORDERED**, this 25th day of August, 2005.

CLAY D. LAND

<sup>16</sup> See also Donald P. Vandergrift, Jr., *The Privilege of Self-Critical Analysis: A Survey of the Law* 60 Alb. L. Rev. 171, 180-81 (1996).

<sup>17</sup> The Court observes that although it has granted summary judgment to the ARMC Defendants as to all of Plaintiffs' claims, it retains the authority to order the ARMC Defendants to produce the documents pursuant to *Rule 54 (b) of the Federal Rules of Civil Procedure*, as the Court has not entered final judgment as to those parties.

<sup>18</sup> In light of this ruling, the Court anticipates that the remaining parties may need to amend the scheduling/discovery order for the limited purpose of addressing the scheduling of the additional limited discovery permitted by this Order. The parties are ordered to confer and provide the Court with a proposed amended scheduling order within thirty days of the date of this Order.

UNITED STATES DISTRICT JUDGE

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## Florida v. Tenet Healthcare Corp.

United States District Court for the Southern District of Florida

August 25, 2005, Decided ; August 29, 2005, Filed

CASE NO. 05-20591-CIV-SEITZ, CASE NO. 05-80183-CIV-SEITZ

**Reporter**

420 F. Supp. 2d 1288 \*; 2005 U.S. Dist. LEXIS 41107 \*\*

STATE OF FLORIDA, OFFICE OF THE ATTORNEY GENERAL, DEPARTMENT OF LEGAL AFFAIRS, et al., Plaintiffs, v. TENET HEALTHCARE CORPORATION, Defendant. BOCA RATON COMMUNITY HOSPITAL, INC., d/b/a BOCA RATON COMMUNITY HOSPITAL, on behalf of itself and on behalf of a class of all others similarly situated, Plaintiff, v. TENET HEALTHCARE CORPORATION, Defendant.

**Subsequent History:** Motion granted by [\*Boca Raton Cnty. Hosp. Inc. v. Tenet Healthcare Corp., 2006 U.S. Dist. LEXIS 38560 \(S.D. Fla., Apr. 24, 2006\)\*](#)

Motion granted by [\*Boca Raton Cnty. Hosp. v. Tenet Healthcare Corp., 2006 U.S. Dist. LEXIS 115508 \(S.D. Fla., Dec. 28, 2006\)\*](#)

## **Core Terms**

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outlier, allegations, enterprise, charges, reimbursements, unjust enrichment, conspiracy, costs, motion to dismiss, Threshold, unfair, predicate act, converted, inflated, argues, cases, Pool, regulations, patients, stolen, violations, deceptive, alleged injury, funds, contends, alleged conduct, Medicare Act, turbocharging, proximate cause, alleged facts

## **LexisNexis® Headnotes**

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Public Health & Welfare Law > ... > Medicare > Coverage > General Overview

### **[HN1](#) [down] Medicare, Coverage**

Medicare, established in Title XVIII of the Social Security Act, [\*42 U.S.C.S. § 1395 et seq.\*](#), is the federal program that provides health care insurance to the nation's aged and disabled.

Public Health & Welfare Law > ... > Providers > Reimbursement > General Overview

### **[HN2](#) [down] Providers, Reimbursement**

The outlier provision of Medicare under Title XVIII of the Social Security Act, [\*42 U.S.C.S. § 1395 et seq.\*](#), permits hospitals to request additional payments in any case where charges, adjusted to cost, exceed an amount that the Secretary of Health and Human Services specifies. [\*42 U.S.C.S. § 1395ww\(d\)\(5\)\(A\)\(ii\)\*](#). According to the Centers for

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Medicare & Medicaid Services, this additional payment is designed to protect the hospital from large financial losses due to unusually expensive cases. The outlier payment is meant to approximate the marginal cost of care. [42 U.S.C.S. § 1395ww\(d\)\(5\)\(A\)\(iii\)](#).

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

### [\*\*HN3\*\*](#) Motions to Dismiss, Failure to State Claim

[Fed. R. Civ. P. 12\(b\)\(6\)](#) provides that dismissal of a claim is appropriate when it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations. At this stage of the proceedings, a court must accept the plaintiff's allegations in the complaint as true, and view those allegations in a favorable light to determine whether the complaint states claims for which relief can be granted. Thus, a court may dismiss a complaint for failure to state a claim only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Pleadings > Complaints > General Overview

### [\*\*HN4\*\*](#) Motions to Dismiss, Failure to State Claim

To survive a motion to dismiss, plaintiffs must do more than merely state legal conclusions; they are required to allege some specific factual bases for those conclusions or face dismissal of their claims. Indeed, conclusory allegations, unwarranted factual deductions or legal conclusions masquerading as facts will not prevent dismissal for failure to state a claim. Therefore, in considering motions to dismiss, the court is not bound by the legal conclusions in the complaint, and must look instead at the pleaded facts to determine whether the plaintiffs' claims can proceed through discovery.

Constitutional Law > Supremacy Clause > Federal Preemption

Public Health & Welfare Law > Social Security > Medicare > Medicare Act Interpretation

### [\*\*HN5\*\*](#) Supremacy Clause, Federal Preemption

Medicare is a vast and complicated federal program. In Medicare, Congress has enacted a comprehensive statutory regime and conferred on the Health and Human Services Secretary exceptionally broad authority to prescribe standards for carrying out certain sections of the Social Security Act. Regulatory schemes can displace state law causes of action just as completely as statutes can. However, the federal Medicare statute can be found to preempt state law causes of action if and only if Congress intended it to do so.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Antitrust & Trade Law > ... > Private Actions > Racketeer Influenced & Corrupt Organizations > Scope

### [\*\*HN6\*\*](#) Racketeer Influenced & Corrupt Organizations, Claims

The test for standing under the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), is whether the alleged injury was directly caused by the RICO violation. Further, a RICO plaintiff must demonstrate that its damages flow from the commission of the predicate acts. A plaintiff who complains of harm flowing merely from the misfortunes visited upon a third person by the defendant's acts is generally said to stand at too remote a distance to recover.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

## [HN7](#) [down] Racketeer Influenced & Corrupt Organizations, Claims

Under the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), if the existence of a public authority that could prosecute a claim against putative RICO defendants meant that the plaintiff is too remote, then no private cause of action could ever be maintained, for every RICO predicate offense, as well as the RICO enterprise itself, is separately prosecutable by the government.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Antitrust & Trade Law > ... > Private Actions > Racketeer Influenced & Corrupt Organizations > Scope

## [HN8](#) [down] Racketeer Influenced & Corrupt Organizations, Claims

Pursuant to [18 U.S.C.S. § 1962\(c\)](#) of the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), it is illegal for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity. [18 U.S.C.S. § 1962\(c\)](#). Thus, in order to establish a federal civil RICO violation under [18 U.S.C.S. § 1962\(c\)](#), the plaintiffs must satisfy four elements of proof: (1) conduct; (2) of an enterprise; (3) through a pattern; (4) of racketeering activity. In civil cases, however, RICO plaintiffs must also satisfy the requirements of [18 U.S.C.S. § 1964\(c\)](#), which states that any person injured in his business or property by reason of RICO's substantive provisions has the right to recover threefold the damages he sustains. [18 U.S.C.S. § 1964\(c\)](#). Thus, under [§ 1964\(c\)](#), RICO claimants must show (1) the requisite injury to business or property; and (2) that such injury was by reason of the substantive RICO violation.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

## [HN9](#) [down] Racketeer Influenced & Corrupt Organizations, Claims

For purposes of the Racketeer Influenced and Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), a "pattern of racketeering activity" requires at least two acts of racketeering activity. An act of racketeering is commonly referred to as a predicate act. A pattern of racketeering activity is shown when a racketeer commits at least two distinct but related predicate acts. If distinct statutory violations are found, the predicate acts will be considered to be distinct irrespective of the circumstances under which they arose.

Torts > Intentional Torts > Conversion > Elements

## [HN10](#) [down] Conversion, Elements

To state a claim under [§ 2314](#) of the National Stolen Property Act, a plaintiff must allege (1) that the defendant transported, transmitted or transferred or caused to be transported, transmitted or transferred in interstate commerce, monies that were stolen or converted; (2) that such monies had a value of \$ 5,000 or more; and (3) that the defendant transported the monies willfully and with knowledge that the monies had been stolen or converted. [18 U.S.C.S. § 2314](#).

Torts > Intentional Torts > Conversion > Elements

#### [HN11](#) Conversion, Elements

To allege an [18 U.S.C.S. § 2315](#) violation of the National Stolen Property Act, a plaintiff must show that: (1) the defendant received, possessed, concealed, stored or disposed of stolen money; (2) that such monies had a value in excess of \$ 5,000; (3) that such monies had crossed a state or United States boundary after having been stolen or unlawfully converted; and (4) that the defendant knew that the property had been stolen or unlawfully converted. [18 U.S.C.S. § 2315](#). The word "stolen" includes any wrongful and dishonest taking. Likewise, the word "converted" means the unauthorized exercise of control over the property of another inconsistent with the owner's rights.

Torts > Intentional Torts > Conversion > Elements

#### [HN12](#) Conversion, Elements

Although there must be a taking against the will of the owner for a claim under the National Stolen Property Act, or a trespass to his possession, the requirement is satisfied where the owner is induced by some fraud or trickery to deliver the property to one who feloniously converts it to his own use. In such circumstances there is an absence of real consent and the taking of possession is wrongful.

Torts > Intentional Torts > Conversion > Elements

#### [HN13](#) Conversion, Elements

The legal standard for claims under the National Stolen Property Act requires that a plaintiff allege that the monies that a defendant took did not rightfully belong to the defendant.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

#### [HN14](#) Racketeer Influenced & Corrupt Organizations, Claims

Essential to any successful claim under the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), are the basic requirements of establishing a RICO enterprise. Whatever the pleading requirements for other causes of action, plaintiffs in RICO claims must plead specific facts, not mere conclusory allegations, which establish the enterprise.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

#### [HN15](#) Racketeer Influenced & Corrupt Organizations, Claims

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Under the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), a RICO enterprise exists where a group of persons associates, formally or informally, with the purpose of conducting illegal activity. To allege an enterprise under [18 U.S.C.S. § 1962\(c\)](#), a plaintiff must name a RICO person distinct from the RICO enterprise. The plain language of [§ 1962\(c\)](#) envisions two separate entities. Thus, RICO forbids the imposition of liability where the enterprise is nothing more than a subdivision or part of the person. Where the plaintiffs allege that the enterprise is an association-in-fact, the crucial factor is whether each entity alleged to be part of the association-in-fact is free to act independently and advance its own interests contrary to those' of the other entities.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

#### [HN16](#) Racketeer Influenced & Corrupt Organizations, Claims

Under the Racketeer Influenced and Corrupt Organizations Act (RICO), [18 U.S.C.S. § 1961 et seq.](#), both the United States Supreme Court and the United States Court of Appeals for the Eleventh Circuit have held that the existence of a legal distinction between the RICO defendant and the RICO enterprise is sufficient to establish an enterprise under RICO. Therefore, under established and binding precedent, corporations and their agents are distinct entities for RICO purposes.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Torts > ... > Causation > Proximate Cause > General Overview

#### [HN17](#) Racketeer Influenced & Corrupt Organizations, Claims

The "by reason of" requirement contained in [18 U.S.C.S. § 1964\(c\)](#) of the Racketeer Influenced and Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), implicates two concepts: (1) a sufficiently direct injury so that the plaintiffs have standing to sue; and (2) proximate cause, whereby the allegedly wrongful conduct is shown to be a substantial cause of the alleged injury and the causal connection is foreseeable and not speculative.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Torts > ... > Causation > Proximate Cause > General Overview

#### [HN18](#) Racketeer Influenced & Corrupt Organizations, Claims

It is well-established that plaintiffs under the Racketeer Influenced and Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), must prove proximate causation in order to recover. A proximate cause is not, however, the same thing as sole cause. Instead, a factor is a proximate cause if it is a substantial factor in the sequence of responsible causation.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > Elements

#### [HN19](#) Racketeer Influenced & Corrupt Organizations, Claims

To establish a conspiracy violation under the Racketeer Influenced and Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), specifically [18 U.S.C.S. § 1962\(d\)](#), a plaintiff must allege that the defendant objectively manifested, through words or actions, an agreement to participate in the conduct of the affairs of the enterprise through the commission of two or more predicate crimes. The focus is on the agreement to participate in the enterprise through the pattern of racketeering activity, not on the individual predicate acts. Although the defendant must have agreed to participate in the affairs of the enterprise, the plaintiff may prove agreement: (1) by showing an agreement on an overall objective, or (2) by showing that the defendant agreed personally to commit two predicate acts and therefore to participate in a single objective conspiracy. Further, to be guilty of conspiracy parties must have agreed to commit an act that is itself illegal -- parties cannot be found guilty of conspiring to commit an act that is not itself against the law.

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > Elements

## [\*\*HN20\*\*](#) [] **Racketeer Influenced & Corrupt Organizations, Claims**

The United States Court of Appeals for the Eleventh Circuit has recognized that, particularly at the pleading stage, a conspiracy under the Racketeer Influenced and Corrupt Organizations Act, [18 U.S.C.S. § 1961 et seq.](#), need not be supported by direct evidence, but rather, may be inferred from the parties' conduct.

Contracts Law > Remedies > Equitable Relief > Quantum Meruit

## [\*\*HN21\*\*](#) [] **Equitable Relief, Quantum Meruit**

Under Florida law, to state a claim for unjust enrichment, a plaintiff must allege that: (1) the plaintiff conferred a benefit on the defendant, who had knowledge of the benefit; (2) the defendant voluntarily accepted and retained the benefit; and (3) under the circumstances, it would be inequitable for the defendant to retain the benefit without paying for it.

Contracts Law > Remedies > Equitable Relief > Quantum Meruit

## [\*\*HN22\*\*](#) [] **Equitable Relief, Quantum Meruit**

Liability in unjust enrichment has in principle nothing to do with fault. It has to do with wealth being in one person's hands when it should be in another person's. Thus, the paradigm examples of unjust enrichment are mistaken transfers. However, as soon as a claimant relies on a wrong to supply the unjust factor, the right on which the plaintiff relies arises from that wrong, not from unjust enrichment.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Claims

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

## [\*\*HN23\*\*](#) [] **State Regulation, Claims**

To state a cause of action under the Florida Deceptive and Unfair Trade Practices Act (FDUPTA), Fla. Stat. § 501 et seq., the complaint must not only plead that the conduct complained of was unfair and deceptive, but also that the complaining party was aggrieved by the alleged act. A FDUPTA plaintiff, therefore, need only allege facts

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sufficient to show that it was actually aggrieved by the unfair and deceptive conduct. A court, in determining whether the alleged conduct violates FDUTPA, shall also take into consideration whether the Federal Trade Commission and other federal courts deem such conduct to be an unfair method of competition or an unconscionable, unfair or deceptive act or practice under federal law. Because the legislature does not define what is an unfair or deceptive act, a practice which offends established public policy or is immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers may violate FDUTPA.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

#### **HN24[] Trade Practices & Unfair Competition, State Regulation**

It is well-established that the Florida Deceptive and Unfair Trade Practices Act, Fla. Stat. § 501 et seq., does not apply to any acts or practices that are required or specifically permitted by federal or state law. However, an act does not need to violate a specific rule or regulation in order to be considered deceptive. Therefore, the relevant analysis is whether the moving party for dismissal, has demonstrated that a specific federal or state law affirmatively authorized it to engage in the conduct alleged in the complaints, not whether plaintiffs have demonstrated that the defendant's conduct violates a specific rule or regulation.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

#### **HN25[] Trade Practices & Unfair Competition, State Regulation**

Florida Deceptive and Unfair Trade Practices Act, Fla. Stat. § 501 et seq., has been enacted to provide remedies for conduct outside the reach of traditional common law torts such as fraud, and therefore, a plaintiff need not prove the elements of fraud to sustain an action under the statute.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Claims

#### **HN26[] State Regulation, Claims**

Section 17200 of the California Unfair Competition Law provides a remedy for any injuries resulting from unfair competition, defined as any unlawful, unfair or fraudulent business act or practice. Cal. Bus. & Prof. Code § 17200.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > General Overview

Governments > Legislation > Statutory Remedies & Rights

#### **HN27[] Trade Practices & Unfair Competition, State Regulation**

There is no constitutional impediment in permitting non-Californians a right of action under a domestic statute because California has a clear and substantial interest in preventing fraudulent practices in the state, or in extending state-created remedies to out-of-state parties harmed by wrongful conduct occurring in California.

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Claims

Antitrust & Trade Law > ... > Racketeer Influenced & Corrupt Organizations > Claims > General Overview

## **HN28** [ ] State Regulation, Claims

A California district court has defined "unlawful acts" under the California Unfair Competition Law (UCL), [Cal. Bus. & Prof. Code § 17200](#), as business practices that constitute violations of civil or criminal, federal or regulatory law. Thus, a claimant may "borrow" a violation of another law that is committed in the course of business activity to support a claim under [§ 17200](#). An adequately pled Racketeer Influenced and Corrupt Organizations Act violation is sufficient to support a claim under the unlawful prong of California's UCL.

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**Judges:** PATRICIA A. SEITZ, UNITED STATES DISTRICT JUDGE.

**Opinion by:** PATRICIA A. SEITZ

## **Opinion**

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**[\*1292] ORDER ON DEFENDANT TENET HEALTHCARE CORPORATION'S MOTIONS TO DISMISS**

THIS MATTER is before the Court upon Defendant Tenet Healthcare Corporation's Motions to Dismiss filed in Case No. 05-20591-CIV-SEITZ [DE-29] and Case No. 05-80183-CIV-SEITZ [DE-30]. The Plaintiffs in these two cases-- Boca Raton Community Hospital ("Boca"), thirteen public hospitals in Florida ("the Hospital Plaintiffs"), <sup>1</sup> and the Florida Attorney General ("Florida AG") -- allege that Tenet purposefully inflated the amount that it charged [\*\*\*4] for hospital services in order to increase Medicare reimbursements that its hospitals received. Specifically, the Plaintiffs <sup>2</sup> contend that Tenet engaged in "turbocharging" to obtain excessive outlier payments on cases that qualified for additional reimbursements under the Medicare program pursuant to a complex formula prescribed by the Secretary of the U.S. Department of Health and Human Services ("HHS").

[\*\*5] Defendant Tenet moves to dismiss the Complaints on the grounds that: (1) Medicare [\*1293] preempts the Plaintiffs' state law claims and supercedes their federal RICO claims; (2) Plaintiffs failed to exhaust Medicare's administrative remedies; (3) Plaintiffs lack standing to assert their RICO claims because Tenet's alleged conduct did not proximately cause Plaintiffs' alleged injuries; (4) Plaintiffs have failed to allege facts which, if proven, would constitute a predicate act under RICO; (5) Plaintiffs have failed to adequately allege an enterprise or a conspiracy under RICO; (6) the Florida Deceptive and Unfair Trade Practices Act ("FDUTPA") claim must fail because Tenet's alleged conduct was authorized by then-applicable Medicare regulations and the Florida AG has failed to plead this claim with particularity; (7) substantive limits on the scope of state regulatory jurisdiction bar Boca's claim under California's Unfair Competition Law ("UCL"); and (8) the unjust enrichment count fails to state a claim because the Plaintiffs cannot demonstrate that anything was taken from them.

The Court has considered the Motions, the responses and replies thereto, the *amicus* brief of the United [\*\*\*6] States of America, the applicable case law, and the oral argument of counsel at the June 20, 2005, hearing. Having considered the allegations of the Complaints -- viewed in the light most favorable to the Plaintiffs -- as well as the Medicare regulatory structure, the Court concludes that: (1) Plaintiffs' claims are not preempted under, or superseded by, Medicare; (2) Plaintiffs are not required to pursue the administrative remedies under the Medicare Act; (3) Plaintiffs properly allege RICO standing; (4) Plaintiffs have adequately alleged predicate acts, a RICO enterprise, and proximate cause; (5) Plaintiffs have alleged sufficient facts supporting a RICO conspiracy; (6) the FDUTPA and UCL claims are properly pled and are not subject to dismissal at this stage; and (7) the unjust enrichment claim must be dismissed with prejudice. Accordingly, Tenet's Motions to Dismiss are granted in part, denied in part.

**1. FACTUAL BACKGROUND**

This action involves the operation of the Medicare outlier trust fund or pool for inpatient hospital services. [HN1↑](#) Medicare, established in Title XVIII of the Social Security Act ("SSA"), [42 U.S.C. § 1395, et seq.](#), is the [\*\*\*7] federal program that provides health care insurance to the nation's aged and disabled. Compl. of Boca Raton Community Hosp. ("Boca Compl.") P 22; Am. Compl. of State of Fla., Office of Att'y Gen., et al. ("Pub. Hosp. Compl.") P I. Medicare is administered by the Centers for Medicare & Medicaid Services ("CMS"), a non-independent agency within HHS, and has over 40 million beneficiaries. *Id.*

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<sup>1</sup> The thirteen Hospital Plaintiffs in Case No. 05-20591 are: Bert Fish Medical Center, Inc.; Cape Memorial Hospital, Inc.; Halifax Hospital Medical Center; Hendry County Hospital Authority; Holmes County Hospital Corporation; Jackson County Hospital District; Lee Memorial Health System; North Brevard County Hospital District; North Broward Hospital District; Public Health Trust of Miami-Dade County, Florida, Sarasota County Public Hospital District; South Broward Hospital District; and West Orange Healthcare District.

<sup>2</sup> The term "Plaintiffs" will be used throughout this Order to refer to all three Plaintiff groups -- Boca, the Hospital Plaintiffs, and the Florida AG -- collectively.

Because this case addresses the operation of the Medicare outlier trust fund for inpatient hospital services, it is necessary to situate the allegations in the Complaints within the pertinent regulatory and statutory framework governing Medicare reimbursements.

**A. Medicare Regulatory Background and the Outlier Pool** Medicare and its implementing regulations establish an Inpatient Prospective Payment System ("IPPS") under which hospitals are reimbursed for inpatient services provided to Medicare beneficiaries at prospectively fixed rates. Boca Compl. PP 36-37; Pub. Hosp. Compl. PP 26-27. Under IPPS, each patient's condition is classified into one of over 520 Diagnosis-Related Groups ("DRG"), to which CMS has assigned a numeric weight reflecting the amount of resources needed, on average, [\*\*8] to treat a patient with the corresponding diagnosis. *Id.* Greatly simplified, a hospital's payment for treating a specific [\*1294] patient is determined by multiplying the numeric weight for that DRG by a standardized amount. *Id.* The standardized amount is based on the average resources used to treat cases in all DRGs, and is adjusted to take into account regional wage rates as well as other factors. *Id.* Hospitals submit their claims for reimbursement to "fiscal intermediaries," usually private insurance companies, to which the Secretary of HHS delegates the day-to-day administration of the Medicare program. See [42 U.S.C. § 1395h](#).

#### 1. The Outlier System

Although IPPS assumes that fixed payments based on cases of average complexity will provide adequate compensation to efficiently run hospitals, Congress recognized that an extremely costly case could undermine any averaging. Boca Compl. P 43; Pub. Hosp. Compl. P 28. Therefore, in addition to fixed IPPS rates, the Medicare statute also requires that hospitals be reimbursed for atypical medical cases known as "outliers." *Id.* Outlier payments are designed to supplement standard IPPS payments "for [\*\*9] extraordinarily high-cost cases."<sup>3</sup> *Id.*; see [42 C.F.R. § 412.84](#). Under IPPS, a hospital may receive outlier payments when the cost it incurs to treat a patient exceeds the normal IPPS payment by a fixed deductible, the exact magnitude of which is established by a computer program on an annual basis (*i.e.*, the "Outlier Threshold"). Boca Compl. P 44; Pub. Hosp. Compl. P 29. The higher the Outlier Threshold, the fewer the number of cases that qualify as outliers and, for those that qualify, the lower the outlier payments. Boca Compl. P 44; Pub. Hosp. Compl. P 30.

[\*\*10] The statute empowers the Secretary to promulgate regulations establishing when outlier payments are appropriate. See [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(iii\)](#) ("The amount of such additional payment under clauses (i) and (ii) shall be determined by the Secretary and shall . . . approximate the marginal cost of care beyond the cutoff point applicable under clause (i) or (ii)."). The statute also authorizes hospitals to submit claims for outlier payments that satisfy the criteria set forth in the Secretary's outlier regulations. See [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(ii\)](#). Exercising this statutory authority, the Secretary decided to tie the outlier payment system to hospital charges -- not actual costs. Under the Secretary's formula, although a case qualifies as an outlier if its costs exceed a certain threshold, *i.e.*, "a fixed dollar amount determined by the Secretary," for all cases before October 1, 2003, the hospital's costs were determined based on the hospital's billed charges, adjusted by the hospital's cost-to-charge ratio ("CCR"). [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(II\); 42 C.F.R. § 412.84\(h\)](#) [\*\*11].

Congress constrained the Secretary's discretion in reimbursing outlier cases by setting a five to six percent target for the total amount of outlier payments made each fiscal year in the aggregate to all hospitals, as compared to total aggregate IPPS reimbursements to all hospitals. [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(iv\)](#). For the years at issue in this case, from 1999-2003, the Secretary established a target of 5.1 %. See 68 Fed. Reg. at 34501. In 2003, the Secretary amended the rules regarding outlier reimbursements, and determined [\*1295] that outlier payments are subject to reconciliation on a case-by-case basis when the cost report relevant to each case is settled. See [42 C.F.R. § 412.84\(i\)\(3\); 68 Fed. Reg. at 34501](#). The amended rule thus implements a formula designed to "ensure

<sup>3</sup> Specifically, [HN2](#) [↑] the outlier provision permits hospitals to "request additional payments in any case where charges, adjusted to cost," exceed an amount that the Secretary of HHS specifies. *Id.*; [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(ii\)](#). According to CMS, "this additional payment is designed to protect the hospital from large financial losses due to unusually expensive cases." *Id.*, [68 Fed. Reg. 10420, 10421 \(Mar. 5, 2004\)](#). The outlier payment is meant to "approximate the marginal cost of care." *Id.*; [42 U.S.C. § 1395ww\(d\)\(5\)\(A\)\(iii\)](#).

that when final outlier payments are made, they . . . reflect an accurate assessment of the actual costs the hospital incurred." *Id.* The amended rule did not, however, "make retroactive adjustments to outlier payments to ensure total payments [to all hospitals] are 5.1 percent of [all inpatient spending]," [68 Fed. Reg. at 34502](#), [\\*\\*12](#) nor did it restrict a hospital's right to set its own charges or to submit outlier claims for cases that purportedly meet the prescribed criteria.

## 2. The Cost-to-Charge Ratio

Each hospital, including the Tenet hospitals, uses what is called a "charge master" that lists charges for each item or service that the hospital provides. Boca Compl. P 45; Pub. Hosp. Compl. P 31. While the outlier system is based on the costs that a hospital incurs to treat a specific Medicare patient, the charges (as reflected on the "charge master") act as a surrogate for a hospital's costs if there is a rational relationship between the hospital's charges and its underlying costs. Boca Compl. P 47; Pub. Hosp. Compl. P 32. To that end, each hospital has a CCR, which is an average that can be used to transform a charge into a cost.<sup>4</sup> [\\*\\*13](#) *Id.* Outlier payments equal 80% of the difference between the hospital's costs for treating a patient (calculated by adjusting its charges by its CCR), less the sum of the IPPS payment and the Outlier Threshold.<sup>5</sup> Boca Compl. P 48; Pub. Hosp. Compl. P 33.

The outlier system assumes, and CMS issuances require, that a hospital's charges be reasonably and consistently related to its costs of providing the services. *Id.* (citing Prov. Reimb. Man., Part 1, §§ 2202-2203; [42 C.F.R. § 413.53\(b\)\(2\)\(ii\)](#)). As CMS indicated in September 1988, "the use of hospital-specific cost-to-charge ratios is essential to ensure that outlier payments are made only for cases that have extraordinarily high costs, and not merely high charges." Boca Compl. P 49; Pub. Hosp. Compl. P 34; [68 Fed. Reg. at 10423](#) (Mar. 5, 2003) (citing [53 Fed. Reg. 38476, 38503](#) (Sept. 30, 1988)).

## **B. Tenet's Alleged "Turbocharging"**

Tenet is the nation's second-largest for-profit hospital chain. Boca Compl. P 5; Pub. Hosp. Compl. P 24. At all relevant times, Tenet owned or operated approximately 100 hospitals in 13 states, including 15 in Florida. *Id.* [\\*\\*14](#) Beginning in 1999 and continuing into 2003, Plaintiffs allege, Tenet engaged in a scheme to improperly maximize its outlier payments by artificially inflating its charges. Boca Compl. PP 50, 75; Pub. Hosp. Compl. PP 35, 52. By so doing, the Tenet Hospitals transformed ordinary or average-cost IPPS patients into outlier patients, even though the costs that the hospital actually incurred in treating the patients fell within the norm and would not qualify for outlier funds. Boca Compl. P 51; Pub. Hosp. Compl. P 36. By dramatically increasing their billed charges, the Tenet Hospitals represented to CMS that their costs had similarly increased. *Id.* Thus, when the Tenet Hospitals artificially inflated their charges, their "costs" -- computed by using CCRs that predated the charge increases -- [\[\\*1296\]](#) rose dramatically despite the fact that their real costs remained the same or even declined. Boca Compl. P 52; Pub. Hosp. Compl. P 37.

While the audited CCR should have eventually caught up with the hospitals, that was not the case. Instead, many of the Tenet Hospitals dramatically increased their charges over time to the extent that their CCRs fell precipitously below the range that was considered [\\*\\*15](#) reasonable under Medicare regulations (*i.e.* three standard deviations from the mean of the log distribution of CCRs for all hospitals) by the next settled cost report. Boca Compl. P 54; Pub. Hosp. Compl. P 39. The fiscal intermediary then assigned a Statewide Average ("SWA") CCR to these hospitals instead of the hospital-specific CCR figure. *Id.* The SWA was considerably higher than the hospital's actual CCR.<sup>6</sup> Boca Compl. P 54; Pub. Hosp. Compl. P 40. Therefore, when the fiscal intermediary applied the

<sup>4</sup> For example, if a hospital's CCR is 0.5 and its charges for a patient total \$ 10,000, then its costs to treat that patient would be roughly \$ 5,000. *Id.*

<sup>5</sup> The calculation is represented by the following equation: Outlier payment = 80% x [(charges x CCR) -- IPPS Payment -- Outlier Threshold]. Boca Compl. P 33; Pub. Hosp. Compl. P 48.

higher SWA to compute an individual hospital's outlier payment, it generated excessive outlier payments to Tenet. Boca Compl. P 54; Pub. Hosp. Compl. P 40.

On average, between June 1, 2000, and December 31, 2002, Tenet received outlier payments of over \$ 35 million [\*\*16] per month, for a total of \$ 1.1 billion in a period of only 31 months. *Id.* In contrast, if Tenet's outlier payments had been 5.1% of its IPPS payments, Tenet would have received roughly \$ 6 million per month during the same time period. *Id.* Thus, Plaintiffs allege, Tenet's inflation of its charges resulted in Tenet receiving an additional \$ 29 million per month of outlier payments. More than a third of Tenet's hospitals had dramatic increases in their outlier payments since 2000, with three in particular -- Doctors Medical Center (in California), Garfield Medical Center (in California), and Brownsville Medical Center (in Texas) -- holding positions in the top 10 of the 200 hospitals nationwide with the greatest increases in outlier payments since 2000. Boca Compl. P 76; Pub. Hosp. Compl. P 56.

### C. The Complaints

The Plaintiffs commenced their respective actions on March 2, 2005. In their First Amended Complaint, filed in Case No. 05-20591-CIV-SEITZ, the Florida AG and the Hospital Plaintiffs assert claims for RICO violations through transporting and receiving stolen or converted money, [18 U.S.C. § 1962\(c\)](#) (Count I); conspiracy to violate [18 U.S.C. § 1962](#) [\*\*17] [\(c\)](#) through transporting and receiving stolen or converted money, in violation of [18 U.S.C. § 1962\(d\)](#) (Count II); violation of Florida's civil RICO statute, [Fla. Stat. §§ 772.103\(3\)](#) and [772.104](#) (Count III); conspiracy to violate [Fla. Stat. § 772.103\(4\)](#) (Count IV); violation of the Florida Deceptive and Unfair Trade Practices Act (Count V); and unjust enrichment (Count VI). Boca's Complaint in Case No. 05-80183-CIV-SEITZ alleges claims of RICO violations under [18 U.S.C. § 1962\(c\)](#) (Count I); conspiracy to violate [18 U.S.C. § 1962\(c\)](#) (Count II); violation of California's Unfair Competition Law (Count V); and unjust enrichment (Count VII).<sup>7</sup>

## II. STANDARD OF REVIEW

**HN3**[] [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) provides that dismissal [\*\*18] of a claim is appropriate [\*1297] when "it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations." [Blackston v. Alabama](#), 30 F.3d 117, 120 (11th Cir. 1994). At this stage of the proceedings, the Court must accept the Plaintiff's allegations in the Complaints as true, and view those allegations in a favorable light to determine whether the Complaints state claims for which relief can be granted. [S & Davis Int'l, Inc. v. Republic of Yemen](#), 218 F.3d 1292, 1298 (11th Cir. 2000). Thus, a court may dismiss a complaint for failure to state a claim only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations. See [Hishon v. King & Spalding](#), 467 U.S. 69, 73, 104 S. Ct. 2229, 81 L. Ed. 2d 59 (1984).

However, **HN4**[] "to survive a motion to dismiss, plaintiffs must do more than merely state legal conclusions; they are required to allege some specific factual bases for those conclusions or face dismissal of their claims." [Jackson v. BellSouth Telecomm.](#), 372 F.3d 1250, 1263 (11th Cir. 2004). Indeed, "conclusory allegations, unwarranted factual deductions [\*\*19] or legal conclusions masquerading as facts will not prevent dismissal [for failure to state a claim]." [Davila v. Delta Air Lines](#), 326 F.3d 1183, 1185 (11th Cir. 2003). Therefore, in considering Tenet's Motions to Dismiss, the Court is "not bound by the legal conclusions in the complaint," and must look instead at the pleaded facts to determine whether the Plaintiffs' claims can proceed through discovery. [Day v. Taylor](#), 400 F.3d 1272, 1275 (11th Cir. 2005).

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<sup>6</sup> CMS assigns the SWA to a hospital when its CCR falls below the national threshold because CMS presumes that a CCR below this level is unreasonable and probably due to a faulty data reporting or entry. Boca Compl. P 55; Pub. Hosp. Compl. P 39.

<sup>7</sup> Boca voluntarily dismissed its fraud-based causes of action, set forth in Counts III, IV, and VI of its Complaint.

### III. DISCUSSION

#### A. Federal Preemption Does Not Bar These Actions

In its Motions to Dismiss, Tenet first argues that the Plaintiffs' Complaints must be dismissed in their entirety because the state law claims are preempted, and the federal RICO claims superceded, by the comprehensive regulatory scheme that Congress adopted through the Medicare program. More specifically, Tenet contends that Plaintiffs may not bring state law claims for what amounts to alleged overpayments to Tenet because the Medicare scheme sets forth both (1) the substantive rules for determining the amount of Medicare reimbursement due to Tenet; and (2) the administrative process by which that amount is finally [\*\*20] determined. See Def.'s Mem. at 11. Likewise, Tenet argues that the federal RICO claims are superceded by the "comprehensive and reticulated" Medicare scheme. *Id.* at 11-12.

**HN5** [↑] "Medicare is a vast and complicated federal program." *Stephenson v. Shalala*, 87 F.3d 350, 351 (9th Cir. 1996). In Medicare, Congress has enacted a comprehensive statutory regime and "conferred on the [HHS] Secretary exceptionally broad authority to prescribe standards for carrying out certain sections of the Act." *Id. at 356* (quoting *Schweiker v. Gray Panthers*, 453 U.S. 34, 43, 101 S. Ct. 2633, 69 L. Ed. 2d 460 (1981)). Regulatory schemes can displace state law causes of action just as completely as statutes can. See *Fidelity Fed. Sav. & Loan Ass'n v. de la Cuesta*, 458 U.S. 141, 153, 102 S. Ct. 3014, 73 L. Ed. 2d 664 (1982) ("Federal regulations have no less preemptive effect than federal statutes."); see also *Chrysler Corp. v. Brown*, 441 U.S. 281, 295, 99 S. Ct. 1705, 60 L. Ed. 2d 208 (1979). However, the federal Medicare statute can be found to preempt state law causes of action "if and only if Congress intended it to do so." *Mass. Med. Soc'y v. Dukakis*, 815 F.2d 790, 791 (1st Cir. 1987).

Although Tenet [\*\*21] cites nearly two dozen federal preemption cases to the Court, not one of them involves the Medicare Act. In contrast, the four federal [\*1298] courts of appeals that have addressed the question in the context of the Medicare Act have rejected Tenet's argument, noting, *inter alia*, that Medicare is not a field preempting statute. *Downhour v. Soman*, 85 F.3d 261, 266 (6th Cir. 1996); *Med. Soc'y of N. Y. v. Cuomo*, 976 F.2d 812, 820 (2d Cir. 1992); *Pa. Med. Soc'y v. Marconis*, 942 F.2d 842, 847 (3d Cir. 1991); *Mass. Med. Soc'y*, 815 F.2d at 791.

Only last year, another district court rejected this argument when Tenet itself made it. See *United States v. Tenet Healthcare Corp.*, 343 F. Supp. 2d 922 (C.D. Cal. 2004). In that case, the federal government filed suit against Tenet under various common law theories, including unjust enrichment. The government alleged that 26 Tenet hospitals had submitted more than 2,400 Medicare claims that were upcoded and that, as a result, CMS paid Tenet more than it was entitled to receive. In denying Tenet's motion to dismiss based on preemption, the Court held that:

Here, [\*\*22] although the government's claim implicates reimbursement determinations, it is not the type of claim that falls within the scope of § 405(h) [of the Medicare Act]. Since the Court is not faced with a claim for reimbursement from a dissatisfied provider that should be channeled through the administrative process, this case does not "arise under" the Medicare Act. Rather, because the government's action is predicated on the submission of inaccurate and misleading claims, the common law, not the Medicare Act, provides both standing and the substantive basis for the claim.

*Tenet*, 343 F. Supp. 2d at 928. Upon review of the case law, there is no indication that Congress intended to preempt state law causes of action through the implementation of the Medicare Act. Further, while the Plaintiffs' claims may address reimbursement determinations, at least peripherally, they are not claims that arise under the Medicare Act. Accordingly, Tenet's motions to dismiss on this basis are denied.

#### B. Exhaustion of Medicare Remedies

As a parallel argument to their preemption claim, Tenet argues that the Complaints must be dismissed because Plaintiffs failed to allege [\*\*23] that they invoked the Medicare regulatory process that Congress established. Tenet correctly argues that the Medicare statute specifically provides a mechanism for the Plaintiffs to seek review of reimbursement determinations, first through an administrative process and ultimately in the courts. See [42 U.S.C. § 1395oo](#); [Regions Hosp. v. Shalala, 522 U.S. 448, 452-53, 118 S. Ct. 909, 139 L. Ed. 2d 895 \(1998\)](#). However, while Tenet contends that the Plaintiffs' claims set forth in the Complaints are "nothing more than a dressed up complaint about the reimbursements Plaintiffs received from CMS," the characterization of these RICO-based actions as ones for such types of reimbursements is inappropriate. Further, the Eleventh Circuit has clarified that actions against a party other than the HHS Secretary or the federal government are not subject to the exhaustion requirements of the SSA. See [United States ex rel. Body v. Blue Cross/Blue Shield of Ala., 156 F.3d 1098, 1104 \(11th Cir. 1998\)](#) ("actions such as Body's, which do not seek payment from the government and could not be brought under [42 U.S.C.] section 405, are therefore not barred by subsection 405(h). [\*\*24] "). Because the Plaintiffs do not seek payment from the Government, but instead seek recovery from Tenet for damages resulting from the alleged "turbocharging" scheme, Tenet's argument with respect to exhaustion of administrative remedies is not persuasive.

### [\*1299] C. Plaintiffs Have Properly Alleged RICO Standing

Tenet also asserts that the Plaintiffs lack standing to make their RICO and Florida RICO claims<sup>8</sup> because Tenet's alleged conduct did not proximately cause Plaintiffs' alleged injury. According to Tenet, the Plaintiffs' alleged harm is far too remote from Tenet's conduct because the independent actions of CMS, its fiscal intermediaries, and other hospitals stand in the middle of the causal chain. See Def.'s Mem. at 16-17. Specifically, Tenet asserts that Plaintiffs' causation theory fails because: (1) Tenet hospitals make up only a fraction of the hospitals with low CCRs receiving payments for outliers, and thus, the practices of hospitals other than Tenet's led the Secretary to raise the Outlier Threshold; (2) it is CMS, and not Tenet, that assigns the SWA to a hospital when its CCR falls below the national threshold; and (3) the Secretary, in exercising his sole discretion, [\*\*25] elected to raise the Outlier Threshold instead of raising the outlier percentage target. *Id.* at 18. Tenet therefore contends that, even assuming *arguendo* that its alleged actions were wrongful, it did not, as a matter of law, cause the Plaintiffs any direct injury.<sup>9</sup> *Id.* at 19.

[\*\*26] In response, the Plaintiffs maintain that their Complaints properly allege "some direct relation between the injury asserted and the injurious conduct alleged," as required under [Holmes v. Sec. Investor Prof. Corp., 503 U.S. 258, 267, 112 S. Ct. 1311, 117 L. Ed. 2d 532 \(1992\)](#). Plaintiffs rely significantly on excerpts from the March 11, 2003, testimony of CMS Administrator Thomas A. Scully, before the Senate Appropriations Subcommittee on Labor, Health and Human Services, and Education. In relevant part, Administrator Scully testified that:

As a direct result [of the excessive outlier payments,] more hospitals have been forced to absorb the costs of the complex cases they treat, while a relatively small number of hospitals that have been aggressively gaming

<sup>8</sup>The Florida RICO law was patterned after its federal counterpart. See [Jackson, 372 F.3d at 1263-64](#) (quoting [Jones v. Childers, 18 F.3d 899, 901 \(11th Cir. 1994\)](#) (noting that "interpretation of Florida's RICO law is informed by case law interpreting the federal RICO statute . . . on which Chapter 772 is patterned.")). The Court therefore applies the same analysis to Plaintiff's federal and state RICO claims. *Id.*; see also [All Care Nursing Serv., Inc. v. High Tech Staffing Servs., Inc., 135 F.3d 740, 745 \(11th Cir. 1998\)](#) ("Florida's RICO statutes have consistently been interpreted using federal RICO claim cases.").

<sup>9</sup>Tenet bases its standing argument on the following characterization of Plaintiffs' alleged causal chain:

Increasing gross charges gave some Tenet hospitals low CCRs; CMS's fiscal intermediary assigned all hospitals with low CCRs (including some Tenet hospitals) the SWA; using the SWA gave some hospitals (including some Tenet hospitals) higher outlier payments from CMS; higher outlier payments by CMS to these hospitals (only some of which were Tenet hospitals) increased the volume of outlier payments made nationwide; CMS increased the outlier threshold in order to decrease outlier payments nationwide; and this increase by CMS in the outlier threshold potentially deprived plaintiffs of a fraction of outlier payments they might have qualified for had CMS not raised the outlier threshold.

the current rules benefit by getting a hugely disproportionate share of outlier payments. As you can see, the behavior of a few hundred hospitals -- those that took advantage of the outlier program -- [is] the main cause of the sharp increases in the loss threshold.

Boca Compl. at P 73, Ex. C; Pub. Hosp. Compl. at P 51. Further, Plaintiffs respond to Tenet's reliance on the independent actions of CMS, its fiscal intermediaries, [\[\\*\\*27\]](#) [\[\\*1300\]](#) and other hospitals by arguing that: (1) the causal connection is far simpler and less tenuous than Tenet alleges; (2) the mere presence of third parties, such as CMS or other hospitals, does not preclude the Plaintiffs' RICO claims; (3) Tenet cannot evade liability merely because some other hospitals may have engaged in the same form of misconduct; and (4) even if other intermediaries contributed to the alleged injury, expert witnesses will be able to ascertain with reasonable certainty Tenet's direct contribution to the damage, as well as guide the Court in apportioning recoveries to the Hospital Plaintiffs. See Pls.' Mem. at 22-26.

## 1. Test for RICO Standing

[HN6](#)  "The test for RICO standing is whether the alleged injury was directly caused by the RICO violation. . . ." *Bivens Gardens Office Bldg., Inc. v. Barnett Banks of Fla., Inc.*, 140 F.3d 898, 908 (11th Cir. 1998) (citing [Holmes, 503 U.S. at 268](#)); see also [Sedima S.P.R.L. v. Imrex Co.](#), 473 U.S. 479, 496, 105 S. Ct. 3275, 87 L. Ed. 2d 346 (1985) (holding that "a plaintiff only has standing if, and can only recover to the extent that, he has been injured in his business or property by the conduct constituting [\[\\*\\*28\]](#) the violation" of RICO). Further, a RICO plaintiff must demonstrate that its damages "flow from the commission of the predicate acts." [Williams v. Mohawk Indus., Inc.](#), 411 F.3d 1252, 1263 (11th Cir. 2005) (citing [Sedima, 473 U.S. at 497](#)); see also [Pelletier v. Zweifel](#), 921 F.2d 1465, 1497 (11th Cir. 1991). "[A] plaintiff who complains of harm flowing merely from the misfortunes visited upon a third person by the defendant's acts [is] generally said to stand at too remote a distance to recover." [Green Leaf Nursery v. E.I. DuPont De Nemours](#), 341 F.3d 1292, 1307 (11th Cir. 2003) (citing [Holmes, 503 U.S. at 268-69](#)). Therefore, the question before the Court is whether the Plaintiffs' alleged injury to their business or property is sufficiently direct to bestow standing to sue for Tenet's alleged RICO violations.

## 2. Analysis

According to the Plaintiffs, the injury that they suffered is a direct, proximate, and foreseeable result of the conduct of Tenet and its hospital co-conspirators. Plaintiffs specifically allege that when Tenet, through its alleged RICO enterprise, committed predicate acts [\[\\*\\*29\]](#) of theft and conversion to take hundreds of millions of dollars more a year from the outlier pool than it was entitled to receive, CMS's computer program automatically increased the Outlier Threshold (*i.e.* the deductible applied to the Plaintiffs) in the subsequent year to take into account the large payout to Tenet the previous year. Pls.' Mem. at 23; see Boca Compl. at P 65; Pub. Hosp. Compl. at P 44. As a result of the increasing Outlier Threshold, the other hospitals members of the outlier pool (including the Hospital Plaintiffs) received less than that to which they otherwise would have been entitled. Tenet, in the subsequent year, again raised its charges to keep pace with the increase in the Outlier Threshold. These actions, Plaintiffs contend, drove the Outlier Threshold even higher in the next year, and further reduced the amount of outlier payments to the other participating hospitals. *Id.* It is this continuing cycle that the Plaintiffs allege caused them direct injury, as Tenet's alleged intentional inflation of its outlier claims directly reduced the outlier payments to the other participating hospitals.

Upon review of the Plaintiffs' allegations, the Court [\[\\*\\*30\]](#) finds that, for purposes of the Motions to Dismiss, the Plaintiffs have alleged sufficient facts supporting the requisite direct injury. The Hospital Plaintiffs have set forth extensive allegations describing how Tenet's practice of "turbocharging" [\[\\*1301\]](#) has injured their business or property by driving up the Outlier Threshold and reducing the reimbursements that they were entitled to receive from the outlier pool. These allegations appear to be supported by the statements of Administrator Scully.

Although Tenet contends that the involvement of third parties -- such as CMS and other hospitals that contribute to the outlier pool -- as potential players in the causal chain that led to the Plaintiffs' injuries precludes a finding of RICO standing, the Court must disagree. First, as to the involvement of CMS, the mere fact that the government

may be able to pursue relief against Tenet does not preclude a separate action by the Plaintiffs.<sup>10</sup> See *Rodriguez v. McKinney*, 878 F. Supp. 744, 749 (E.D. Pa. 1995) ("Nor is the causal nexus destroyed here merely because DOE [the Department of Education] occupied a spatially intermediate position between defendant and plaintiffs in [\*\*31] the flow of the alleged fraud") (citing *Prudential Ins. Co. of Am. v. U.S. Gypsum Co.*, 828 F. Supp. 287, 297 (D.N.J. 1993)). Indeed, [HN7](#) "if the existence of a public authority that could prosecute a claim against putative RICO defendants meant that the plaintiff is too remote under *Holmes*, then no private cause of action could ever be maintained, for every RICO predicate offense, as well as the RICO enterprise itself, is separately prosecutable by the government." *Commer. Cleaning Servs., L.L.C. v. Colin Serv. Sys., Inc.*, 271 F.3d 374, 385 (2d Cir. 2001).

[\*\*32] Second, Tenet's contention that the Plaintiffs lack standing because the practices of other non-Tenet hospitals also contributed to the Secretary's decision to raise the Outlier Threshold also fails. Tenet essentially asks the Court to relieve it of liability because other hospitals may have engaged in the same form of alleged misconduct. However, even if other wrongdoing contributed to the alleged injury, that may not relieve Tenet of responsibility for its own alleged conduct. As this case proceeds through discovery, and if evidence exists to support a finding that Tenet inflated its outlier charges and caused injury to the Plaintiffs, the parties can seek expert testimony to apportion each player's direct contribution to the damage and to ascertain the amount of the injury that each Hospital Plaintiff suffered.

Finally, the mere fact that the Secretary, in exercising his sole discretion, elected to raise the Outlier Threshold instead of raising the outlier percentage target does not preclude a finding of RICO standing. Tenet argues, in essence, that its conduct was too remote because CMS has the discretion to modify the amount contributed to the outlier pool from 5.1% to 6.0%, [\*\*33] and that had CMS done that, the Hospital Plaintiffs would not have been injured. Tenet's point here is that it was CMS's intervening decisions -- and not Tenet's alleged "turbocharging" -- that led to Plaintiffs' alleged injuries. But as Plaintiffs point out, this argument fails because "what CMS might have done is irrelevant since that is not what the Complaints allege that CMS, in fact, did." Pls.' Mem. at 25. Further, the factual allegations in the Complaints indicate that even had the Secretary raised the contribution to 6.0% in response to Tenet's misconduct, rather than raising the Outlier Threshold, the Hospital Plaintiffs still could have been damaged through their need to make higher contributions via withholdings to subsidize [\*1302] Tenet's alleged artificially inflated billings (*i.e.*, the hospitals would have been required to make the additional 0.9% contribution).

While it does appear that, for pleading purposes, Plaintiffs have sufficiently alleged a direct injury to meet the requirements of RICO standing, the degree to which other intervening acts contributed to the alleged injury must be explored more fully during discovery and may ultimately form the basis for a subsequent [\*\*34] motion for summary judgment. However, given this stage of the litigation, the Court finds that Plaintiffs have sufficiently alleged that Tenet's unlawful conduct had a direct impact on them. *Williams*, 411 F.3d at 1264. Consequently, Plaintiffs have standing to maintain their RICO claims against Tenet.

#### D. Plaintiffs Have Stated a Claim Under RICO

[HN8](#) Pursuant to [18 U.S.C. § 1962\(c\)](#), it is illegal "for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity. . . ." [18 U.S.C. § 1962\(c\)](#). Thus, in order to establish a federal civil RICO violation under [§ 1962\(c\)](#), the plaintiffs must satisfy four elements of proof: "(1) conduct; (2) of an enterprise; (3) through a pattern; (4) of racketeering activity." *Williams*, 411 F.3d at 1256 (citing *Jones v. Childers*, 18 F.3d 899, 910 (11th Cir. 1994)). In civil cases, however, RICO plaintiffs must also satisfy the requirements of [18 U.S.C. § 1964](#) [\*\*35] (c), which states that "any person injured in his

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<sup>10</sup> As Plaintiffs' counsel identified at the oral argument, the damages that the Government may choose to seek from Tenet are different than those that Plaintiffs claim in these actions. Indeed, "the government would be seeking to recover its shortfall and [the Plaintiffs] would be seeking to recover damages as a result of the increased threshold; the increased deductible." See Tr. of June 20, 2005, Oral Argument ("Tr."), DE-62 at 26.

business or property by reason of? RICO's substantive provisions has the right to "recover threefold the damages he sustains. . . ." [18 U.S.C. § 1964\(c\)](#). Thus, under [§ 1964\(c\)](#), RICO claimants must show (1) the requisite injury to business or property; and (2) that such injury was "by reason of? the substantive RICO violation. [Williams, 411 F.3d at 1256.](#)

Tenet challenges Plaintiffs' RICO claims on three grounds. First, Tenet argues that Plaintiffs have not alleged facts sufficient to support a finding that their conduct constituted a predicate act under RICO. Second, Tenet maintains that Plaintiffs failed to properly plead a RICO enterprise. And third, Tenet contends that the allegations do not demonstrate that its alleged racketeering activity caused the Hospital Plaintiffs' injuries. The Court now addresses each of these issues in turn.

### 1. Predicate Act

[HN9](#) For purposes of the RICO Act, a "pattern of racketeering activity" requires at least two acts of racketeering activity. [Williams, 411 F.3d at 1256-57](#) (quoting [Cox v. Adm'r U.S. Steel & Carnegie, 17 F.3d 1386, 1397 \(11th Cir. 1994\)](#), [\[\\*\\*36\]](#) modified on other grounds, [30 F.3d 1347 \(11th Cir. 1994\)](#)). An act of racketeering is commonly referred to as a predicate act. A pattern of racketeering activity is shown when a racketeer commits at least two distinct but related predicate acts. *Id.* (quoting [Maiz v. Virani, 253 F.3d 641, 671 \(11th Cir. 2001\)](#) (internal quotation marks, citations, and brackets omitted)). "If distinct statutory violations are found, the predicate acts will be considered to be distinct irrespective of the circumstances under which they arose." [Cox, 17 F.3d at 1397](#) (quotation marks, citations, and emphasis omitted).

Plaintiffs assert that Tenet, by its alleged "turbocharging" practice, stole or converted money from the outlier pool. They maintain, therefore, that their Complaints properly allege a pattern of racketeering activity under [sections 2314](#) and [2315](#) of the National Stolen Property Act ("NSPA"). Tenet seeks dismissal of the RICO claims on the grounds that the allegations of theft or conversion fail to constitute [\[\\*1303\]](#) a predicate act because: (1) Tenet obtained the alleged monies with CMS's consent; and (2) Plaintiffs have no colorable claim of right [\[\\*\\*37\]](#) to the allegedly "stolen" funds.

[HN10](#) To state a claim under [§ 2314 of the NSPA, the Hospital Plaintiffs](#) must allege (1) that Tenet transported, transmitted or transferred or caused to be transported, transmitted or transferred in interstate commerce, monies that were stolen or converted; (2) that such monies had a value of \$ 5,000 or more; and (3) that Tenet transported the monies willfully and with knowledge that the monies had been stolen or converted. [18 U.S.C. § 2314](#); 11th Cir. Pattern Crim. Jury Instr. 78.1 (2003). Further, [HN11](#) to allege a [§ 2315](#) violation, the Hospital Plaintiffs must show that: (1) Tenet received, possessed, concealed, stored or disposed of stolen money; (2) that such monies had a value in excess of \$ 5,000; (3) that such monies had crossed a State or United States boundary after having been stolen or unlawfully converted; and (4) that Tenet knew that the property had been stolen or unlawfully converted. [18 U.S.C. § 2315](#); 11th Cir. Pattern Crim. Jury Instr. 79 (2003). As set forth in the Eleventh Circuit Pattern Jury Instructions, "the word 'stolen' includes any wrongful and dishonest taking." 11th Cir. Pattern Crim. [\[\\*\\*38\]](#) Jury Instr. 78.1 (2003); see also [United States v. Turley, 352 U.S. 407, 412, 77 S. Ct. 397, 1 L. Ed. 2d 430 \(1957\)](#) ("stealing" has no accepted common law meaning and includes any "felonious taking with . . . intent to deprive the owner of the rights and benefits of ownership"); [Lyda v. United States, 279 F.2d 461, 464 \(5th Cir. 1960\)](#)<sup>11</sup> (noting that the term "stealing" is "commonly used to denote any dishonest transaction whereby one obtains that which rightfully belongs to another"). Likewise, "the word 'converted' means the unauthorized exercise of control over the property of another inconsistent with the owner's rights." 11th Cir. Pattern Crim. Jury Instr. 78.1 (2003); see also [United States v. Evans, 579 F.2d. 360, 361 \(5th Cir. 1978\)](#) (finding trial court did not err in instructing jury that "converted," as used in [§ 2314](#), meant "to appropriate dishonestly or illegally to one's own use anything of value").

[\[\\*\\*39\]](#) The Complaints allege facts sufficient to satisfy each of the aforementioned required elements. As alleged, Tenet intentionally stole from the Medicare outlier system by grossly inflating its hospitals' charges and engaging in

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<sup>11</sup> In [Bonner v. Prichard, 661 F.2d 1206, 1209 \(11th Cir. 1981\)](#) (en banc), the Eleventh Circuit adopted as binding precedent all decisions of the former Fifth Circuit handed down prior to October 1, 1981.

a "systematic, ongoing course of conduct with the goal and intent to steal and/or convert money from the Outlier Pool." Boca Compl. at PP 49-61, 102; Pub. Hosp. Compl. at PP 34-61. Additionally, the Complaints allege that:

the money (i.e. Outlier overpayments) sought and received by the Tenet Hospitals did not belong to them. At no time did Tenet or the Tenet Hospitals have a legitimate ownership or possessory right, entitlement or interest in that money from the Outlier Pool. Thus, Tenet and the Tenet Hospitals' exercise of control over the money was unauthorized and wrong.<sup>12</sup>

Boca Compl. at P 104; Pub. Hosp. Compl. at P 81. Further, the Complaints allege that Tenet's receipt and exercise of control over payments from the Outlier Pool injured the Hospital Plaintiffs who "were forced to absorb the costs of care for Outlier patients that they would have otherwise been compensated for from the Outlier Pool but for Tenet's improper and illegal acts. <sup>\*\*40</sup>" Boca Compl. at P 108; Pub. Hosp. Compl. at P 85. The Complaints continue <sup>[\*1304]</sup> to allege that Tenet transmitted these "stolen" funds in interstate commerce over several years in amounts that exceeded \$ 5,000.00 for most, if not all, of the thousands of predicate acts it committed. Boca Compl. at PP 104-07, 113-14; Pub. Hosp. Compl. at PP 81-84, 90-91. The necessary elements for proving violations of the NSPA as predicate acts under RICO have, therefore, been pled.

Tenet argues that the RICO claims based on NSPA violations must fail because CMS "consented" to Tenet's alleged scheme. Tenet relies on case law interpreting the terms "stealing" and "converting" as requiring a showing that the taking was without the owner's consent. See Def.'s Mem. at 22-23. As Tenet argues, theft requires a "taking of property without the owner's consent." Black's Law Dictionary 1477 (6th ed. 1991); see also [United States v. Turley, 352 U.S. 407, 413, 77 S. Ct. 397, 1 L. Ed. 2d 430 \(1957\)](#). Likewise, conversion is the "unauthorized and wrongful exercise of the dominion and control over another's personal property." [United States v. McRee, 7 F.3d 976, 985 n.2 \(11th Cir. 1993\)](#) (citing Black's Law Dictionary <sup>\*\*41</sup> 332 (6th ed. 1991)). This argument fails for several reasons. First, there are no allegations in the Complaints that CMS both knew of, and consented to, Tenet's allegedly dishonest scheme. Rather, this argument depends on facts (i.e. that CMS had knowledge and gave consent) outside of the four corners of the Complaints, and must be ignored at this juncture. [Fed. R. Civ. P. 12\(b\)\(6\)](#); see also [Crowell v. Morgan Stanley, 87 F. Supp. 2d 1287, 1290 \(S.D. Fla. 2000\)](#). Second, in [Stewart v. United States, 151 F.2d 386 \(8th Cir. 1945\)](#), the Court rejected a similar argument and held that <sup>HN12</sup> "although there must be a taking against the will of the owner, or a trespass to his possession, the requirement is satisfied where the owner is induced by some fraud or trickery to deliver the property to one who feloniously converts it to his own use. In such circumstances there is an absence of real consent and the taking of possession is wrongful." [Stewart, 151 F.2d at 388](#). Given the allegations that Tenet made submissions to CMS that did not reflect actual costs, in an effort to receive excessive outlier payments <sup>\*\*42</sup> to which they were not entitled (but to which the Plaintiffs were allegedly entitled), the Court cannot find that CMS knowingly consented to the allegedly wrongful takings based on the mere fact that CMS disbursed monies to Tenet.<sup>12</sup>

Finally, Tenet contends that the RICO claims must fail because the Hospital Plaintiffs did not allege that they had a colorable claim of right to the stolen outlier funds. In support, Tenet cites to a case holding that "in order for property to be considered stolen,' the property <sup>\*\*43</sup> must rightly belong to someone other than the person who has it." [United States v. One Lucite Ball Containing Lunar Material, 252 F. Supp. 2d 1367, 1378 \(S.D. Fla. 2003\)](#) (internal quotations omitted). Tenet argues that because the distribution of Medicare reimbursements is "purely a creature of statute and regulation, and Plaintiffs have not demonstrated a specific statutory or regulatory violation, they cannot be held liable for a felonious taking. However, this argument misses the point. <sup>HN13</sup> The legal standard for claims under the NSPA requires that Plaintiffs allege that the monies that Tenet took did not rightfully belong to Tenet. See [Lyda, 279 F.2d at 464](#) <sup>[\*1305]</sup> (stealing "denotes any dishonest transaction whereby one person obtains that which rightfully belongs to another."). The Hospital Plaintiffs have properly alleged that Tenet stole and converted monies that did not rightfully belong to it. Boca Compl. at PP 104-06; Pub. Hosp. Compl. at PP 81-83. While the Plaintiffs will ultimately have to prove their own interest in the outlier funds, at this juncture, viewing the

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<sup>12</sup> In so ruling, the Court is not concluding that allegations exist to support a finding of "fraud or trickery." Indeed, Plaintiffs have dismissed their fraud claims, and have agreed to eliminate references to alleged fraud from the Complaints. However, given the allegations, there is support for a finding that CMS did not "consent" to the alleged scheme because Tenet's excessive outlier reimbursements were based on intentionally inaccurate charge submissions to CMS that did not reasonably reflect costs.

allegations in the light most favorable to the Plaintiffs, there is at least impliedly [\*\*44] (if not explicitly) the allegation that the funds that Plaintiffs seek to recover were funds that would have been theirs. Accordingly, at this stage of the litigation, dismissal of the Complaints for failure to properly allege RICO predicate acts would be inappropriate.

## 2. Enterprise

Next, Tenet asserts that Plaintiffs have failed to properly allege a RICO enterprise. [HN14](#) [↑] "Essential to any successful RICO claim are the basic requirements of establishing a RICO enterprise." [Jackson, 372 F.3d at 1264](#); see also [Cedric Kushner Promotions, Ltd. v. King, 533 U.S. 158, 161, 121 S. Ct. 2087, 150 L. Ed. 2d 198 \(2001\)](#). "Whatever the pleading requirements for other causes of action, plaintiffs in RICO claims must plead specific facts, not mere conclusory allegations, which establish the enterprise." [Manax v. McNamara, 842 F.2d 808, 811 \(5th Cir. 1988\)](#) (internal quotation omitted).

[HN15](#) [↑] A RICO enterprise exists "where a group of persons associates, formally or informally, with the purpose of conducting illegal activity." [United States v. Hewes, 729 F.2d 1302, 1311 \(11th Cir. 1984\)](#); see also [United States v. Turkette, 452 U.S. 576, 583, 101 S. Ct. 2524, 69 L. Ed. 2d 246 \(1981\)](#). [\*\*45] To allege an enterprise under § 1962(c), the Plaintiffs must "name a RICO person distinct from the RICO enterprise." [United States v. Goldin Indus., Inc., 219 F.3d 1268, 1271 \(11th Cir. 2000\)](#) ("Goldin I"); see also [Cedric Kushner Promotions, Ltd. v. King, 533 U.S. 158, 162, 121 S. Ct. 2087, 150 L. Ed. 2d 198 \(2001\)](#) (noting that § 1962(c) "requires some distinctness between the RICO defendant and the enterprise."). The "plain language of § 1962(c) envisions two separate entities." [Id. at 1270](#). Thus, "RICO forbids the imposition of liability where the enterprise is nothing more than a subdivision or part of the person." [United States v. Goldin Indus., Inc., 219 F.3d 1271, 1276 \(11th Cir. 2000\)](#) ("Goldin II"). Where, as here, the Plaintiffs allege that the enterprise is an association-in-fact, the "crucial factor is whether each entity alleged to be part of the association-in-fact is free to act independently and advance its own interests contrary to those' of the other entities." [Lockheed Martin Corp. v. Boeing Co., 357 F. Supp. 2d 1350, 1365 \(M.D. Fla. 2005\)](#) (quoting [Goldin II, 219 F.3d at 1277](#)).

Tenet contends that the [\*\*46] Complaints do not adequately allege a RICO enterprise because Tenet and the hospital co-conspirators "form a single unit" and are not distinct entities. However, Tenet's argument appears to be rooted in an antitrust and intra-corporate conspiracy doctrine<sup>13</sup> that has been rejected in the RICO context. See Def.'s Mem. at 26. In recent [\*1306] years, [HN16](#) [↑] both the Supreme Court and the Eleventh Circuit have held that the existence of a legal distinction between the RICO defendant and the RICO enterprise is sufficient to establish an enterprise under RICO. See [Kushner, 533 U.S. at 165-66](#); see also [Kirwin v. Price Communs. Corp., 391 F.3d 1323, 1327 \(11th Cir. 2004\)](#) (specifically rejecting the intracorporate conspiracy doctrine as a bar to § 1962(d) claims). Therefore, under established and binding precedent, "corporations and their agents are distinct entities" for RICO purposes. [Kirwin, 391 F.3d at 1327](#); see also [Kushner, 533 U.S. 163](#) ("The corporate owner/employee, a natural person, is distinct from the corporation itself, a legally different entity with different rights and responsibilities due to its different legal status. [\*\*47] ").

Here, the Plaintiffs allege that Tenet's RICO enterprise consists of Tenet; a number of hospitals that are wholly-owned, [\*\*48] separately incorporated subsidiaries of Tenet; at least one hospital that is part of a joint venture with Tenet; and hospitals leased by subsidiaries of Tenet; and their officers, directors, managers, employees, agents, representatives, and outside consultants. Boca Compl. at PP 87, 92, 94; Pub. Hosp. Compl. at PP 25, 66, 71. The

<sup>13</sup> The intracorporate conspiracy doctrine holds that acts of corporate agents are attributed to the corporation itself, thereby negating the multiplicity of actors necessary for the formation of a conspiracy." [Kirwin v. Price Commc' ns Corp., 391 F.3d 1323, 1326 \(11th Cir. 2004\)](#) (citing [McAndrew v. Lockheed Martin Corp., 206 F.3d 1031, 1035 \(11th Cir. 2000\)](#) (en banc)). When applicable, the doctrine precludes a finding of conspiracy because "a corporation cannot conspire with its employees, and its employees, when acting in the scope of their employment, cannot conspire among themselves." [Id.](#); see also [Copperweld Corp. v. Independence Tube Corp., 467 U.S. 752, 769, 104 S. Ct. 2731, 81 L. Ed. 2d 628 \(1984\)](#) (holding, in the antitrust context, that "officers or employees of the same firm do not provide the plurality of actors imperative for a [Sherman Antitrust Act] § 1 conspiracy.").

allegations of the Complaints are sufficient to indicate that Tenet and the hospitals that allegedly form the Tenet RICO enterprise, as well as its employees and officers, are legally distinct entities that played separate and distinct roles in the enterprise. Boca Compl. at PP 5, 92, 94, 96-97, 100, 105; see also Pub. Hosp. Compl. at PP 24-25, 66, 71, 73-74. Therefore, applying *Kushner* and *Kirwin*, the Hospital Plaintiffs have properly alleged a RICO enterprise sufficient to withstand a motion to dismiss.

### 3. Proximate Cause

**HN17** [↑] The "by reason of requirement contained in [18 U.S.C. § 1964\(c\)](#) implicates two concepts: (1) a sufficiently direct injury so that Plaintiffs have standing to sue; and (2) proximate cause, whereby the allegedly wrongful conduct is shown to be a substantial cause of the alleged injury and the causal [\*\*49] connection is foreseeable and not speculative. [Williams, 411 F.3d at 1260-61](#) (citations omitted). The Court has already concluded that Plaintiffs' allegations support their standing to sue Tenet. In order for the RICO claims to survive the Motions to Dismiss, the allegations must also support a finding of proximate cause.<sup>14</sup>

**HN18** [↑] "It is well-established that RICO plaintiffs must prove proximate causation in order to recover." [Id. at 1261](#) (citing [Cox v. Adm'r U.S. Steel & Carnegie, 17 F.3d 1386, 1399 \(11th Cir. 1994\)](#)). A proximate cause is not, however, the same thing as sole cause. Instead, a factor is a proximate cause if it is a substantial factor in [\*\*50] the sequence of responsible causation. *Id.* Here, even though Tenet argues that other intervening causes destroyed the causal chain between Tenet's actions and Plaintiffs' alleged injuries, Plaintiffs have alleged facts indicating that Tenet's "turbocharging" practice was a substantial factor in the causal chain leading to their injuries. For instance, Plaintiffs allege [\*1307] that as outlier claims skyrocketed, due in significant part to Tenet's overcharging scheme, CMS raised the Outlier Threshold to try to stay within the 5.1 percent target, consequently reducing the frequency and amount of the Plaintiffs' own outlier payments. Boca Compl. P 81; Pub. Hosp. Compl. P 59. Plaintiffs therefore allege that they were damaged by not receiving significant amounts of outlier funds to which they were otherwise entitled. Boca Compl. P 82; Pub. Hosp. Compl. PP 59-60. Finally, Plaintiffs allege that between June 1, 2000, and December 31, 2002, Tenet hospitals received an additional \$ 29 million per month, on average, in outlier payments, and that more than a third of Tenet's hospitals had dramatic increases in their outlier payments since 2000. Boca Compl. PP 54, 76; Pub. Hosp. Compl. PP 40, 56. [\*\*51] These allegations, if proven, would suggest that Tenet's alleged misconduct was a substantial link in the causal chain resulting in the Plaintiffs' financial injuries. Thus, for reasons similar to those identified in the standing section, the Court finds that Plaintiffs have sufficiently alleged proximate cause.<sup>15</sup> [Williams, 411 F.3d at 1262](#) ("although the plaintiffs in this case may not ultimately satisfy the proximate-cause requirement, . . . it remains possible that plaintiffs may prove their allegations, and [the Court] cannot say at this [Rule 12\(b\)\(6\)](#) stage that there is no possibility of such proof.").

### [\*\*52] E. Plaintiffs Have Stated a Claim for RICO Conspiracy

Tenet further challenges the sufficiency of Plaintiffs' allegations as it relates to their RICO conspiracy claims. **HN19** [↑] To establish a RICO conspiracy violation under [18 U.S.C. § 1962\(d\)](#), the Hospital Plaintiffs must allege "that the defendant objectively manifested, through words or actions, an agreement to participate in the conduct of the affairs of the enterprise through the commission of two or more predicate crimes." [United States v. Starrett, 55 F.3d 1525,](#)

<sup>14</sup> The Eleventh Circuit has recognized the significant overlap between the standing and proximate cause issues. [Williams, 411 F.3d at 1261, n.4](#). Notwithstanding the interconnectedness of the two concepts, the Court reviews the proximate cause issue as a separate, distinct element of a RICO claim.

<sup>15</sup> Tenet's argument regarding the presence of intervening players and acts, addressed in the standing section of this Order, also merits discussion here. As a general matter, the "presence of intervening factors breaks the causal chain between predicate acts and injury, thereby precluding a proximate cause finding." [Andrews v. Am. Nat'l Red Cross, Inc., 176 F. Supp. 2d 673, 689 \(W.D. Tex. 2001\)](#). However, at this stage of the litigation, the degree of involvement by each alleged actor in the causal chain is unknown, and Tenet has simply failed to demonstrate that it should be absolved of all liability merely because some other actors may have impacted on Plaintiffs' injuries.

[1543 \(11th Cir. 1995\)](#). "The focus is on the agreement to participate in the enterprise through the pattern of racketeering activity, not on the individual predicate acts." [Id. at 1544](#). Although Tenet "must [have] agreed to participate in the affairs of the enterprise," [United States v. Valera, 845 F.2d 923, 929 \(11th Cir. 1998\)](#), the Hospital Plaintiffs may prove Tenet's agreement: "(1) by showing an agreement on an overall objective, or (2) by showing that [Tenet] agreed personally to commit two predicate acts and therefore to participate in a single objective' conspiracy." [Starrett, 55 F.3d at 1544](#) [\*\*53] (citations omitted). Further, "to be guilty of conspiracy . . . parties must have agreed to commit an act that is itself illegal -- parties cannot be found guilty of conspiring to commit an act that is not itself against the law." [United States v. Vaghela, 169 F.3d 729, 732 \(11th Cir. 1999\)](#); see also [Jackson, 372 F.3d at 1269; Spain v. Brown & Williamson Tobacco Corp., 363 F.3d 1183, 1199](#) (11th Cir. 2004).

In summary, the Hospital Plaintiffs have alleged that Tenet agreed to participate in the conduct of the affairs of the enterprise: (1) when Tenet engaged in a scheme to improperly inflate the outlier [\[\\*1308\]](#) charges submitted to CMS; (2) when Tenet and its hospitals directly manipulated the charges submitted to CMS; (3) when "Tenet . . . agreed to participate, and participated, in an inflated charging scheme to steal and/or convert money from the Outlier Pool . . . "; and (4) when the object of the conspiracy was to illegally obtain excessive reimbursements from CMS. Boca Compl. at PP 75, 121-22; Pub. Hosp. Compl. at PP 52, 98-99. As alleged, Tenet and its hospital co-conspirators illegally inflated the claims submitted for outlier payments. [\[\\*\\*54\]](#) Boca Compl. at PP 49-61, 100(c) & (e); Pub. Hosp. Compl. at PP 34-41, 77(c) & (e). That agreement to violate the NSPA, if proven, demonstrates the existence of a conspiracy through the conspirators' actions. Thus, the Hospital Plaintiffs have properly pled that Tenet and its hospital co-conspirators were engaged in a conspiracy by alleging that they had an agreement on an overall objective. [Starrett, 55 F.3d at 1544; Valera, 845 F.2d at 929](#).

Tenet argues that the Plaintiffs have failed to allege facts, as opposed to legal conclusions, sufficient to sustain a finding that an agreement existed. In assessing the sufficiency of the conspiracy claim, the Court can look to whether the defendant's actions "manifested an agreement to participate" in the alleged racketeering activity. [Starrett, 55 F.3d at 1548](#). Further, [HN20](#) [↑] the Eleventh Circuit has recognized that, particularly at the pleading stage, the RICO conspiracy need not be supported by direct evidence, but rather, may be inferred from the parties' conduct. [Republic of Panama v. BCCI Holdings \(Luxembourg\) S.A., 119 F.3d 935, 950 \(11th Cir. 1997\)](#). Although the allegations [\[\\*\\*55\]](#) in the Complaints border on being conclusory, given the liberal notice pleadings standard applicable to this claim, the allegations suffice to survive dismissal. Plaintiffs have asserted extensive allegations, as noted above, from which it can be inferred that Tenet's "turbocharging" scheme was devised as part of a conspiracy. Accordingly, while this issue must be further developed during discovery and may be revisited on summary judgment, the Court cannot grant Tenet's motion to dismiss the conspiracy claim at this time.

## F. Unjust Enrichment

[HN21](#) [↑] Under Florida law, to state a claim for unjust enrichment, the plaintiff must allege that: (1) the plaintiff conferred a benefit on the defendant, who had knowledge of the benefit; (2) the defendant voluntarily accepted and retained the benefit; and (3) under the circumstances, it would be inequitable for the defendant to retain the benefit without paying for it. [Greenberg v. Miami Children's Hosp. Research Inst., 264 F. Supp. 2d 1064, 1072 \(S.D. Fla. 2003\)](#) (citing [Toolrend, Inc. v. CMT Utensili, SRL, 198 F.3d 802, 805 \(11th Cir. 1999\)](#)); see also [Duncan v. Kasim, Inc., 810 So.2d 968, 971 \(Fla. 2002\)](#). [\[\\*\\*56\]](#) Tenet seeks dismissal of this claim on the dual basis that Plaintiffs have failed to demonstrate that they actually conferred any benefit on Tenet, and that the Plaintiffs cannot base an unjust enrichment claim on alleged wrongdoing for which an independent basis for recovery exists.

In support of their claim, the Hospital Plaintiffs assert that they conferred a benefit on Tenet "because the reductions in the standardized amount they were to receive under IPPS have been used to pay Tenet for the inflated and improper costs' it claimed in connection with the treatment of Outlier patients. Thus the monies received by Tenet from the Outlier Pool far exceeded the true costs of treating the aforesaid Outlier patients." See Boca Compl. at P 141. Tenet contends that because the Hospital Plaintiffs have no right, or any colorable claim of title, to the outlier funds, they cannot demonstrate that [\[\\*1309\]](#) they actually conferred any benefit on Tenet or that anything was actually taken away from them. Further, Tenet argues that even if the Court finds that the Hospital

Plaintiffs did confer some benefit on Tenet by virtue of their reduced standardized reimbursements, such benefit is far too indirect [\*\*57] to maintain an unjust enrichment claim. See [Nova Info. Sys., Inc. v. Greenwich Ins. Co., 365 F.3d 996, 1007 \(11th Cir. 2004\)](#) (finding that "at best, [the plaintiff] conferred an indirect or incidental benefit on [the defendant]," which could not support a claim for compensation under the doctrine of unjust enrichment).

The Court need not reach the issue of whether the Hospital Plaintiffs actually conferred a benefit on Tenet, because the allegations of the Complaint, which are premised on Tenet's purported RICO violations and theft of outlier funds, cannot support a claim for unjust enrichment. [HN22](#) [↑] "Liability in unjust enrichment has in principle nothing to do with fault. It has to do with wealth being in one person's hands when it should be in another person's." [Guyana Tel. & Tel. Co. v. Melbourne Int'l Comms., Ltd., 329 F.3d 1241, 1245 n.3 \(11th Cir. 2003\)](#). Thus, the "paradigm examples of unjust enrichment are mistaken transfers." *Id.* However, as soon as a claimant relies on a wrong to supply the unjust factor, as the Hospital Plaintiffs do here, "the right on which [the plaintiff] relies arises from that wrong, not from unjust enrichment. [\*\*58]" *Id.* (citation omitted). Here, the Hospital Plaintiffs predicate their unjust enrichment claim on "the wrongful conduct of Tenet" in allegedly submitting "inflated and improper costs." Boca Compl. at PP 188, 189; Pub. Hosp. Compl. at PP 142-43. The Plaintiffs' right of recovery, if any, "arises from the wrong of the [alleged] tort," which, if proven, might entitle them to damages, "rather than unjust enrichment." [Guyana, 329 F.3d at 1245 n.3](#). Because "the law of unjust enrichment is concerned solely with enrichments that are unjust independently of [alleged] wrongs," Plaintiffs' unjust enrichment claims must be dismissed. [Flint v. ABB, Inc., 337 F.3d 1326, 1330 n.2 \(11th Cir. 2003\)](#) (noting that when the plaintiff relies on a wrong to supply the unjust factor, "the causative event is a wrongful enrichment rather than an unjust enrichment").

## G. Florida Deceptive and Unfair Trade Practices Act

Tenet's challenge to the Florida Attorney General's FDUTPA claim is two-fold. First, Tenet contends that because its alleged conduct was authorized by then-applicable Medicare regulations, it cannot form the basis for a FDUTPA claim. Second, Tenet [\*\*59] argues that the FDUTPA claim must fail because it is not pled with particularity in accordance with [Fed. R. Civ. P. 9\(b\)](#). Upon careful review of the allegations in the Pub. Hosp. Compl., both arguments must fail.

The Florida legislature enacted FDUTPA to protect the "consuming public and legitimate business enterprises from those who engage in unfair methods of competition, or unconscionable, deceptive, or unfair acts or practices in the conduct of any trade or commerce." [Fla. Stat. §§ 501.202\(2\), 501.204\(1\) \(2005\)](#). [HN23](#) [↑] To state a cause of action under FDUTPA, the complaint must not only plead that the conduct complained of was unfair and deceptive, but also that the complaining party was aggrieved by the alleged act. [Haun v. Don Mealey Imps., 285 F. Supp. 2d 1297, 1308 \(M.D. Fla. 2003\)](#). A FDUTPA plaintiff, therefore, need only allege facts sufficient to show that it was actually aggrieved by the unfair and deceptive conduct. [Tuckish v. Pompano Motor Co., 337 F. Supp. 2d 1313, 1320 \(S.D. Fla. 2004\)](#). A court, in determining whether the alleged conduct violates FDUTPA, should [\*1310] also take into [\*\*60] consideration whether the Federal Trade Commission and other federal courts deem such conduct to be an "unfair method of competition or an unconscionable, unfair or deceptive act or practice under federal law." [Mack v. Bristol-Myers Squibb Co., 673 So.2d 100, 105 \(Fla. 1st DCA 1996\)](#). Because the legislature did not define what is an unfair or deceptive act, a practice which "offends established public policy or is immoral, unethical, oppressive, unscrupulous or substantially injurious to consumers may violate FDUTPA." [Betts v. Advance Am., 213 F.R.D. 466, 482 \(M.D. Fla. 2001\)](#).

[HN24](#) [↑] It is well-established that FDUTPA does not apply to any acts or practices that are "required or specifically permitted by federal or state law." [3B TV, Inc. v. Office of Atty. Gen., 794 So.2d 744, 747 \(Fla. 1st DCA 2001\)](#) (quoting [Fla. Stat. § 501.212\(1\)](#)); see also [Eirman v. Olde Disc. Corp., 697 So.2d 865, 866 \(Fla. 4th DCA 1997\)](#) (holding that conduct did not violate FDUTPA because it was authorized by then-existing rules of the U.S. Securities & Exchange Commission). However, an act does not need to violate a specific rule or regulation [\*\*61] in order to be considered deceptive. [Dep't of Legal Affairs v. Father & Son Moving & Storage, Inc., 643 So.2d 22, 24 \(Fla. 4th DCA 1994\)](#). Therefore, the relevant analysis for this Court is whether Tenet, as the moving party, has

demonstrated that a specific federal or state law affirmatively authorized it to engage in the conduct alleged in the Complaints, *not* whether Plaintiffs have demonstrated that Tenet's conduct violates a specific rule or regulation.

Other than its conclusory assertion that its "alleged conduct was authorized by then-applicable Medicare regulations," see Def.'s Mem. at 38, Tenet does not identify any federal statute or regulation that "specifically permitted" it to grossly inflate its charges for outlier procedures in order to garner outlier payments for average-cost Medicare cases, as alleged in the Complaints. Tenet merely cites to [42 C.F.R. § 412.84](#) (which provides the regulatory guidelines for outlier payments) and states, with no supporting analysis or factual discussion, that "submitting accurate charges" is specifically permitted. Of course, the Plaintiffs maintain that the charges that Tenet used to [\[\\*\\*62\]](#) maximize its outlier reimbursements were not accurate, in the sense that they did not correlate reasonably to the actual costs of the procedures being performed. See Pub. Hosp. Compl. at P 36. Therefore, accepting the Plaintiffs' allegations as true, and viewing those allegations in the light most favorable to the Plaintiffs, Tenet's alleged conduct may form the basis for a FDUTPA claim.

Likewise, Tenet's insistence that the Florida AG must plead its FDUTPA claim "with particularity" is without merit. Tenet correctly states that [Fed. R. Civ. P. 9\(b\)](#) requires that in all averments of fraud, the circumstances constituting fraud "shall be stated with particularity." However, the Florida AG's FDUTPA claim is not premised on allegations of fraud. [HN25](#) FDUTPA was enacted to provide remedies for conduct outside the reach of traditional common law torts such as fraud, and therefore, "the plaintiff need not prove the elements of fraud to sustain an action under the statute." *Davis v. Powertel, Inc.*, 776 So.2d 971, 974 (Fla. 1st DCA 2000); see also [Office of Attorney Gen., Dept. of Legal Affairs v. Wyndham Int'l, Inc.](#), 869 So.2d 592, 598 (Fla. 1st DCA 2004) [\[\\*\\*63\]](#) ("A deceptive or unfair trade practice constitutes a somewhat unique tortious act because, although it is similar to a claim of fraud, it is different in that, unlike fraud, a party asserting a deceptive trade practice claim need not show actual reliance on the representation or omission at [\[\\*1311\]](#) issue."). Accordingly, the Florida AG's failure to allege facts constituting fraud is not fatal to its FDUTPA claim.<sup>16</sup>

#### H. Boca's Claim Under the California Unfair Competition Law

[HN26](#) [Section 17200](#) of the California Unfair Competition Law ("UCL") provides a remedy for any injuries resulting from unfair competition, defined as "any unlawful, unfair or fraudulent business act or practice." [Cal. Bus. & Prof. Code § 17200](#) [\[\\*\\*64\]](#). Tenet argues that: (1) Boca, a resident of Florida, cannot assert a claim under the UCL because of the fundamental limits on the scope of state regulatory jurisdiction; (2) Boca has not alleged an unlawful, unfair or fraudulent business practice; and (3) Boca is not entitled to restitution. Upon review of the applicable case law, the Court disagrees.

First, Tenet's argument with respect to the territorial limitations of the UCL overlooks the fact that Boca has alleged unfair conduct occurring in the State of California. Specifically, Boca alleges that Tenet devised, implemented, and directed the scheme that is the subject of the Complaints at its executive headquarters in Santa Barbara, California. See Boca Compl. at PP 5, 170. Boca further alleges that Tenet ultimately received the ill-gotten gains from its outlier overcharge scheme in California. *Id.* at PP 78-80, 100(g), 105, 107, 112-13, 171. Because Boca has alleged that it was harmed by wrongful conduct occurring in California, Boca may assert a claim under the UCL.<sup>17</sup>

<sup>16</sup> In a footnote, Tenet also argues that the FDUTPA claim must be dismissed to the extent that the Florida AG seeks recovery for conduct prior to July 1, 2001. See Def.'s Mem. at n. 16. However, Tenet has not demonstrated that these pre-2001 claims are subject to dismissal at this time.

<sup>17</sup> Tenet's reliance on [Norwest Mortgage, Inc. v. Superior Court](#), 72 Cal. App. 4th 214, 225-26, 85 Cal. Rptr. 2d 18 (Cal. Ct. App. 1999) is misplaced. Tenet relies on *Norwest* for its assertion that Boca's UCL claim must be dismissed. However, in *Norwest*, the Court specifically held that it was dismissing the UCL claim because the facts demonstrated that the non-Californians were injured by conduct occurring outside of California's borders, by defendants whose headquarters and principal places of operation are outside of California. *Id.* Here, as noted above, Boca has specifically alleged conduct taking place in California, and Tenet's executive headquarters are in Santa Barbara, California.

Diamond Multimedia Sys., Inc. v. Superior Court, 19 Cal.4th 1036, 1063-64, 80 Cal. Rptr. 2d 828, 968 P.2d 539(Cal. 1999) HN27<sup>18</sup> (finding no constitutional impediment in permitting [\*\*65] non-Californians a right of action under a domestic statute because California had a "clear and substantial interest in preventing fraudulent practices in this state," or in "extending state-created remedies to out-of-state parties harmed by wrongful conduct occurring in California.") (emphasis in original) (citations omitted).

[\*\*66] Second, Tenet incorrectly states that Boca has failed to state a claim under the UCL. Boca's claim is premised on the unlawful and unfair prongs of the UCL.<sup>18</sup> In Watson Labs., Inc. v. Rhone-Poulenc Rorer, Inc., 178 F. Supp. 2d 1099, 1120 (C.D. Cal. 2001), HN28<sup>19</sup> the court defined "unlawful acts" under the UCL as business practices that constitute violations of civil or criminal, federal or regulatory law. *Id.* Thus, a claimant may "borrow" a violation of another law that is committed in the course of business activity to support a claim under § 17200. *Id.*; see also Korea Supply Co. v. Lockheed Martin Corp., 29 Cal. 4th 1134, 1143, 131 Cal. Rptr. 2d 29, 63 P.3d 937 (Cal. 2003). An adequately pled RICO violation is sufficient to support a claim under the unlawful prong of California's [\*1312] UCL. Conn. Gen. Life Ins. Co. v. New Images of Beverly Hills, 108 Fed. Appx. 497, 498 (9th Cir. 2004). Because the Court previously concluded that Boca's Complaint states a claim under RICO, such allegations suffice to support Tenet's UCL claim. Boca has also adequately alleged unfair business practices. See Cel-Tech Commc ns, Inc. v. Los Angeles Cellular Tel. Co., 20 Cal.4th 163, 187, 83 Cal. Rptr. 2d 548, 973 P.2d 527 (Cal. 1999) [\*\*67] (finding that unfair conduct is that which "threatens an incipient violation of an **antitrust law**, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law or otherwise significantly threatens or harms competition."). Tenet's motion to dismiss Boca's UCL claim is, therefore, denied.

#### IV. CONCLUSION

For the reasons discussed above, it is hereby

ORDERED that:

- (1) Defendant Tenet Healthcare Corporation's Motions to Dismiss filed in Case No. 05-20591-CIV-SEITZ [DE-29] and Case No. 05-80183 [DE-30] are GRANTED IN PART, DENIED IN PART;
- (2) The Motions to Dismiss are GRANTED to the extent that Plaintiffs' unjust enrichment claims, set forth in Count VI in Case No. 05-20591-CIV-SEITZ and Count VII in Case No. 05-80183-CIV-SEITZ, are DISMISSED WITH PREJUDICE;
- (3) The Motions to Dismiss are DENIED in all other aspects.

DONE [\*\*68] AND ORDERED in Miami, Florida, this 25th day of August, 2005.

PATRICIA A. SEITZ

UNITED STATES DISTRICT JUDGE

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End of Document

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<sup>18</sup> Boca is not proceeding on the theory that Tenet's practices were fraudulent. See Pls.' Mem. at n. 26.



## *Freeman Indus. LLC v. Eastman Chem. Co.*

Supreme Court of Tennessee, At Knoxville

May 3, 2005, Session ; August 25, 2005, Filed

No. E2003-00527-SC-S09-CV

### **Reporter**

172 S.W.3d 512 \*; 2005 Tenn. LEXIS 668 \*\*; 2005-2 Trade Cas. (CCH) P94,914

FREEMAN INDUSTRIES, LLC v. EASTMAN CHEMICAL COMPANY, ET AL.

**Subsequent History:** Appeal after remand at, Remanded by [\*Freeman Indus. LLC v. Eastman Chem. Co., 2006 Tenn. App. LEXIS 761 \(Tenn. Ct. App., Nov. 30, 2006\)\*](#)

**Prior History:** [\*\*1] Tenn. R. App. P. 11 Appeal by Permission; Judgment of the Court of Appeals Affirmed in Part; Reversed in Part; Remanded to the Trial Court. Appeal by Permission from the Court of Appeals Circuit Court for Sullivan County. No. C34355-L. Richard E. Ladd, Chancellor.

[\*Freeman Indus. L.L.C. v. Eastman Chem. Co., 2004 Tenn. App. LEXIS 321 \(Tenn. Ct. App., May 18, 2004\)\*](#)

**Disposition:** Judgment of the Court of Appeals Affirmed in Part; Reversed in Part; Remanded to the Trial Court.

## **Core Terms**

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purchasers, indirect, unjust enrichment, commerce, anticompetitive conduct, trial court, antitrust, effects, sorbates, interstate commerce, anti trust law, defendants', remedies, consumer, exhaust, circumstances, courts, supermarket, contracts, violator, prices, substantial effect, cause of action, overcharge, futile, antitrust statute, bring suit, regulation, products, principal place of business

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrers & Objections > Motions to Dismiss

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

Civil Procedure > Appeals > Standards of Review > De Novo Review

### **HN1[ Motions to Dismiss, Failure to State Claim**

A motion to dismiss a complaint for failure to state a claim pursuant to Tenn. R. Civ. P. 12.02(6) admits the truth of all of the relevant and material allegations contained in the complaint, but it asserts that the allegations fail to establish a cause of action. When reviewing a dismissal of a complaint under Rule 12.02(6), the court must take the

factual allegations of the complaint as true and review the trial court's legal conclusions de novo without any presumption of correctness.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN2[] Regulated Practices, Price Fixing & Restraints of Trade**

Tenn. Code Ann. § 47-25-106 (2001) provides for a civil remedy against those who violate the Tennessee Trade Practices Act (TTPA), Tenn. Code Ann. § 47-25-101 et seq. (2001).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN3[] Regulated Practices, Price Fixing & Restraints of Trade**

See Tenn. Code Ann. § 47-25-106.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN4[] Regulated Practices, Price Fixing & Restraints of Trade**

By providing a civil remedy to "any person who is injured or damaged" as the result of violations of the Tennessee Trade Practices Act (TTPA), Tenn. Code Ann. § 47-25-101 et seq. (2001), the plain language of Tenn. Code Ann. § 47-25-106 provides a cause of action to indirect purchasers.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN5[] Regulated Practices, Price Fixing & Restraints of Trade**

The plain language of Tenn. Code Ann. § 47-25-106 does not prohibit recovery to indirect purchasers who are nonresidents of Tennessee. Moreover, Tenn. Code Ann. §§ 47-25-101 and 47-25-102 (2001) prohibit price fixing agreements that tend to affect the price to the "producer or consumer" of such products. These statutes reflect a clear intent to protect and afford a remedy to ultimate consumers.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Contracts Law > Defenses > Public Policy Violations

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN6**  **Regulated Practices, Price Fixing & Restraints of Trade**

See [Tenn. Code Ann. § 47-25-101](#) (2001).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Contracts Law > Defenses > Public Policy Violations

Antitrust & Trade Law > Public Enforcement > State Civil Actions

**HN7**  **Regulated Practices, Price Fixing & Restraints of Trade**

See [Tenn. Code Ann. § 47-25-102](#).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Business & Corporate Compliance > ... > Types of Damages > Consequential Damages > Actions for Price

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

**HN8**  **Regulated Practices, Price Fixing & Restraints of Trade**

The Supreme Court of Tennessee has identified two purposes of the Tennessee Trade Practices Act (TTPA), [Tenn. Code Ann. § 47-25-101 et seq.](#) (2001). The first purpose is to preserve full and free competition in the sale of merchandise that "had become a part of the mass of property in the State." The second purpose is to preserve full and free competition in the manufacture and sale of "articles of domestic growth and domestic raw material" and to prevent combinations tending to affect the price or cost of these articles to the producer or consumer. Permitting indirect purchasers to recover under the TPPA promotes these purposes.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

**HN9**  **Regulated Practices, Trade Practices & Unfair Competition**

"Control" means power or authority to manage, direct, superintend, restrict, regulate, govern, administer, or oversee as well as the ability to exercise a restraining or directing influence over something. A sale "controlled by" an antitrust violation includes not only a sale made by the violator to the direct purchaser but also a transaction

between the direct purchaser and the consumer in which the price of the product purchased by the consumer is influenced by the antitrust violator's conduct.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > State Regulation

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN10** [blue download icon] **Purchasers, Direct Purchasers**

A plain reading of [Tenn. Code Ann. § 47-25-106](#) permits a person to recover the consideration or sum that was "controlled by" or influenced by the antitrust violator. In other words, an indirect purchaser may recover from the antitrust violator the amount of the overcharge that the direct purchaser passed on to the indirect purchaser.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

#### **HN11** [blue download icon] **Purchasers, Direct Purchasers**

Indirect purchasers do not have a cause of action under federal **antitrust law** because they do not suffer a legally cognizable injury.

Antitrust & Trade Law > Clayton Act > General Overview

#### **HN12** [blue download icon] **Antitrust & Trade Law, Clayton Act**

See [15 U.S.C.S. § 15](#).

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **HN13** [blue download icon] **Antitrust & Trade Law, Clayton Act**

The United States Supreme Court's holding in Illinois Brick Co. applies only to federal antitrust law. Clearly, states may provide a remedy to indirect purchasers under their own antitrust laws.

Governments > Legislation > Interpretation

#### **HN14** [ ↗ ] **Legislation, Interpretation**

While legislative inaction is generally irrelevant to the interpretation of existing statutes, the legislature's failure to express disapproval of a judicial construction of a statute is persuasive evidence of legislative adoption of the judicial construction.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Private Actions > Standing > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN15** [ ↗ ] **Regulated Practices, Price Fixing & Restraints of Trade**

Unlike many states that have applied Illinois Brick Co. in disallowing indirect purchasers from bringing a private action under their antitrust laws, Tennessee does not have a statutory "harmony clause" mandating courts to interpret the Tennessee Trade Practices Act (TTPA), [Tenn. Code Ann. § 47-25-101 et seq.](#) (2001), consistently with federal law.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN16** [ ↗ ] **Regulated Practices, Price Fixing & Restraints of Trade**

The Supreme Court of Tennessee joins other jurisdictions in declining to interpret Illinois Brick Co. v. Illinois as precluding indirect purchasers from bringing suit under the Tennessee Trade Practices Act (TTPA), [Tenn. Code Ann. § 47-25-101 et seq.](#) (2001).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [HN17](#) [blue download icon] Regulated Practices, Price Fixing & Restraints of Trade

By construing [\*Tenn. Code Ann. § 47-25-106\*](#) (2001) as permitting indirect purchaser suits, the Supreme Court of Tennessee is affording a remedy to the ultimate victims of the antitrust conduct.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [HN18](#) [blue download icon] Regulated Practices, Price Fixing & Restraints of Trade

Antitrust is a complex area of law and generally involves highly complex litigation. The ends of justice should not be defeated simply because the risk of complicated litigation exists.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [HN19](#) [blue download icon] Regulated Practices, Price Fixing & Restraints of Trade

An indirect purchaser may bring an action under [\*Tenn. Code Ann. § 47-25-106\*](#) for conduct in violation of the Tennessee Trade Practices Act (TTPA), [\*Tenn. Code Ann. § 47-25-101 et seq.\*](#) (2001), even though the indirect purchaser is a non-resident of Tennessee.

Antitrust & Trade Law > Sherman Act > Penalties

Governments > State & Territorial Governments > Legislatures

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [HN20](#) [blue download icon] Sherman Act, Penalties

In considering the reach of the Tennessee Trade Practices Act (TTPA), [\*Tenn. Code Ann. § 47-25-101 et seq.\*](#) (2001), the Supreme Court of Tennessee has concluded that the legislature clearly intended to prohibit trusts, combinations, and agreements affecting all commerce not covered by the federal statute, and upon which it had a right to legislate. It did not intend to stop short of its power or to exceed it.

Governments > Legislation > Interpretation

## [HN21](#) [blue download icon] Legislation, Interpretation

Courts have a duty to construe statutes in such a manner as to avoid conflict with the United States Constitution if the construction can be accomplished without disregarding the legislature's intent.

Governments > Legislation > Interpretation

Governments > Legislation > Overbreadth

#### **HN22** [blue document icon] **Legislation, Interpretation**

Although a statute includes terms that are overly broad, courts have a duty to limit a statute's application to circumstances within the legislature's intent.

Antitrust & Trade Law > Procedural Matters > Jurisdiction > Exclusive Jurisdiction

Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > Exclusive Jurisdiction

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

#### **HN23** [blue document icon] **Jurisdiction, Exclusive Jurisdiction**

The United States Supreme Court considers state antitrust regulations to supplement and complement the federal antitrust laws and the enforcement of these state laws to be consistent with the federal antitrust laws. Furthermore, a state generally is not prohibited from giving effect to its antitrust laws merely because the regulation affects interstate commerce.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Transportation Law > Interstate Commerce > Balancing Tests

Business & Corporate Compliance > ... > Transportation Law > Interstate Commerce > State Powers

Constitutional Law > Congressional Duties & Powers > Commerce Clause > General Overview

#### **HN24** [blue document icon] **Public Enforcement, State Civil Actions**

A state antitrust regulation that has only incidental effects on interstate commerce and is regulated evenhandedly to effectuate a legitimate local interest does not run afoul of the Commerce Clause unless the burden imposed on interstate commerce is clearly excessive when compared to the punitive local benefits.

Governments > Legislation > Interpretation

#### **HN25** [blue document icon] **Legislation, Interpretation**

In construing statutes, the court must ascertain and give effect to the legislature's intent and purpose. Furthermore, the court must construe a statute so as to avoid a constitutional conflict if any reasonable construction exists that satisfies the Constitution's requirements.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Transportation Law > Intrastate Commerce

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN26**[] **Regulated Practices, Price Fixing & Restraints of Trade**

The Tennessee Trade Practices Act (TTPA), [\*Tenn. Code Ann. § 47-25-101 et seq.\*](#) (2001), prohibits agreements adversely affecting competition in the "sale of articles imported into this state" or influencing the "price or the cost to the producer or the consumer of any such product or article." [\*Tenn. Code Ann. § 47-25-101\*](#) (2001).

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN27**[] **Regulated Practices, Price Fixing & Restraints of Trade**

The purpose of the Tennessee Trade Practices Act (TTPA), [\*Tenn. Code Ann. § 47-25-101 et seq.\*](#) (2001), is to protect the state's trade or commerce affected by the anticompetitive conduct. The Supreme Court of Tennessee rejects any standard that requires examination of the anticompetitive conduct in determining whether a particular case falls within the scope of the TTPA.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Transportation Law > Intrastate Commerce

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN28**[] **Regulated Practices, Price Fixing & Restraints of Trade**

Anticompetitive conduct cannot predominantly affect both intrastate commerce and interstate commerce.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## **HN29**[] **Regulated Practices, Price Fixing & Restraints of Trade**

The proper standard for determining whether a case falls within the scope of the Tennessee Trade Practices Act (TTPA), [Tenn. Code Ann. § 47-25-101 et seq.](#), is a "substantial effects" standard. Pursuant to this standard, courts must decide whether the alleged anticompetitive conduct affects Tennessee trade or commerce to a substantial degree. Federal courts have applied the substantial effects standard to the Sherman Antitrust Act.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### [HN30](#) [L] **Regulated Practices, Price Fixing & Restraints of Trade**

A "substantial effects" standard for determining whether alleged anticompetitive conduct affects Tennessee trade or commerce to a substantial degree furthers the goal of the Tennessee Trade Practices Act, [Tenn. Code Ann. § 47-25-101 et seq.](#), of protecting Tennessee commerce without offending constitutional provisions.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Transportation Law > Intrastate Commerce

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### [HN31](#) [L] **Regulated Practices, Price Fixing & Restraints of Trade**

The determination of whether an effect is substantial does not involve "mathematical nicety." The anticompetitive conduct, however, need not threaten the demise of Tennessee businesses or affect market prices to substantially affect intrastate commerce.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

### [HN32](#) [L] **Entitlement as Matter of Law, Appropriateness**

Summary judgment is appropriate only when the moving party demonstrates that no genuine issues of material fact exist and that the moving party is entitled to judgment as a matter of law. Tenn. R. Civ. P. 56.04.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

### [HN33](#) [L] **Summary Judgment, Entitlement as Matter of Law**

The purpose of summary judgment is to resolve controlling issues of law rather than to find facts or resolve disputed factual issues.

Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

#### **HN34** [ ] **Standards of Review, De Novo Review**

The court must review a trial court's decision to grant or deny summary judgment de novo with no presumption of correctness attached to the trial court's conclusions. It must also view the evidence in the light most favorable to the non-moving party, drawing all reasonable inferences in the non-moving party's favor.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Contracts Implied in Fact

Contracts Law > Remedies > Equitable Relief > General Overview

Contracts Law > Types of Contracts > General Overview

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Quasi Contracts

#### **HN35** [ ] **Types of Contracts, Contracts Implied in Fact**

The court has previously recognized two types of implied contracts: contracts implied in fact and contracts implied in law. Contracts implied in fact arise under circumstances establishing the parties' mutual intention to contract. Contracts implied in law or quasi contracts are created by law without the parties' assent and are based upon reason and justice. Courts may impose a contract implied in law where no contract exists under various quasi contractual theories, including unjust enrichment.

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN36** [ ] **Remedies, Equitable Relief**

The elements of an unjust enrichment claim are: 1) a benefit conferred upon the defendant by the plaintiff; 2) appreciation by the defendant of such benefit; and 3) acceptance of such benefit under such circumstances that it would be inequitable for him to retain the benefit without payment of the value thereof. The most significant requirement of an unjust enrichment claim is that the benefit to the defendant be unjust. The plaintiff must further demonstrate that he or she has exhausted all remedies against the person with whom the plaintiff enjoyed privity of contract.

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN37** [ ] **Remedies, Equitable Relief**

A plaintiff need not be in privity with a defendant to recover under a claim of unjust enrichment.

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN38**[ Remedies, Equitable Relief

A benefit is any form of advantage that has a measurable value including the advantage of being saved from an expense or loss. The underlying principle of the doctrine of unjust enrichment is that a party who receives a benefit that he or she desires, under circumstances rendering retention of the benefit without providing compensation inequitable, must compensate the provider of the benefit.

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN39**[ Remedies, Equitable Relief

To recover for unjust enrichment, a plaintiff need not establish that the defendant received a direct benefit from the plaintiff. Rather, a plaintiff may recover for unjust enrichment against a defendant who receives any benefit from the plaintiff if the defendant's retention of the benefit would be unjust.

Civil Procedure > ... > Justiciability > Exhaustion of Remedies > General Overview

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN40**[ Justiciability, Exhaustion of Remedies

To maintain an action for unjust enrichment, a plaintiff is not required to exhaust all remedies against the party with whom the plaintiff is in privity if the pursuit of the remedies would be futile.

**Counsel:** Barry C. Barnett, Dallas, Texas; Daniel R. Karon, Cleveland, Ohio; Isaac L. Diel and Rex A. Sharp, Prairie Village, Kansas; John S. Bingham, Kingsport, Tennessee; and Todd R. Seelman, Denver, Colorado, for the appellant, Freeman Industries, LLC.

Herbert S. Washer, New York, New York, and Morris Hadden, Kingsport, Tennessee, for the appellee, Daicel Chemical Industries, Ltd.

Michelle K. Fisher and Thomas Demittrack, Cleveland, Ohio, and William T. Gamble, Kingsport, Tennessee, for the appellee, Eastman Chemical Company.

Jennifer B. Patterson and Michael D. Blechman, New York, New York, and Morris Hadden, Kingsport, Tennessee, for the appellees, Hoechst Aktiengesellschaft and Nutrinova Nutrition Specialities & Food Ingredients, GmbH.

Eugene G. Illovsy, Walnut Creek, California, and Morris Hadden, Kingsport, **[\*\*2]** Tennessee, for the appellee, Nippon Gohsei Industries, Ltd.

**Judges:** JANICE M. HOLDER, J., delivered the opinion of the court, in which FRANK F. DROWOTA, III, C.J., and E. RILEY ANDERSON, ADOLPHO A. BIRCH, JR., and WILLIAM M. BARKER, JJ., joined.

**Opinion by:** JANICE M. HOLDER

## **Opinion**

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[\*515] We granted permission to appeal to determine: 1) whether an indirect purchaser may bring an action under the Tennessee Trade Practices Act against defendants involved in an price-fixing scheme; 2) whether the conduct complained of falls within the scope of the act; and 3) whether the trial court erred in declining to grant summary judgment to the defendants as to the plaintiff's unjust enrichment claim. We conclude that although an indirect purchaser may bring an action under the Tennessee Trade Practices Act, the conduct complained of in this case did not substantially affect Tennessee commerce and thus falls outside the scope of the act. We further conclude that to sustain an unjust enrichment claim, the plaintiff is not required to: 1) establish that the defendants received a direct benefit or 2) exhaust all remedies against the party with whom the plaintiff is in privity if the pursuit of the remedies would be [\*516] futile. Because the plaintiff failed to provide a factual basis to support its bare allegation that any attempt to exhaust its remedies would have been futile, the trial court erred in failing to grant the defendants' motion for summary judgment on the unjust enrichment claim. Accordingly, the judgment of the Court of Appeals is affirmed in part and reversed in part, and the case is remanded [\*\*3] to the trial court for further proceedings in accordance with this opinion.

Defendant Eastman Chemical Co. ("Eastman") is a Delaware corporation with its principal place of business in Kingsport, Tennessee. Defendants Hoechst Aktiengesellschaft ("Hoechst") and Nutrinova Nutrition Specialities & Food Ingredients, GmbH ("Nutrinova") are German corporations with principal places of business in Frankfurt, Germany. Defendants Daciel Chemical Industries, Ltd. ("Daciel") and Nippon Gohsei Industries, Ltd. ("Nippon") are Japanese corporations with principal places of business in Tokyo and Osaka, Japan, respectively. Eastman, Hoechst, Nutrinova, Daciel, and Nippon (collectively "defendants") are producers of sorbates. Sorbates are food preservatives used in small quantities in high-moisture and high-sugar [\*\*4] products to slow the growth of mold.

Between 1998 and 2001, each defendant pleaded guilty to fixing the prices of sorbates in violation of the Sherman Antitrust Act. See 15 U.S.C. § 1 (1997). The defendants also have settled federal lawsuits brought by a nationwide class of direct purchasers of sorbates as well as lawsuits brought by indirect purchasers in fourteen states, including Tennessee, and the District of Columbia.

Plaintiff Freeman Industries, LLC ("Freeman") is a New York corporation with its principal place of business in Tuckahoe, New York. Freeman is an end-user of food products containing sorbates and purchases these products at supermarkets in New York. Freeman, as an indirect purchaser of sorbates, filed a lawsuit against the defendants claiming a violation of the Tennessee Trade Practices Act ("TTPA"), Tenn. Code Ann. § 47-25-101 et seq. (2001), and unjust enrichment.

The trial court granted the defendants' motion to dismiss Freeman's TTPA claim. The trial court concluded that the TTPA does not apply to indirect purchasers or to transactions occurring outside of Tennessee. The trial court denied the defendants' [\*\*5] motion for summary judgment as to Freeman's unjust enrichment claim.

On interlocutory review, the Court of Appeals concluded that although indirect purchasers may recover under the TTPA, the act does not apply to indirect purchasers who are not "Tennessee consumers." The Court of Appeals further concluded that Freeman could not recover under the TTPA because it failed to establish that it "had a transaction *in Tennessee* that was substantially affected by the defendants' illegal conduct." With respect to Freeman's unjust enrichment claim, the Court of Appeals held that a plaintiff is not required to confer a direct benefit upon a defendant to proceed with a claim for unjust enrichment. The Court of Appeals therefore modified the portion of the trial court's judgment that held that the TTPA is not applicable to indirect purchasers and affirmed the trial court's judgment in all other respects. We granted review.

## ANALYSIS

### A. Tennessee Trade Practices Act

We must first decide whether the trial court erred in granting the defendants' motion to dismiss Freeman's TTPA claims pursuant to Tennessee Rule of Civil Procedure 12.02(6). HN1 A motion to dismiss a complaint for

failure [\*\*6] to state a claim pursuant to [Rule 12.02\(6\)](#) "admits the truth of all of the relevant and material allegations contained in the complaint, but it asserts that the allegations fail to establish a cause of action." [Leach v. Taylor, 124 S.W.3d 87, 90 \(Tenn. 2004\)](#). When reviewing a dismissal of a complaint under [Rule 12.02\(6\)](#), we must take the factual allegations of the complaint as true and review the trial [\*517] court's legal conclusions de novo without any presumption of correctness. *Id.*

## 1. Indirect Purchasers

[HN2](#) [Tennessee Code Annotated section 47-25-106](#) (2001) provides for a civil remedy against those who violate the TPPA. [Section 47-25-106](#) states that:

[HN3](#) any person who is injured or damaged by any such arrangement, contract, agreement, trust, or combination described in this part may sue for and recover, in any court of competent jurisdiction, from any person operating such trust or combination, the full consideration or sum paid by the person for any goods, wares, merchandise, or articles, the sale of which is controlled by such combination or trust.

[HN4](#) By providing a civil remedy to "any person who is injured or damaged" as the [\*\*7] result of violations of the TPPA, the plain language of [section 47-25-106](#) provides a cause of action to indirect purchasers. See [City of Cookeville ex rel. Reg'l Med. Ctr. v. Humphrey, 126 S.W.3d 897, 902 \(Tenn. 2004\)](#) (providing that where the language of a statute is clear and unambiguous, we must apply the statute in accordance with its plain language). Contrary to the Court of Appeals' holding, [HN5](#) the plain language of [section 47-25-106](#) does not prohibit recovery to indirect purchasers who are non-residents of Tennessee. Moreover, [sections 47-25-101 and -102](#)<sup>1</sup> (2001) prohibit price fixing agreements that tend to affect the price to the "producer or consumer" of such products. These statutes reflect a clear intent to protect and afford a remedy to ultimate consumers.

[\*\*8] [HN8](#) This Court has identified two purposes of the TPPA. See [Baird v. Smith, 128 Tenn. 410, 161 S.W. 492, 493 \(Tenn. 1913\)](#). The first purpose is to preserve full and free competition in the sale of merchandise that "had become a part of the mass of property in the State." *Id.* The second purpose is to preserve full and free competition in the manufacture and sale of "articles of domestic growth and domestic raw material" and to prevent combinations tending to affect the price or cost of these articles to the producer or consumer. *Id.* We believe that permitting indirect purchasers to recover under the TPPA promotes these purposes.

The defendants contend that the language of [Tennessee Code Annotated section 47-25-106](#) permitting recovery of "the full consideration or sum paid by the person" for the products, "the sale of which is controlled by such combination or trust," [\*518] limits recovery to direct purchasers. According to the defendants, the only sale "controlled by" an antitrust violator is the transaction between the violator and the direct purchaser. We believe that their argument is flawed. First, [HN9](#) "control" means "power or authority [\*\*9] to manage, direct, superintend, restrict, regulate, govern, administer, or oversee" as well as "the ability to exercise a restraining or directing

<sup>1</sup> [Tennessee Code Annotated section 47-25-101](#) (2001) provides that

[HN6](#) All arrangements, contracts, agreements, trusts, or combinations between persons or corporations made with a view to lessen, or which tend to lessen, full and free competition in the importation or sale of articles imported into this state, or in the manufacture or sale of articles of domestic growth or of domestic raw material, and all arrangements, contracts, agreements, trusts, or combinations between persons or corporations designed, or which tend, to advance, reduce, or control the price or the cost to the producer or the consumer of any such product or article, are declared to be against public policy, unlawful, and void.

[Tennessee Code Annotated 47-25-102](#) prohibits agreements [HN7](#) "to sell and market . . . products and articles, manufactured in this state, or imported into this state, to any producer or consumer at prices reduced below the cost of production or importation into this state." The statute further prohibits "any other arrangements, contracts, or agreements, by and between its agents and subagents, which tend to lessen full and free competition in the sale of all such articles manufactured and imported into the state, and which amount to a subterfuge for the purpose of obtaining the same advantage and purposes."

influence over something." Black's Law Dictionary 329 (6th ed. 1990). A sale "controlled by" an antitrust violation includes not only a sale made by the violator to the direct purchaser but also a transaction between the direct purchaser and the consumer in which the price of the product purchased by the consumer is influenced by the antitrust violator's conduct.

Second, we believe that this language pertains not to persons who may recover but to the recovery itself.[HN10](#)<sup>1</sup>] A plain reading of [section 47-25-106](#) permits a person to recover the consideration or sum that was "controlled by" or influenced by the antitrust violator. In other words, an indirect purchaser may recover from the antitrust violator the amount of the overcharge that the direct purchaser passed on to the indirect purchaser.<sup>2</sup>

[\*\*10] Third, we conclude that the United States Supreme Court's holding in [Illinois Brick Co. v. Illinois](#), 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977), does not require a different result. In that case, the Supreme Court held that "the overcharged direct purchaser, and not others in the chain of manufacture or distribution, is the party 'injured in his business or property' within the meaning of [section 4 of the Clayton Act]."<sup>3</sup> [Illinois Brick Co.](#), 431 U.S. at 729. Thus, [HN11](#)<sup>4</sup>] indirect purchasers do not have a cause of action under federal [antitrust law](#) because they do not suffer a legally cognizable injury. See id. The Court in [Illinois Brick Co.](#) was concerned that permitting offensive use of the "pass-on" theory by indirect purchasers would create: 1) a risk of recovery of the entire overcharge by both the direct and indirect purchasers, resulting in multiple liability for the defendant; 2) difficulty in apportioning the responsibility for the overcharge among those in the chain of distribution; and 3) lack of incentive for direct purchasers to bring suit. [Id. at 737-38](#). The Court further reasoned that permitting indirect purchasers to [\*\*11] bring suit would result in highly complex litigation due to the necessity of determining the amount of the overcharge passed on to the indirect purchasers. [Id. at 732](#).

[HN13](#)<sup>5</sup>] The Supreme Court's holding in [Illinois Brick Co.](#), however, applies only to federal [antitrust law](#). Clearly, states may provide a remedy to indirect purchasers under their own antitrust laws. [California v. \[\\*519\] ARC Am. Corp.](#), 490 U.S. 93, 103, 104 L. Ed. 2d 86, 109 S. Ct. 1661 (1989).

In response to [Illinois Brick Co.](#), many states [\*\*12] amended their antitrust statutes to either provide indirect purchasers with a private right of action or permit the state's attorney general to bring an action as *parens patriae* on behalf of indirect purchasers.<sup>6</sup> The defendants identify various failed attempts by the Tennessee legislature to amend the TTPA to expressly permit indirect purchaser claims in support of its contention that the TTPA does not currently provide for such suits. [HN14](#)<sup>7</sup>] While legislative inaction is generally irrelevant to the interpretation of existing statutes, the legislature's failure to "express disapproval of a judicial construction of a statute is persuasive

<sup>2</sup> The defendants contend that permitting Freeman to recover the full consideration that it paid to the direct purchaser for the food products violates the constitutional principles of fairness and due process. Because we interpret [Tennessee Code Annotated section 47-25-106](#) as permitting Freeman to recover only the amount of the overcharge that the direct purchaser passed on to Freeman, we need not reach this issue.

<sup>3</sup> Section 4 of the Clayton Act, [15 U.S.C. § 15](#), provides:

[HN12](#)<sup>8</sup>] Any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws may sue therefor in any district court of the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

<sup>4</sup> See, e.g., [Ala. Code § 6-5-60](#) (2004); [Cal. Bus. & Prof. Code § 16750](#) (1987); [Colo. Rev. Stat. § 6-4-111](#) (1992); [D.C. Code Ann. § 28-4509](#) (1981); [Haw. Rev. Stat. §§ 480-3](#) (1987), [480-13](#) (2002), [480-14](#) (2003); [740 Ill. Comp. Stat. 10/7](#) (2003); [Kan. Stat. Ann. § 50-161](#) (2000); [Me. Rev. Stat. tit. 10, § 1104](#) (2004); [Mich. Comp. Laws § 445.778](#) (1985); [Minn. Stat. § 325D.57](#) (1984); [Miss. Code Ann. § 75-21-9](#) (2005); [Neb. Rev. Stat. § 59-821](#) (2002); [Nev. Rev. Stat. § 598A.210](#) (1999); [N.M. Stat. Ann. § 57-1-3](#) (1979); [N.Y. Gen. Bus. Law § 340](#) (1999); [N.D. Cent. Code § 51-08.1-08](#) (1991); [Or. Rev. Stat. § 646.775](#) (2001); [R.I. Gen. Laws § 6-36-12](#) (1979); [S.D. Codified Laws § 37-1-33](#) (1991); [Vt. Stat. Ann. tit. 9, § 2465](#) (1999); [Wis. Stat. § 133.18](#) (1987).

evidence of legislative adoption of the judicial construction." *Hamby v. McDaniel*, 559 S.W.2d 774, 776 (Tenn. 1977); see *Forman, Inc. v. Nat'l Council on Comp. Ins., Inc.*, 13 S.W.3d 365, 373 (Tenn. Ct. App. 1999).

[\*\*13] The present case, however, involves the Tennessee legislature's failure to amend a state statute in response to a federal court's interpretation of a federal statute. Furthermore, the United States Supreme Court has emphasized that its holding in *Illinois Brick Co.* applies only to federal **antitrust law**. *ARC Am. Corp.*, 490 U.S. at 103. This case is this Court's first opportunity to address the issue of whether indirect purchasers have a cause of action under the TPPA. Under these circumstances, it is

impossible to assert with any degree of assurance that [legislative] failure to act represents (1) approval of the status quo, as opposed to (2) inability to agree upon how to alter the status quo, (3) unawareness of the status quo, (4) indifference to the status quo, or even (5) political cowardice.

*Johnson v. Transp. Agency Santa Clara County, Cal.*, 480 U.S. 616, 672, 94 L. Ed. 2d 615, 107 S. Ct. 1442 (1987) (Scalia, J., dissenting). Therefore, we, like other jurisdictions, decline to presume that our state legislature considered *Illinois Brick Co.* as affecting the TPPA and thus requiring an amendment to the current statute.

Furthermore, [HN15](#) [↑] unlike [\*\*14] many states that have applied *Illinois Brick Co.* in disallowing indirect purchasers from bringing a private action under their antitrust laws, Tennessee does not have a statutory "harmony clause" mandating courts to interpret the TPPA consistently with federal law. Cf. *Stifflear v. Bristol-Myers Squibb Co.*, 931 P.2d 471, 476 (Colo. Ct. App. 1996); *Vacco v. Microsoft Corp.*, 260 Conn. 59, 793 A.2d 1048, 1056 (Conn. 2002); *Davidson v. Microsoft Corp.*, 143 Md. App. 43, 792 A.2d 336, 341 (Md. Ct. Spec. App. 2002); *Major v. Microsoft Corp.*, 2002 OK CIV APP 120, 60 P.3d 511, 513 (Okla. Ct. App. 2002); *Siena v. Microsoft Corp.*, 796 A.2d 461, 464 (R.I. 2002); *Abbott Labs., Inc. v. Segura*, 907 S.W.2d 503, 505, 38 Tex. Sup. Ct. J. 961 (Tex. 1995). [HN16](#) [↑] Thus, we join other jurisdictions in declining to interpret *Illinois Brick Co.* as precluding indirect purchasers from bringing suit under the TPPA. See *Bunkers Glass Co. v. Pilkington PLC*, 206 Ariz. 9, 75 P.3d 99, 107 (Ariz. [\[\\*520\]](#) 2003); *Comes v. Microsoft Corp.*, 646 N.W.2d 440, 445 (Iowa 2002); *Hyde v. Abbott Labs., Inc.*, 123 N.C. App. 572, 473 S.E. 2d 680, 686-87 (N.C. Ct. App. 1996); [\[\\*\\*15\]](#) *Arthur v. Microsoft Corp.*, 267 Neb. 586, 676 N.W.2d 29, 38 (Neb. 2004).

In addition, the concerns identified by the United States Supreme Court in *Illinois Brick Co.* do not justify prohibiting indirect purchaser suits under the TPPA. The Supreme Court expressed concerns regarding the possibility of multiple liability. *Illinois Brick Co.*, 431 U.S. at 730. The risk that an antitrust violator may be subject to both a direct purchaser suit and an indirect purchaser suit under the TPPA does exist. Our trial courts, however, are competent to handle such a problem. See *Bunkers Glass Co.*, 75 P.3d at 108; *Comes*, 646 N.W.2d at 449-50. In fact, many *Illinois Brick Co.* repealer statutes leave the solution of the risk of multiple liability to the trial courts. *Bunkers Glass Co.*, 75 P.3d at 108 (citing statutes from Illinois, New Mexico, and South Dakota).

The Supreme Court also expressed concern regarding the decreased incentive for direct purchasers to bring suit. *Illinois Brick Co.*, 431 U.S. at 745. The Court, however, recognized that direct purchasers likely will not bring suit due [\*\*16] to fear of retaliation by their suppliers. *Id. at 746*. Rather, the direct purchasers frequently pass on the overcharge to the indirect consumers who are the injured parties. *Id. at 764* (Brennan, J. dissenting); *Comes*, 646 N.W.2d at 450. The Supreme Court conceded that by allowing only direct purchaser actions, the person "actually injured," the indirect purchaser who ultimately paid the overcharge, is not afforded redress. *Illinois Brick Co.*, 431 U.S. at 746. Thus, the indirect purchasers, the real victims of the antitrust violations, have the true incentive to bring suit. [HN17](#) [↑] By construing *Tennessee Code Annotated section 47-25-106* (2001) as permitting indirect purchaser suits, we are affording a remedy to the ultimate victims of the antitrust conduct. Accepting the defendants' position would leave such victims of illegal activity with no redress, a result that hardly comports with notions of fair play.

Finally, the Supreme Court expressed concern regarding the risk of highly complex litigation due to the difficulty in apportioning damages. *Id. at 745-47*. [HN18](#) [↑] Antitrust, however, [\[\\*\\*17\]](#) is a complex area of law and generally involves highly complex litigation. See *Comes*, 646 N.W.2d at 451. We do not believe that the ends of justice should be defeated simply because the risk of complicated litigation exists. See *id.*

Accordingly, we conclude that [HN19](#)<sup>↑</sup> an indirect purchaser may bring an action under [Tennessee Code Annotated section 47-25-106](#) for conduct in violation of the TPPA even though the indirect purchaser is a non-resident of this state.

## 2. Scope of the TPPA

We must next determine whether the conduct complained of falls within the scope of the TPPA. [Tennessee Code Annotated section 47-25-101](#) (2001) provides that

all arrangements, contracts, agreements, trusts, or combinations between persons or corporations made with a view to lessen, or which tend to lessen, full and free competition in the importation or sale of articles imported into this state, or in the manufacture or sale of articles of domestic growth or of domestic raw material, and all arrangements, contracts, agreements, trusts, or combinations between persons or corporations designed, or which tend, to advance, [\[\\*\\*18\]](#) reduce, or control the price or the cost to [\[\\*521\]](#) the producer or the consumer of any such product or article, are declared to be against public policy, unlawful, and void.

This Court last addressed the reach of the TPPA in [Standard Oil Co. v. State, 117 Tenn. 618, 100 S.W. 705, 709 \(1907\)](#), in which we held that this state's antitrust statutes did not apply to interstate commerce "when properly construed" and that the statute's purpose was to "correct and prohibit abuses of trade within the state." At the time of this holding, a theory of dual sovereignty presuming mutually exclusive jurisdiction for state and federal regulation prevailed. See [Abbott Labs. v. Durrett, 746 So. 2d 316, 330-34 \(Ala. 1999\)](#) (discussing the theory of dual sovereignty).

In [Standard Oil Co.](#), this Court reasoned that the state legislature knew it did not have the power to enact laws that regulated interstate commerce and thus did not intend to enact unconstitutional law. [100 S.W. at 710](#). We further reasoned that the state legislature intended to correct and punish the wrongs to trade that were being perpetrated against commerce within the state, which the Sherman [\[\\*\\*19\]](#) Antitrust Act could not reach and for which no efficient remedy was available. *Id.* Thus, [HN20](#)<sup>↑</sup> we concluded that "the Legislature clearly intended to prohibit trusts, combinations, and agreements affecting all commerce not covered by the federal statute, and upon which it had a right to legislate. It did not intend to stop short of its power or to exceed it." [Id. at 711](#).

The language of Tennessee's antitrust statutes have not changed significantly since [Standard Oil Co. Compare Standard Oil Co., 100 S.W. at 707, with Tenn. Code Ann. § 47-25-101](#) (2001). In [Standard Oil Co.](#), however, this Court did not rely upon the plain language of this state's antitrust statutes in determining its scope. Rather, our holding was based upon two principles of statutory construction. First, [HN21](#)<sup>↑</sup> courts have a duty to construe statutes in such a manner as to avoid conflict with the United States Constitution if the construction can be accomplished without disregarding the legislature's intent. [Standard Oil Co., 100 S.W. at 710](#). Second, [HN22](#)<sup>↑</sup> although a statute includes terms that are overly broad, courts have a duty to limit a [\[\\*\\*20\]](#) statute's application to circumstances within the legislature's intent. [Id. at 711](#). We based our holding upon the state legislature's constitutionally permitted scope of authority in the areas of [antitrust law](#) and interstate commerce that prevailed at that time as well as upon our duty to construe a statute so as to avoid any unconstitutionality.

The dual sovereignty theory presuming mutually exclusive jurisdiction for state antitrust laws and federal antitrust laws has since been rejected. [HN23](#)<sup>↑</sup> The United States Supreme Court now considers state antitrust regulations to supplement and complement the federal antitrust laws and the enforcement of these state laws to be consistent with the federal antitrust laws. See [ARC Am. Corp., 490 U.S. at 101-02](#). Furthermore, a state generally is not prohibited from giving effect to its antitrust laws merely because the regulation affects interstate commerce. See [Standard Oil Co. v. Tenn., 217 U.S. 413, 54 L. Ed. 817, 30 S. Ct. 543 \(1910\)](#). Specifically, [HN24](#)<sup>↑</sup> a state antitrust regulation that has only incidental effects on interstate commerce and is regulated evenhandedly to effectuate a legitimate local interest does not [\[\\*\\*21\]](#) run afoul of the Commerce Clause unless the burden imposed on interstate commerce is clearly excessive when compared to the punitive local benefits. See [Pike v. Bruce Church, Inc., 397 U.S. 137, 142, 25 L. Ed. 2d 174, 90 S. Ct. 844 \(1970\)](#).

[\*522] [HN25](#) In construing statutes, we must ascertain and give effect to the legislature's intent and purpose. See [Lipscomb v. Doe, 32 S.W.3d 840, 844 \(Tenn. 2000\)](#). Furthermore, we must construe a statute so as to avoid a constitutional conflict if any reasonable construction exists that satisfies the Constitution's requirements. [Davis-Kidd Booksellers, Inc. v. McWherter, 866 S.W.2d 520, 529 \(Tenn. 1993\)](#). Thus, in construing the reach of the TTPA, we must develop a standard that is consistent with the legislature's intent and purpose without offending constitutional provisions.

[HN26](#) The TTPA prohibits agreements adversely affecting competition in the "sale of articles imported into this state" or influencing the "price or the cost to the producer or the consumer of any such product or article." [Tenn. Code Ann. § 47-25-101](#) (2001). According to its plain language, the TTPA prohibits arrangements that [\*\*22] decrease competition or affect the prices of goods even if those goods arrived in Tennessee through interstate commerce. The act does not contain any language indicating that the legislature intended that the scope of the act be limited to intrastate commerce. Had the legislature intended such a limitation, the legislature simply could have included the limitation in the act.

In developing a standard for determining the application of the TTPA to a particular set of circumstances, we must determine whether the focus should be upon the anticompetitive conduct of the defendant or the effects of the anticompetitive conduct. In examining whether the circumstances of a particular case fall within the TTPA, the Court of Appeals has employed a conduct-based test focusing upon the character of the defendant's anticompetitive conduct giving rise to the dispute. See [Lynch Display Corp. v. Nat'l Souvenir Ctr., Inc., 640 S.W.2d 837, 840 \(Tenn. Ct. App. 1982\)](#) (holding that a lease between a Tennessee corporation and a Maryland corporation and an associated franchise agreement between a Tennessee corporation and a District of Columbia corporation were "predominantly interstate [\*\*23] in character" and "only incidentally affected intrastate commerce"). Any test focusing upon the anticompetitive conduct giving rise to the dispute, however, would be difficult to apply when the plaintiff is an indirect purchaser who did not transact directly with the defendant.

Furthermore, [HN27](#) the purpose of the TTPA is to protect the state's trade or commerce affected by the anticompetitive conduct. See [State ex rel. Astor v. Schlitz Brewing Co., 104 Tenn. 715, 59 S.W. 1033, 1039 \(Tenn. 1900\)](#) ("The thing condemned and punished by the Act is injury to trade. The thing intended to be protected is trade. . . ."). Thus, we reject any standard that requires examination of the anticompetitive conduct in determining whether a particular case falls within the scope of the TTPA. Rather, the effect of the anticompetitive conduct on Tennessee trade or commerce is determinative of whether the TTPA is applicable under the circumstances.

We must now determine the standard to employ in examining whether the effects of the anticompetitive conduct on Tennessee trade or commerce fall within the scope of the TTPA. One possible standard is a "predominant effects" standard. The term [\*\*24] "predominant" is defined as "something greater or superior in power and influence to others with which it is connected or compared." Black's Law Dictionary 1177 (6th ed. 1990). Thus, [HN28](#) anticompetitive conduct cannot predominantly affect both intrastate commerce and interstate commerce. Under a "predominant effects" standard, courts would be required to [\*523] weigh the effects of anticompetitive conduct on Tennessee commerce against its effects on interstate commerce and determine which effects are greater. If the effects on interstate commerce are greater than the effects on Tennessee commerce, the TTPA would not apply.

In construing the TTPA, other jurisdictions have utilized a "predominant" standard in applying a conduct-based test. See e.g., [In re Terazosin Hydrochloride Antitrust Litig., 160 F. Supp. 2d 1365, 1378 \(S.D. Fla. 2001\)](#); [FTC v. Mylan Labs., Inc., 99 F. Supp. 2d 1, 4 \(D.C. Cir. 1999\)](#). In our modern society, however, interstate and international transactions have become more common. Numerous technological advances, including the internet, enable consumers and businesses from opposite areas of the country to engage in transactions with ease. [\*\*25] See generally, John Rothchild, Protecting the Digital Consumer: The Limits of Cyberspace Utopianism, [74 Ind. L.J. 893 \(1999\)](#) (discussing the increase in business-to-consumer online commerce). Adoption of a predominant effects standard would render the TTPA obsolete except in those rare circumstances in which the effects on intrastate commerce are greater than the effects on interstate commerce. We do not believe that this standard is sufficient to advance the TTPA's purpose of protecting Tennessee trade and commerce.

We conclude that [HN29](#)[<sup>↑</sup>] the proper standard for determining whether a case falls within the scope of the TTPA is a "substantial effects" standard. Pursuant to this standard, courts must decide whether the alleged anticompetitive conduct affects Tennessee trade or commerce to a substantial degree. Federal courts have applied the substantial effects standard to the [Sherman Antitrust Act](#). See [Hartford Fire Ins. Co. v. California, 509 U.S. 764, 796, 125 L. Ed. 2d 612, 113 S. Ct. 2891 \(1993\)](#) (concluding that "the Sherman Act applies to foreign conduct that was meant to produce and did in fact produce some substantial effect in the United States"); [McLain v. Real Estate Bd. of New Orleans, Inc., 444 U.S. 232, 242, 62 L. Ed. 2d 441, 100 S. Ct. 502 \(1980\)](#) [\*\*26] (holding that "to establish the jurisdictional element of a Sherman Act violation it would be sufficient for petitioners to demonstrate a substantial effect on interstate commerce" generated by activity that is primarily local in nature). Other states also apply a form of substantial effects standard in determining whether an action falls within their antitrust statute. See e.g., [Amarel v. Connell, 202 Cal. App. 3d 137, 248 Cal.Rptr. 276, 284 \(Cal. Ct. App. 1988\)](#) (holding that a cause of action under California's [antitrust law](#) is not precluded so long as the anticompetitive conduct had a "direct, substantial and reasonably foreseeable effect within the state"); [Olstad v. Microsoft Corp., 2005 WI 121, 700 N.W.2d 139 \(Wis. 2005\)](#) (concluding that Wisconsin's antitrust statute applies if the actionable conduct "substantially affects' the people of Wisconsin and has impacts in [the] state, even if the illegal activity resulting in those impacts occurred predominantly or exclusively outside [the] state"). We believe that [HN30](#)[<sup>↑</sup>] a "substantial effects" standard furthers the TTPA's goal of protecting Tennessee commerce without offending constitutional provisions.

[\*\*27] [HN31](#)[<sup>↑</sup>] The determination of whether an effect is substantial does not involve "mathematical nicety." [Anesthesia Advantage, Inc. v. Metz Group, 912 F.2d 397, 401 \(10th Cir. 1990\)](#). Rather, the test is pragmatic, turning upon the particular facts of the case. See *id.* at 402; [Huelsman v. Civic Ctr. Corp., 873 F.2d 1171, 1175 \(8th Cir. 1989\)](#). The anticompetitive conduct, however, need not threaten the demise of Tennessee businesses or affect market prices to substantially affect intrastate [\*524] commerce. See [Hosp. Bldg. Co. v. Trs. of Rex Hosp., 425 U.S. 738, 745-47, 48 L. Ed. 2d 338, 96 S. Ct. 1848 \(1976\)](#) (referring to the Sherman Antitrust Act).

In the present case, Freeman alleges that Eastman engaged in conduct from its principal place of business in Kingsport, Tennessee, including: 1) communicating with its co-defendants through in-person meetings, telephone calls, letters, and email resulting in an agreement to fix the prices of sorbates; 2) implementing the agreement by drafting price schedules and letters to third parties, adjusting prices and production volumes of sorbates, and taking orders and implementing sales to customers at the new [\*\*28] prices; and 3) attempting to conceal its conduct by limiting the number of its employees having knowledge of the agreement. These allegations primarily relate to the defendants' actions in conspiring and implementing the conspiracy to fix the prices of sorbates.

The focus under the substantial effects standard, however, is not on the anticompetitive conduct itself but on the effects of the conduct on Tennessee commerce. While Freeman alleged that Eastman took orders and implemented sales to customers at the new prices from Tennessee, we do not believe that this bare allegation without more is sufficient to establish that Tennessee commerce was substantially affected. Furthermore, Freeman fails to establish how the defendants' anticompetitive conduct affected Tennessee commerce to a substantial degree even though the conduct resulted in Freeman paying higher prices to retailers for items containing sorbates. To the contrary, there is no indication that the items that Freeman purchased contained sorbates manufactured by Eastman, the lone defendant with ties to Tennessee. Therefore, we conclude that Freeman's claim does not fall within the scope of the [TTPA](#) and that the trial court [\*\*29] properly granted the defendants' motion to dismiss Freeman's claim.

## B. Unjust Enrichment

We must next determine whether the trial court erred in denying the defendants' motion for summary judgment regarding Freeman's claim of unjust enrichment. [HN32](#)[<sup>↑</sup>] Summary judgment is appropriate only when the moving party demonstrates that no genuine issues of material fact exist and that the moving party is entitled to judgment as a matter of law. See [Tenn. R. Civ. P. 56.04](#); [Penley v. Honda Motor Co., 31 S.W.3d 181, 183 \(Tenn. 2000\)](#). [HN33](#)[<sup>↑</sup>] Its purpose "is to resolve controlling issues of law rather than to find facts or resolve disputed factual issues." [XJ](#)

Props., Inc. v. Racetrac Petroleum, Inc., 151 S.W.3d 443, 446 (Tenn. 2004) (citation omitted). Thus, HN34[<sup>1</sup>] we must review a trial court's decision to grant or deny summary judgment de novo with no presumption of correctness attached to the trial court's conclusions. See Mooney v. Sneed, 30 S.W.3d 304, 306 (Tenn. 2000). We must also view the evidence in the light most favorable to the non-moving party, drawing all reasonable inferences in the non-moving party's favor. Staples v. CBL & Assocs., Inc., 15 S.W.3d 83, 89 (Tenn. 2000). [\*\*30]

HN35[<sup>1</sup>] We have previously recognized two types of implied contracts: contracts implied in fact and contracts implied in law. See Paschall's, Inc. v. Dozier, 219 Tenn. 45, 407 S.W.2d 150, 153-54 (Tenn. 1966). Contracts implied in fact arise under circumstances establishing the parties' mutual intention to contract. Id. at 154 (citation omitted). Contracts implied in law or quasi contracts are created by law without the parties' assent and are based upon reason and justice. Id. (citation omitted); Angus v. City of Jackson, 968 S.W.2d 804, 808 (Tenn. Ct. App. 1997). Courts may impose a contract implied in law where no [\*525] contract exists under various quasi contractual theories, including unjust enrichment. Whitehaven Cnty. Baptist Church v. Holloway, 973 S.W.2d 592, 596 (Tenn. 1998).

HN36[<sup>1</sup>] The elements of an unjust enrichment claim are: 1) "[a] benefit conferred upon the defendant by the plaintiff"; 2) "appreciation by the defendant of such benefit"; and 3) "acceptance of such benefit under such circumstances that it would be inequitable for him to retain the benefit without payment of the value thereof." Paschall's, Inc., 407 S.W.2d at 155. [\*\*31] The most significant requirement of an unjust enrichment claim is that the benefit to the defendant be unjust. Id.; Whitehaven Cnty. Baptist Church, 973 S.W.2d at 596. The plaintiff must further demonstrate that he or she has exhausted all remedies against the person with whom the plaintiff enjoyed privity of contract. Paschall's, Inc., 407 S.W.2d at 155; Whitehaven Cnty. Baptist Church, 973 S.W.2d at 596.

HN37[<sup>1</sup>] A plaintiff need not be in privity with a defendant to recover under a claim of unjust enrichment. See Paschall's, Inc., 407 S.W.2d at 154. Thus, Freeman may bring a cause of action for unjust enrichment against the defendants even though Freeman did not purchase the items containing sorbates directly from the defendants. The defendants, however, contend that Freeman must establish that it conferred a direct benefit, rather than an indirect or incidental benefit, upon the defendants. HN38[<sup>1</sup>] A benefit is any form of advantage that has a measurable value including the advantage of being saved from an expense or loss. Lawrence Warehouse Co. v. Twohig, 224 F.2d 493, 498 (8th Cir. 1955). The underlying [\*\*32] principle of the doctrine of unjust enrichment is that a party who receives a benefit that he or she desires, under circumstances rendering retention of the benefit without providing compensation inequitable, must compensate the provider of the benefit. Paschall's, Inc., 407 S.W.2d at 154. In accordance with this underlying principle, we conclude that HN39[<sup>1</sup>] to recover for unjust enrichment, a plaintiff need not establish that the defendant received a direct benefit from the plaintiff. Rather, a plaintiff may recover for unjust enrichment against a defendant who receives any benefit from the plaintiff if the defendant's retention of the benefit would be unjust. Our conclusion is consistent with other jurisdictions that have also concluded that the benefit received by a defendant need not be direct to establish an unjust enrichment claim. See, e.g., Hirsch v. Bank of Am., 107 Cal. App. 4th 708, 132 Cal.Rptr.2d 220, 229 (Cal. App. 2003) (holding that to confer a benefit, the plaintiff need not pay the money directly to the defendant); HPI Health Care Servs., Inc. v. Mt. Vernon Hosp., Inc., 131 Ill. 2d 145, 545 N.E.2d 672, 679, 137 Ill. Dec. 19 (Ill. 1989) [\*\*33] (permitting recovery of a benefit transferred to the defendant by a third party where the third party mistakenly gave the benefit to the defendant instead of the plaintiff, where the defendant procured the benefit from the third party through wrongful conduct, or where the plaintiff's claim to the benefit is superior to the defendant's claim); State v. ex rel. Palmer v. Unisys Corp., 637 N.W.2d 142, 155 (Iowa 2001) (concluding that "benefits can be direct or indirect, and can involve benefits conferred by third parties").

The defendants further contend that Freeman failed to establish that it exhausted its remedies against the supermarket from which it purchased the food products that contained sorbates. The defendants submitted various affidavits to demonstrate that Freeman had not sought to recover from the supermarket. We conclude that through these affidavits, the [\*526] defendants have negated the exhaustion of remedies element of Freeman's unjust enrichment claim. Thus, the burden shifts to Freeman to provide specific facts establishing the existence of disputed issues of material fact that must be resolved by the trier of fact. See Blair v. West Town Mall, 130 S.W.3d 761, 767 (Tenn. 2004). [\*\*34]

In response, Freeman submitted an affidavit from its counsel maintaining that he was unaware of any viable claims against the supermarket. Freeman essentially contends that pursuit of any causes of action against the supermarket would have been futile. Although our courts have not addressed the issue of futility with regard to the exhaustion of remedies element of an unjust enrichment claim, our courts have recognized this exception in other causes of action with an exhaustion of remedies requirement. See e.g., Wilson v. Miller, 194 Tenn. 390, 250 S.W.2d 575, 578 (Tenn. 1952) (action by a union member to recover union funds pursuant to a union agreement); Cantrell v. Walker Die Casting, Inc., 121 S.W.3d 391, 396 n.3 (Tenn. Ct. App. 2003) (ERISA action). Likewise, we conclude that HN40[<sup>↑</sup>] to maintain an action for unjust enrichment, a plaintiff is not required to exhaust all remedies against the party with whom the plaintiff is in privity if the pursuit of the remedies would be futile. We do not believe, however, that a bare allegation that any attempt to exhaust its remedies against the supermarket would be futile without providing a factual basis to [\*\*35] support the allegation is sufficient to establish a disputed issue of material fact as to the exhaustion-of-remedies element of Freeman's unjust enrichment claim against the defendants. Thus, the trial court erred in denying the defendants' motion for summary judgment.

## CONCLUSION

We conclude that although Freeman may bring a claim against the defendants under the TTPA as an indirect purchaser, the conduct of which Freeman complains does not fall within the scope of the act because Tennessee commerce was not substantially affected by the conduct. As to the unjust enrichment claim, we hold that Freeman was not required to establish that the defendants directly benefitted from the transaction between Freeman and the supermarket. We further hold, however, that the trial court erred in declining to grant the defendants' motion for summary judgment as to the unjust enrichment claim due to Freeman's failure to provide a factual basis to support its allegation that any attempt to exhaust its remedies against the supermarket would have been futile. Accordingly, we affirm the judgment of the Court of Appeals in part and reverse in part, and we remand the case to the trial court for further [\*\*36] proceedings consistent with this opinion.

The costs of appeal are taxed to the appellant, Freeman Industries, and its sureties, for which execution may issue if necessary.

JANICE M. HOLDER, JUSTICE



## [Hydril Co., L.P. v. Grant Prideco, L.P.](#)

United States District Court for the Southern District of Texas, Houston Division

August 25, 2005, Decided

CIVIL ACTION NO. H-05-0337

### **Reporter**

385 F. Supp. 2d 609 \*; 2005 U.S. Dist. LEXIS 18647 \*\*

HYDRIL COMPANY, L.P., et al., Plaintiffs, v. GRANT PRIDECO, L.P., et al., Defendants.

**Subsequent History:** Reversed by, in part, Vacated by, in part, Remanded by [Hydril Co. LP v. Grant Prideco LP, 2007 U.S. App. LEXIS 1621 \(Fed. Cir., Jan. 25, 2007\)](#)

**Prior History:** [Hydril Co., L.P. v. Grant Prideco, L.P., 2005 U.S. Dist. LEXIS 18646 \(S.D. Tex., July 26, 2005\)](#)

## **Core Terms**

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Patent, motion to dismiss, alleges, apprehension, drill, breach of contract claim, antitrust, pipe, patent infringement, antitrust claim, infringement

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN1 [] Motions to Dismiss, Failure to State Claim**

A district court may dismiss a complaint under [Fed. R. Civ. P. 12\(b\)\(6\)](#) if it appears beyond doubt that a plaintiff can prove no set of facts consistent with his factual allegations which would entitle him to the requested relief. Thus, a court must determine whether the complaint states any valid claim for relief in the light most favorable to the plaintiff and with every doubt resolved in the plaintiff's behalf. The complaint must be liberally construed in favor of the plaintiff, and all facts pleaded in the complaint must be taken as true. However, the plaintiff must plead specific facts, not mere conclusory allegations, in order to avoid dismissal for failure to state a claim. Statements that merely create a suspicion that the plaintiff may have a right of action do not foreclose a motion to dismiss.

Civil Procedure > Pleading & Practice > Motion Practice > Content & Form

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

## [\*\*HN2\*\*](#) Motion Practice, Content & Form

In considering a motion to dismiss for failure to state a claim, a district court must limit itself to the contents of the pleadings, including attachments thereto. Documents attached to a motion to dismiss are considered part of the pleadings if they are referred to in the complaint and are central to the claim.

Civil Procedure > Judgments > Enforcement & Execution > General Overview

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > Declaratory Judgments

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > General Overview

Civil Procedure > ... > Declaratory Judgments > Federal Declaratory Judgments > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Patent Law > Remedies > Declaratory Judgments

## [\*\*HN3\*\*](#) Judgments, Enforcement & Execution

The United States Court of Appeals for the Federal Circuit has clearly held that as a matter of Federal Circuit antitrust law, the standards for determining jurisdiction in a declaratory judgment action of patent invalidity also define the minimum level of enforcement necessary to expose the patentee to a Walker Process claim for attempted monopolization. The test for determining jurisdiction in a declaratory judgment action challenging patent validity requires both (1) an explicit threat or other action by the patentee which creates a reasonable apprehension on the part of the plaintiff that it will face an infringement suit, and (2) present activity which could constitute infringement or concrete steps taken with the intent to conduct such activity. The first prong looks to the patent holder's conduct, and the second prong looks to the potential infringer's conduct. The reasonable apprehension of suit test requires more than the nervous state of mind of a possible infringer; it requires that the objective circumstances support such an apprehension.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

## [\*\*HN4\*\*](#) Inequitable Conduct, Anticompetitive Conduct

Because a Walker Process claim is aimed at removing patent law immunity from antitrust claims, the level of enforcement required for a Walker Process claim is an issue associated with patent law and Federal Circuit law rather than Fifth Circuit law. Fifth Circuit law governs whether a patent holder has taken adequate steps to enforce the patent. Which actions can cause a patentee to lose the general protection of the patent law and to risk liability for antitrust damages is clearly an issue unique to the patent law -- and therefore inappropriate for resolution under the potentially varying interpretations of the regional circuits.

Civil Procedure > ... > Subject Matter Jurisdiction > Supplemental Jurisdiction > Pendent Claims

Civil Procedure > ... > Subject Matter Jurisdiction > Supplemental Jurisdiction > General Overview

## [\*\*HN5\*\*](#) Supplemental Jurisdiction, Pendent Claims

If the federal claims are dismissed before trial, the state claims should be dismissed as well.

**Counsel:** **[\*\*1]** For Hydril Company LP, Plaintiff: Mitchell D Lukin, Michael Hawes, Baker & Botts, Houston, TX; David Michael Rodi, Baker Botts LLP, Houston, TX.

For Hydril U.K., Ltd., Plaintiff: David Michael Rodi, Baker Botts LLP, Houston, TX; Michael Hawes, Baker Botts, Houston, TX.

For Grant Pridaco LP, Grant Pridaco Inc, Defendants: Gerard G Pecht, Peter Andrew Stokes, Fulbright and Jaworski, Houston, TX; Daniel James Pirolo, Fulbright and Jaworski LLP, Houston, TX.

**Judges:** Nancy F. Atlas, United States District Judge.

**Opinion by:** Nancy F. Atlas

## **Opinion**

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### **[\*609] MEMORANDUM AND ORDER**

This case is before the Court on the Motion to Dismiss Plaintiffs' Second Amended Complaint ("Motion to Dismiss") [Doc. # 38] filed by Defendants Grant Pridaco, L.P. and Grant Pridaco, Inc. (collectively "Grant Pridaco"). Plaintiffs Hydril Company L.P. and Hydril U.K., Ltd. ("Hydril") filed their Response [Doc. # 44] and **[\*610]** Grant Pridaco filed a Reply [Doc. # 45]. Based on the Court's review of the full record and the application of governing legal authorities, the Court concludes that the Motion to Dismiss should be **granted**.

#### **I. FACTUAL AND PROCEDURAL BACKGROUND**

The factual background of this **[\*\*2]** case was set forth fully in the Court's Memorandum and Order entered June 22, 2005 ("June 22 Order"), and will not be repeated here. Briefly, Hydril manufactures and sells connections used to join segments of drill pipe in the drilling of oil and gas wells. Hydril U.K., Ltd., has sold finished drill pipe on one occasion. Grant Pridaco manufactures and sells both drill pipe and connections.

Grant Pridaco is the owner of United States Patent 6,244,631 ("the 631 Patent), which has been surrendered as part of a reissue proceeding beginning June 6, 2003. Hydril alleges that Grant Pridaco obtained the 631 Patent through fraud and, therefore, its assertion of rights under that patent constitutes a violation of the antitrust laws as recognized in [Walker Process Equipment, Inc. v. Food Machinery & Chem. Corp., 382 U.S. 172, 15 L. Ed. 2d 247, 86 S. Ct. 347 \(1965\)](#) (referred to herein as a "Walker Process" claim).

Hydril in this lawsuit asserted a breach of contract claim, a patent infringement claim involving a different patent, and the *Walker Process* claim. In the June 22 Order, the patent infringement claim was dismissed and Hydril was permitted to amend its *Walker Process* claim. Hydril filed **[\*\*3]** its Second Amended Complaint, adding Hydril U.K., Ltd. as a Plaintiff. Defendants then moved to dismiss the *Walker Process* antitrust claim for a variety of reasons. Specifically, Defendants argue that Plaintiffs have failed to allege facts establishing that they have standing to assert the antitrust claim because they have not alleged an injury-in-fact, antitrust injury, or that Hydril is a proper antitrust Plaintiff. Defendants also argue that Hydril has failed to allege a viable *Walker Process* claim because they have not alleged facts to show that Grant Pridaco engaged in the required level of activity to enforce the 631 Patent. Defendants also asked the Court to decline to exercise supplemental jurisdiction over the pending breach of contract claim. The Motion to Dismiss has been fully briefed and it is now ripe for decision.

#### **II. ANALYSIS**

##### **A. Standard for Motion to Dismiss**

**HN1**[] A district court may dismiss a complaint under [Rule 12\(b\)\(6\)](#) if it appears beyond doubt that the plaintiff can prove no set of facts consistent with his factual allegations which would entitle him to the requested relief. [\*Manguno v. Prudential Property and Cas. Ins. Co.\*, 276 F.3d 720, 725 \(5th Cir. 2002\)](#). [\*\*4] Thus, the Court must determine whether the complaint states any valid claim for relief in the light most favorable to the plaintiff and with every doubt resolved in the plaintiff's behalf. [\*Collins v. Morgan Stanley Dean Witter\*, 224 F.3d 496, 498 \(5th Cir. 2000\)](#). The complaint must be liberally construed in favor of the plaintiff, and all facts pleaded in the complaint must be taken as true. [\*Manguno\*, 276 F.3d at 725](#). However, the plaintiff must plead specific facts, not mere conclusory allegations, in order to avoid dismissal for failure to state a claim. [\*Jones v. Alcoa\*, 339 F.3d 359, 362 \(5th Cir. 2003\)](#), cert. denied, 540 U.S. 1161, 157 L. Ed. 2d 1206, 124 S. Ct. 1173 (2004). Statements that merely create a suspicion that the plaintiff may have a right of action do not foreclose a motion to dismiss. [\*Campbell v. City of San Antonio\*, 43 F.3d 973, 975 \(5th Cir. 1995\)](#).

**HN2**[] "In considering a motion to dismiss for failure to state a claim, a district court [\*611] must limit itself to the contents of the pleadings, including attachments thereto." [\*Collins\*, 224 F.3d at 498](#). Documents "attached to a motion to dismiss are considered part [\*\*5] of the pleadings if they are referred to in the complaint and are central to the claim." [\*Id. at 498-99\*](#).

## B. "Enforcement" Requirement for a Walker Process Claim

Grant Pridaco argues that Hydril's *Walker Process* claim should be dismissed because, *inter alia*, Hydril has not alleged the required level of activity by Grant Pridaco to enforce the 631 Patent. **HN3**[] The Federal Circuit has clearly held that "as a matter of Federal Circuit antitrust law, the standards . . . for determining jurisdiction in a Declaratory Judgment Action of patent invalidity also define the minimum level of enforcement' necessary to expose the patentee to a *Walker Process* claim for attempted monopolization."<sup>1</sup> [\*Unitherm Food Systems, Inc. v. Swift-Eckrich, Inc.\*, 375 F.3d 1341, 1358 \(Fed. Cir. 2004\)](#), cert. denied, 161 L. Ed. 2d 190, 125 S. Ct. 1399 (2005). The test for determining jurisdiction in a Declaratory Judgment Action challenging patent validity requires both (1) an explicit threat or other action by the patentee which creates a reasonable apprehension on the part of the plaintiff that it will face an infringement suit, and (2) present activity which could [\*66] constitute infringement or concrete steps taken with the intent to conduct such activity. [\*Sierra Applied Sciences, Inc. v. Advanced Energy Industries, Inc.\*, 363 F.3d 1361, 1373 \(Fed. Cir. 2004\)](#) (citing [\*BP Chem. Ltd. v. Union Carbide Corp.\*, 4 F.3d 975, 978 \(Fed. Cir. 1993\)](#)). "The first prong looks to the patentholder's conduct, and the second prong looks to the potential infringer's conduct." *Id.* "The reasonable apprehension of suit' test requires more than the nervous state of mind of a possible infringer; it requires that the objective circumstances support such an apprehension." [\*Phillips Plastics Corp. v. Kato Hatsujou Kabushiki Kaisha\*, 57 F.3d 1051, 1053-54 \(Fed. Cir. 1995\)](#).

[\*\*7] In this case, Hydril alleges that Grant Pridaco "has widely publicized the existence of the 631 Patent to the industry in general." Second Amended Complaint, P 48. Hydril also alleges that Grant Pridaco's attorney wrote a letter to OMSCO, a drill pipe distributor, asserting that certain orders from OMSCO's customers may violate the 631 Patent.<sup>2</sup> *Id.* Hydril also alleges "on information and belief that Grant Pridaco sent similar letters to "others in the pipe and drilling industries." *Id.*

<sup>1</sup>

**HN4**[] Because a *Walker Process* claim is aimed at removing patent law immunity from antitrust claims, the level of enforcement required for a *Walker Process* claim is an issue associated with patent law and Federal Circuit law rather than Fifth Circuit law governs whether a patentholder has taken adequate steps to enforce the patent. See [\*Unitherm Food Sys. v. Swift-Eckrich, Inc.\*, 375 F.3d 1341, 1357 \(Fed. Cir. 2004\)](#) ("which actions can cause a patentee . . . to lose the general protection of the patent law and to risk liability for [antitrust] damages is clearly an issue unique to the patent law -- and therefore inappropriate for resolution under the potentially varying interpretations of the regional circuits").

<sup>2</sup>

Neither Hydril Company L.P. nor Hydril U.K., Ltd., alleges enforcement activity by Grant Pridco which would create an objectively reasonable apprehension that Grant Pridco might sue Hydril for [\*612] patent infringement. Initially, there is no [\*\*8] allegation in the Second Amended Complaint that Grant Pridco has accused Hydril of infringing the 631 Patent. The general advertisements mentioning Grant Pridco's patent do not create a reasonable apprehension that Grant Pridco would sue Hydril. Similarly, the January 2003 letter to OMSCO does not contain an explicit threat or other language which, under the totality of the circumstances, could create a reasonable apprehension on Hydril's part that Grant Pridco might sue it for patent infringement. There is no allegation that any similar letters sent by Grant Pridco or its counsel to others in the pipe and drilling industry were more explicit or otherwise indicated Grant Pridco's intention to enforce the 631 Patent against Hydril or others. Additionally, there is no allegation that Grant Pridco engaged in any further activity to follow up on the January 2003 letter to OMSCO, or on any other similar letters to others.

Because Hydril has failed to allege enforcement activity by Grant Pridco which would create an objectively reasonable apprehension that Grant Pridco intended to enforce the 631 Patent against Hydril, Plaintiffs have failed to allege the minimum level of enforcement [\*\*9] necessary to state a *Walker Process* claim against Grant Pridco.

Hydril has been given two opportunities to amend its Complaint, most recently after Defendants' explicit arguments that Hydril's antitrust claim failed for various enumerated reasons. Hydril has had ample time to investigate its *Walker Process* claim, yet has failed to allege legally sufficient facts. The Court concludes Hydril cannot state a claim upon which relief can be granted on the [\*Walker Process\*](#) claim, and that claim is dismissed.

### **C. Contract Claim**

Hydril alleges that Grant Pridco breached a Merger Agreement entered into between the parties in 1997, pursuant to which the parties also entered into a licensing agreement referred to as the "Wedge Agreement." The Court has only supplemental jurisdiction over this state law breach of contract claim.

The case is in its very early stages. Indeed, the Court has not yet entered a docket control order and discovery except as to Plaintiffs' antitrust standing and antitrust injury has been stayed. Because the federal claims have been dismissed at such an early stage of the proceedings, under [28 U.S.C. § 1337\(c\)\(3\)](#), the Court [\*\*10] declines to exercise supplemental jurisdiction over Plaintiffs' pendent state law claim for breach of contract. See [\*Moore v. Willis Independent School Dist.\*, 233 F.3d 871, 876 \(5th Cir. 2000\)](#); [\*Robertson v. Neuromedical Center\*, 161 F.3d 292, 296 \(5th Cir. 1998\)](#), cert. denied, 526 U.S. 1098, 143 L. Ed. 2d 671, 119 S. Ct. 1575 (1999) ("Certainly, [HN5](#) if the federal claims are dismissed before trial, . . . the state claims should be dismissed as well.").

### **III. CONCLUSION AND ORDER**

Based on the foregoing, the Court concludes that Hydril has failed to allege the minimum level of patent enforcement activity necessary to support its *Walker Process* claim. The patent infringement claim was previously dismissed, and the Court declines to exercise supplemental jurisdiction over the state law breach of contract claim. Accordingly, it is hereby

**ORDERED** that Defendants' Motion to Dismiss [Doc. # 38] is **GRANTED**. Hydril's *Walker Process* antitrust claim is **DISMISSED with prejudice**. It is further

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The letter, attached as Exhibit 9 to the Second Amended Complaint, states that Grant Pridco believes the 631 Patent "maybe relevant to" pending orders for certain drill pipe and does not mention Hydril. See Letter to OMSCO, Exh. 9 to Second Amended Complaint.

[\*613] ORDERED that the breach of contract claim is **DISMISSED** without prejudice to Plaintiffs' refiling the claim in state court. Plaintiffs should [\*\*11] take note that the period of limitations for the dismissed state claim is tolled for an additional period of thirty (30) days after the date of this Order unless state law provides for a longer tolling period. [28 U.S.C. § 1367\(d\)](#). The Court will issue a separate Final Order.

SIGNED at Houston, Texas, this **25th** day of **August, 2005**.

Nancy F. Atlas

United States District Judge

**FINAL ORDER**

For the reasons stated in the accompanying Memorandum and Order, it is hereby

**ORDERED** that Defendants' Motion to Dismiss [Doc. # 38] is **GRANTED** and Hydril's Walker Process antitrust claim is **DISMISSED with prejudice**. It is further

**ORDERED** that the breach of contract claim is **DISMISSED** without prejudice to Plaintiffs' refiling the claim in state court. It is further

**ORDERED** that all prior ruling by the Court are hereby made final.

This is a final, appealable order.

SIGNED at Houston, Texas, this **25th** day of **August, 2005**.

Nancy F. Atlas

United States District Judge

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End of Document



## **Insignia Sys., Inc. v. News Corp., Ltd.**

United States District Court for the District of Minnesota

August 25, 2005, Decided ; August 25, 2005, Filed

Civil No. 04-4213 (JRT/FLN)

### **Reporter**

2005 U.S. Dist. LEXIS 42851 \*; 2005 WL 2063890

INSIGNIA SYSTEMS, INC., Plaintiff, v. NEWS CORPORATION, LTD., NEWS AMERICA MARKETING IN-STORE, INC., and ALBERTSON'S INC., Defendants.

**Subsequent History:** Motion to strike denied by, Motion denied by [Insignia Sys. v. News Am. Mktg. In-Store, Inc., 2006 U.S. Dist. LEXIS 47015 \(D. Minn., June 30, 2006\)](#)

Motion granted by, in part, Motion denied by, in part [Insignia Sys. v. News Am. Mktg. In-Store, 2008 U.S. Dist. LEXIS 136296 \(D. Minn., Mar. 26, 2008\)](#)

Related proceeding at [Insignia Sys. v. News Am. Mktg. In-Store Servs., 2008 U.S. Dist. LEXIS 130204 \(D.N.J., Aug. 27, 2008\)](#)

Motion denied by [Insignia Sys. v. News Am. Mktg. In-Store, 2010 U.S. Dist. LEXIS 158219 \(D. Minn., Feb. 4, 2010\)](#)

## **Core Terms**

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retailers, advertising, motion to dismiss, in-store, Sherman Act, allegations, conspiracy, antitrust, competitors, restraint of trade, relevant market, market power, boycott, markets, rule of reason, anticompetitive, foreclosure, foreclosed, horizontal, contracts

**Counsel:** [\*1] Willie L. Hudgins, COLLIER SHANNON SCOTT, PLLC, Washington, D.C., and Robert L. Meller, Jr. and Cynthia L. Hegarty, BEST & FLANAGAN LLP, Minneapolis, MN, for plaintiff.

Stacey Anne Mahoney, CONSTANTINE CANNON, New York, NY, and Todd Wind, FREDRIKSON & BYRON, Minneapolis, MN, for defendants News Corporation, Ltd. and News America Marketing In-Store, Inc.

Michael A. Lindsay, DORSEY & WHITNEY LLP, Minneapolis, MN, and Phillip A. Proger, JONES DAY, Washington, D.C., for defendant Albertson's Inc.

**Judges:** JOHN R. TUNHEIM, United States District Judge.

**Opinion by:** JOHN R. TUNHEIM

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

### **BACKGROUND**

Plaintiff Insignia, Inc. ("Insignia") and defendant News America Marketing In-Store, Inc. ("NAMI") are direct competitors in the in-store advertising market. Each buys shelf space and other advertising space from retailers, like defendant Albertson's, and sells advertising services, including in-store placement in retailers, to consumer packaged goods companies ("CPGs"), i.e. manufacturers of packaged products. Insignia contends that NAMI has engaged in activity that excludes Insignia and other competing in-store advertisers from access to retailers' advertising [\*2] space by (1) signing exclusive agreements with retailers; (2) orchestrating a boycott of other in-store advertisers by retailers; (3) engaging in exclusionary and anticompetitive conduct designed to harm Insignia and consumers; and, (4) making false and disparaging representations about Insignia. Insignia alleges state and federal antitrust violations against NAMI and Albertson's and false advertising violations against NAMI. NAMI and Albertson's move to dismiss under [Rule 12\(b\)\(6\)](#) for failure to state a claim. For the following reasons, the Court grants the motions to dismiss.

## ANALYSIS

### 1. STANDARD OF REVIEW

In a motion to dismiss, the Court construes the complaint in the light most favorable to the plaintiff and presumes all facts alleged in the complaint to be true. [Hishon v. King & Spalding, 467 U.S. 69, 73, 104 S. Ct. 2229, 81 L. Ed. 2d 59 \(1984\)](#); [Schmedding v. Tnemec Co. Inc., 187 F.3d 862, 864 \(8th Cir. 1999\)](#). The Court may dismiss a claim only where the plaintiff cannot prove any set of facts in support of his claim that would entitle him to relief. [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#); [Schmedding, 187 F.3d at 864](#). [\*3]

### II. CLAIMS 3,4,5,7,8, AND 9 - UNLAWFUL BOYCOTT AND EXCLUSIVE DEALING (Sherman Act § 1, Clayton Act § 3, Minn. Stat. §§ 325D.51 and .53)

To establish a claim under [section 1](#) of the Sherman Act, [section 3](#) of the Clayton Act, or [Minnesota Statute sections 325D.51](#) and [325D.53](#), a plaintiff must demonstrate (1) that there was a contract, combination, or conspiracy; and (2) that the agreement unreasonably restrained trade under either a *per se* rule of illegality or a rule of reason analysis. [Minn. Ass'n of Nurse Anesthetists v. Unity Hospital, 5 F. Supp. 2d 694, 704 \(D. Minn. 1998\)](#) ([section 1](#) of the Sherman Act); see 3M [Appleton Papers Inc., 35 F. Supp. 2d 1138, 1142-43 \(D. Minn. 1999\)](#) (analyzing claims under [section 3](#) of the Clayton Act and [section 1](#) of the Sherman Act together); [Howard v. Minn. Timberwolves Basketball Ltd., 636 N.W.2d 551, 557 \(Minn. Ct. App. 2001\)](#) (stating that [Section 1](#) of the Sherman Act is analogous to [Minnesota Statutes sections 325D.51](#) and [325D.53](#)).

#### A. Contract, Combination, Or Conspiracy

"In order to withstand a motion to dismiss, a plaintiff must go further than merely alleging [\*4] a conspiracy existed, for a bare bones accusation of conspiracy without any supporting facts is insufficient to state an antitrust claim." [Northwest Title & Escrow Corp. v. Edina Realty, 1993 U.S. Dist. LEXIS 20734, 1993 WL 593995, \\*1 \(D. Minn. Dec. 11, 1993\)](#) (internal quotation omitted); see also [Five Smiths, Inc. v. Nat'l Football League Players Ass'n, 788 F. Supp. 1042, 1048 \(D. Minn. 1992\)](#) ("general allegations of conspiracy, without a statement of the facts constituting the conspiracy, its objects and accomplishment are inadequate to state a cause of action"). A plaintiff must demonstrate that the defendants "had a conscious commitment to a common scheme designed to achieve an unlawful objective." [Minn. Nurse Anesthetists, 5 F. Supp. 2d at 704](#) (quoting [Monsanto Co. v. Spray-Rite Serv. Corp., 465 U.S. 752, 768, 104 S. Ct. 1464, 79 L. Ed. 2d 775 \(1984\)](#)). "[C]oncerted action forms the essence of a section 1 claim; unilateral actions do not give rise to antitrust liability under [section 1](#)." *Id.* (citing [Willman v. Heartland Hosp. E., 34 F.3d 605, 610 \(8th Cir. 1994\)](#)). Furthermore, "conduct as consistent with permissible competition as with [\*5] illegal conspiracy does not, standing alone, support an inference of antitrust conspiracy."

[Matsushita Elec. Indus. Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574, 587-88, 106 S. Ct. 1348, 89 L. Ed. 2d 538 \(1986\).](#)

Insignia has asserted that Albertson's and, possibly, other unnamed retailers have entered into long-term exclusive relationships with NAMI in exchange for unusually high up-front and guaranteed payments. According to Insignia, these induced relationships were intended to eliminate Insignia from the market. On their face, Insignia's allegations indicate only that NAMI unilaterally initiated a series of relationships that had the effect of preventing Insignia from doing business with some mostly unspecified retailers for an uncertain period of time, and that Albertson's and unspecified other retailers each agreed to exclusive relationships with NAMI at favorable terms. Offering a better deal than does the competition is a time-tested competitive strategy, and accepting a good deal when offered is generally considered to be a sound business practice. Insignia's allegations, therefore, provide insufficient indication of a common scheme designed to achieve an unlawful objective.

#### [\*6] B. Unreasonable Restraint Of Trade

Most agreements are evaluated under the "rule of reason," a standard that asks whether the alleged contract or agreement unreasonably restrains trade in a relevant product or geographic market. Certain kinds of agreements, however, are considered unlawful *per se* because they are of a type that is so often harmful and so rarely justified that proof of anticompetitiveness is not required. [Minnesota Ass'n of Nurse Anesthetists v. Unity Hosp., 208 F.3d 655, 659 \(8th Cir. 2000\)](#) (quoting [NYNEX Corp. v. Discon, Inc., 525 U.S. 128, 133, 119 S. Ct. 493, 142 L. Ed. 2d 510 \(1998\)](#)); see also [Concord Boat Corp. v. Brunswick Corp., 207 F.3d 1039, 1058 \(8th Cir. 2000\)](#).

##### 1. Per se violation

A "group boycott" is a narrow category of *per se* violation, "limited to cases in which firms with market power boycott suppliers or customers in order to discourage them from doing business with a competitor." [Minn. Nurse Anesthetists, 208 F.3d at 659](#) (quoting [FTC v. Ind. Fed'n of Dentists, 476 U.S. 447, 458, 106 S. Ct. 2009, 90 L. Ed. 2d 445 \(1986\)](#)). "It is not an antitrust 'boycott' when one supplier enters [\*7] into an exclusive supply agreement with one customer, even though the supplier's competitors are 'foreclosed' from that customer for the life of the contract." *Id.* A horizontal restraint of trade is another category of *per se* violation. See [Double D Spotting Service, Inc. v. Supervalu, Inc., 136 F.3d 554, 558 \(8th Cir. 1998\)](#). Horizontal restraints of trade result when combinations of traders at one level of the market structure agree to exclude direct competitors from the same level of the market. *Id.*

According to Insignia, Albertson's and other retailers, at the instigation of NAMI, agreed to deal only with NAMI and to exclude Insignia from the in-store advertising market resulting in a group boycott of Insignia and a horizontal restraint of trade. As noted above, Insignia's evidence and allegations indicate only that NAMI arranged one exclusive agreement with Albertson's, and may have arranged other similar relationships. This is insufficient to support an allegation of a group boycott. Additionally, as NAMI and Albertson's are not participants in the market at the same level, any agreement between the two cannot constitute a horizontal restraint of [\*8] trade. Although an agreement between retailers could constitute a horizontal restraint of trade, Insignia has not provided any indication that Albertson's has ever spoken to, let alone entered into an agreement with, another retailer regarding or resulting in the exclusion of Insignia from the market. The Court, therefore, finds that Insignia has not adequately alleged a *per se* violation of the antitrust laws, and Insignia's claims must therefore be analyzed under the Rule of Reason.

##### 2. Rule Of Reason

Exclusive dealing contracts are usually analyzed under the Rule of Reason. [Minn. Nurse Anesthetists, 208 F.3d at 660](#) (citing [Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 333-335, 81 S. Ct. 623, 5 L. Ed. 2d 580 \(1961\)](#)). In order to prevail, a plaintiff must produce evidence to show that the defendant's contractual arrangements were

unreasonable, based on the extent to which competition has been foreclosed in a substantial share of the relevant market, the duration of any exclusive arrangement, and the height of entry barriers. [Concord Boat, 207 F.3d at 1059-60.](#) "Where the degree of foreclosure caused by the exclusivity provisions [\*9] is so great that it invariably indicates that the supplier imposing the provisions has substantial market power, we may rely on the foreclosure rate alone to establish the violation. However, where ... the foreclosure rate is neither substantial nor even apparent, the plaintiff must demonstrate that other factors in the market exacerbate the detrimental effect of the challenged restraints." [Ryko Mfg. Co. v. Eden Servs., 823 F.2d 1215, 1235 \(8th Cir. 1987\)](#). Alternatively, a plaintiff may demonstrate that the challenged practice has actually produced significant anti-competitive effects, in which case formal market analysis is unnecessary. [Minn. Nurse Anesthetists, 5 F. Supp. 2d at 707](#) (citing [Ind. Dentists, 476 U. S. at 460-61](#))).

#### a. Market power/foreclosure

A plaintiff must demonstrate that the defendant has a dominant market share in a well-defined relevant market. [Flegel v. Christian Hosp., 4 F.3d 682, 689 \(8th Cir. 1993\)](#). Assuming that there are, as Insignia asserts, local, regional, and national markets for in-store advertising services, Insignia's complaint provides insufficient indication of NAMI's market [\*10] share or ability to foreclose competitors' participation in the relevant markets. Insignia asserts that NAMI dominates the relevant markets, that Insignia and Floorgraphics, Inc. pose the only significant competition to NAMI, and that NAMI has foreclosed Insignia from doing business with retailers in local, regional, and national markets by entering into exclusive contracts with 35,000 retail stores including the 2,500 Albertson's outlets throughout the nation. Based on this information, NAMI could, conceivably, dominate (in the colloquial sense) any given market with a 50% share as compared to Insignia's and Floorgraphics' hypothetical 25% shares, but fail to be dominant in the legal sense. See [Tops Mkts., Inc. v. Quality Mkts., Inc., 142 F.3d 90, 97 \(2d Cir. 1998\)](#) (finding 72% market share insufficient to support a section 1 claim); [Minn. Nurse Anesthetists, 5 F. Supp. 2d at 708](#) (stating that a market share of 30% is insufficient as a matter of law to constitute sufficient market power to achieve significant foreclosure). Furthermore, absent some indication of the percentage of the local, regional, or national markets that the 35,000 retail outlets [\*11] allegedly under exclusive contract constitute, it is impossible to evaluate the percentage of the market with which Insignia and other competitors are prevented from doing business, let alone determine that Insignia and other competitors are prevented from dealing with a significant number of retailers. See [Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 45-46, 104 S. Ct. 1551, 80 L. Ed. 2d 2 \(1984\)](#) (O'Connor, J., concurring) (quoted in [Minn. Nurse Anesthetists, 208 F.3d 655 at 661](#)) ("Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers and sellers are frozen out of a market by the exclusive deal"). These same deficiencies prevent the Court from determining whether significant barriers to entering this market or other factors exacerbating the detrimental effect of the challenged restraints exist. Insignia provides no indication of any barriers other than NAMI's exclusive contracts with the 35,000 retail outlets. Because it is unclear how large the markets are, or what the terms of the NAMI's alleged contracts are, it is impossible to determine how high a barrier is created by NAMI's exclusive contracts.

#### b. [\*12] Actual detrimental effects

Actual detrimental effects may include an actual increase in the price of the good or service, a decrease in output, or a decline in quality. [Minn. Nurse Anesthetists, 5 F. Supp. 2d at 707](#). Insignia broadly alleges that in-store information and advertising has been reduced and that higher prices have resulted. The Court finds that, as when demonstrating the existence of a contract, combination or conspiracy, such broad, unsupported allegations are inadequate to withstand a motion to dismiss.

Insignia's allegations indicate that NAMI is large and successful - but do not indicate that NAMI wields any particular degree of market power or ability to foreclose competitors from the market, or has entered into any sort of agreement in an attempt to do so. "Size in itself does not create an unlawful monopoly within the meaning of the Sherman Anti-Trust Act." [Kansas City Star Co. v. United States, 240 F.2d 643, 658 \(8th Cir. 1957\)](#). As Insignia's complaint insufficiently alleges either a contract, combination, or conspiracy or an unreasonable restraint of trade, the Court will grant NAMI's and Albertson's motions to dismiss with [\*13] respect to claims 3, 4, 5, 7, 8, and 9.

### III. CLAIMS 1 AND 10 - UNLAWFUL MONOPOLIZATION (Sherman Act § 2 and Minn. Stat. § 325d.52)

In order to make out a claim under either [section 2](#) of the Sherman Act or its Minnesota corollary, [Minnesota Statute section 325D.52](#), a plaintiff is required to plead and, ultimately, prove that the defendant "(1) possessed monopoly power in the relevant market and (2) willfully acquired or maintained that power as opposed to gaining it as a result 'of a superior product, business acumen, or historical accident.'" [Double D, 136 F.3d at 560; Howard, 636 N.W.2d at 556](#) (stating that Minnesota [antitrust law](#) should be interpreted consistently with federal court interpretations of federal [antitrust law](#) unless Minnesota law clearly conflicts.); [Prestressed Concrete, Inc. v. Bladholm Bros. Culvert Co., 498 N.W.2d 274, 276 \(Minn. Ct. App. 1993\)](#) (noting that [section 2](#) of the Sherman Act provided the model for [Minn. Stat. § 325D.52](#)).

Monopoly power under [§ 2](#) of the Sherman Act requires something greater than market power under [§ 1](#). See [Fortner Enterprises v. US. Steel, 394 U.S. 495, 89 S. Ct. 1252, 22 L. Ed. 2d 495 \(1969\)](#). [\*14] Thus, assuming *arguendo* that Insignia has adequately defined the relevant market and has alleged anticompetitive conduct sufficient to withstand a motion to dismiss, based on the Court's analysis in section II(B)(2)(a), *supra*, Insignia has not adequately established NAMI's monopoly power. Accordingly, the Court will grant NAMI's motion to dismiss claims 1 and 10.

### IV. CLAIMS 2 AND 11- ATTEMPTED MONOPOLIZATION (Sherman Act § 2 and Minn. Stat. § 325d.52)

To prevail on an unlawful attempt claim, Insignia must prove "(1) a specific intent by the defendant to control prices or destroy competition; (2) predatory or anticompetitive conduct undertaken by the defendant directed to accomplishing the unlawful purpose; and (3) a dangerous probability of success." [General Indus. Corp. v. Hartz Mountain Corp., 810 F.2d 795, 803 \(8th Cir. 1987\)](#).

"To determine whether there is a dangerous probability of monopolization, courts have found it necessary to consider the relevant market and the defendant's ability to lessen or destroy competition in that market." [Spectrum Sports, Inc. v. McQuillan, 506 U.S. 447, 456, 113 S. Ct. 884, 122 L. Ed. 2d 247 \(1993\)](#). "Proof [\*15] of market power in a monopolization claim and proof of dangerous probability of success in an attempt claim are of the same character." [3M v. Appleton Papers, 35 F. Supp. 2d at 1146](#). Thus, under the Court's analysis in section II(B)(2)(a), *supra*, Insignia has not adequately established NAMI's dangerous probability of success and the motion to dismiss these claims will be granted.

### V. CLAIMS 6 AND 12 - FALSE ADVERTISING (Lanham Act and Minnesota Deceptive Trade Practices Act)

In order to establish its false advertising claims, Insignia must establish (1) a false statement of fact made in a commercial advertisement, (2) which actually deceived or had a tendency to deceive a substantial segment of the intended audience, (3) which was material in that it was likely to influence purchasing decisions, (4) which has or is likely to injure Insignia, in the form of lost sales or lost goodwill. [3M Innovative Props. Co. v. Dupont Dow Elastomers LLC, 361 F. Supp. 2d 958, 968 \(D. Minn. 2005\)](#).

Insignia alleges that "NAMI has made repeated false and misleading ... statements of fact regarding Insignia and the nature, qualities and character of [NAMI's] [\*16] Price Pop Guaranteed program and Insignia's Price POPSign program," including its quality and efficacy, causing "CPGs and retailers to be confused, misled, and deceived about the nature, qualities and character of Insignia's in-store marketing vehicles" and influencing the decisions of "(a) CPGs to purchase Insignia's in-store advertising and promotion products and services; and (b) retailers to grant or honor the right to allow Insignia to sell its in-store advertising and promotion products and services for use in their respective retail stores." (Compl. PP101 and 102.) As a result, "Insignia has suffered economic injury, loss of good will, and other injuries in an amount to be determined at trial." (Compl. P103.)

The Court finds that Insignia fails to adequately allege a false statement of fact made in a commercial advertisement. Insignia's complaint does nothing to indicate what allegedly false statements were made to which party in what context. The allegations seem to indicate that NAMI made objectionable statements to CPGs and retailers in connection with sales of its own product, but not that NAMI engaged in something akin to a widespread

advertising campaign to discredit [\*17] Insignia's product and, thereby, boost its own product's success. Such an allegation is insufficient to satisfy the first prong. See *Med. Graphics Corp. v. SensorMedics Corp.*, 872 F. Supp. 643, 650 (D. Minn. 1994) (infrequent statements by a sales representative to potential customers, as opposed to a traditional advertising campaign, are unlikely to constitute commercial advertising). Accordingly, the Court will grant NAMI's motion to dismiss counts 6 and 12.

## VI. CONCLUSION

The Court is mindful that a party is required only to make a short and plain statement of its claims, and that this bar is not high. Nevertheless, the Court finds that Insignia's complaint, as it stands, simply provides insufficient information with which to determine whether any set of facts exists under which Insignia might be able to support its claims. As such, it is appropriate to grant defendants' motions to dismiss. However, the Court will permit Insignia to amend its complaint within 30 days from the date of this Order.

## ORDER

Based on the foregoing, all the records, files, and proceedings herein, **IT IS HEREBY ORDERED** that:

1. Defendant News America Marketing [\*18] In-Store, Inc.'s motion to dismiss [Docket No. 28] is **GRANTED**.
2. Defendant Albertson's Inc.'s motion to dismiss [Docket No. 30] is **GRANTED**.

**IT IS FURTHER ORDERED** that plaintiff shall have 30 days from the date of this Order to file an amended complaint.

DATED: August 25, 2005

at Minneapolis, Minnesota.

JOHN R. TUNHEIM

United States District Judge

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## MGA Entm't, Inc. v. Mattel, Inc.

United States District Court for the Central District of California

August 25, 2005, Decided ; August 26, 2005, Filed

CASE NO. CV 05-2727 NM (RNBx)

### **Reporter**

2005 U.S. Dist. LEXIS 18594 \*; 2005 WL 5894689

MGA ENTERTAINMENT, INC., Plaintiff, v. MATTEL, INC., a Delaware Corporation, and DOES 1-10, Defendants.

**Prior History:** [Mattel, Inc. v. Bryant, 441 F. Supp. 2d 1081, 2005 U.S. Dist. LEXIS 3568 \(C.D. Cal., Mar. 4, 2005\)](#)

## **Core Terms**

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allegations, competitor, unfair, demand letter, anti-competitive, products, doll, trade dress, litigation privilege, anti trust law, disgorgement, retailers, lawsuit, toy, unfair competition, intimidate, former employee, restitution, infringed, argues, factual allegations, proceedings, employees, distributors, manipulative, stricken, supplier, asserts, Scene, immaterial

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Subject Matter Jurisdiction > Jurisdiction Over Actions > General Overview

Civil Procedure > ... > Responses > Defenses, Demurrs & Objections > Motions to Dismiss

### **HN1[] Subject Matter Jurisdiction, Jurisdiction Over Actions**

A [Fed. R. Civ. P. 12\(b\)\(1\)](#) motion is a challenge to the court's jurisdiction over a matter. The plaintiff bears the burden of establishing that the court has subject matter jurisdiction to hear the action.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Dismiss > Failure to State Claim

### **HN2[] Motions to Dismiss, Failure to State Claim**

Under [Fed. R. Civ. P. 12\(b\)\(6\)](#), a motion to dismiss should be granted only if it appears beyond a doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief. For purposes of such a motion, the complaint is construed in a light most favorable to the plaintiff and all properly pleaded factual allegations are taken as true. All reasonable inferences are to be drawn in favor of the plaintiff.

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Strike > Immortal Matters

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Strike > General Overview

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Strike > Redundant Matters

Civil Procedure > ... > Defenses, Demurrs & Objections > Motions to Strike > Scandalous Matters

### **HN3** Motions to Strike, Immaterial Matters

Under [Fed. R. Civ. P. 12\(f\)](#), a court has the discretion to strike a pleading or portions thereof. [Rule 12\(f\)](#) provides that a court may order stricken from any pleading any redundant, immaterial, impertinent or scandalous matter. Immaterial matter is that which has no essential or important relationship to the claim for relief or the defenses being pleaded. Impertinent matter consists of statements that do not pertain, and are not necessary, to the issues in question. The function of a [Rule 12\(f\)](#) motion to strike is to avoid the expenditure of time and money that must arise from litigating spurious issues by dispensing with those issues prior to trial. Such motions are generally not granted unless it is clear that the matter sought to be stricken could have no possible bearing on the subject matter of the litigation. Any doubt concerning the import of the allegations to be stricken weighs in favor of denying the motion to strike.

International Trade Law > General Overview

Trademark Law > Subject Matter of Trademarks > Nontraditional Trademarks > Color Marks

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > Trade Dress Protection > Causes of Action

Trademark Law > ... > Trade Dress Protection > Infringement Actions > Burdens of Proof

Business & Corporate Compliance > ... > Trade Dress Protection > Infringement Actions > Elements of Trade Dress Infringement

Trademark Law > Causes of Action Involving Trademarks > Infringement Actions > Burdens of Proof

Trademark Law > ... > Factors for Determining Confusion > Intent of Defendant to Confuse > General Overview

Trademark Law > ... > Eligibility for Trademark Protection > Evidence of Secondary Meaning > General Overview

### **HN4** International Trade Law

In the United States Court of Appeals for the Ninth Circuit, trade dress refers to the total image of a product and may include features such as size, shape, color, color combinations, texture, or graphics. To establish trade dress infringement, a plaintiff must show: (1) that its product design is non-functional, (2) that the design is inherently distinctive or has acquired a secondary meaning, and (3) that there is a likelihood of confusion. The intent of the alleged infringer may be relevant to both the second and third elements of this test.

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Business & Corporate Compliance > ... > Trade Dress Protection > Infringement Actions > Elements of Trade Dress Infringement

Trademark Law > Likelihood of Confusion > General Overview

Trademark Law > ... > Factors for Determining Confusion > Intent of Defendant to Confuse > General Overview

Trademark Law > Special Marks > Trade Names > General Overview

Trademark Law > ... > Particular Subject Matter > Names > General Overview

#### **HN5** Federal Unfair Competition Law, Trade Dress Protection

The relevant intent for purposes of a trade dress claim (and the likelihood of confusion analysis) is the defendant's intent to deceive the public or the intent of deriving benefit from the reputation of the plaintiff's trade-mark or trade name.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN6** Regulated Practices, Trade Practices & Unfair Competition

The California Unfair Competition Law (UCL), [Cal. Bus. & Prof. Code § 17200 et seq.](#), prohibits, among other things, unfair business acts or practices. California courts generally define "unfair" broadly under the UCL in order to provide the courts with the maximum discretion to prohibit new schemes to defraud.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN7** Regulated Practices, Trade Practices & Unfair Competition

When a plaintiff who claims to have suffered injury from a direct competitor's unfair act or practice invokes [Cal. Bus. & Prof. Code § 17200](#), the word "unfair" in that section means conduct that threatens an incipient violation of an **antitrust law**, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN8** Regulated Practices, Trade Practices & Unfair Competition

The antitrust laws were enacted for the protection of competition, not competitors.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

#### **HN9** Private Actions, Remedies

Restitution and disgorgement are sometimes appropriate remedies under the California Unfair Competition Law, [Cal. Bus. & Prof. Code § 17200 et seq.](#)

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## **HN10** [ ] **Private Actions, Remedies**

The California Unfair Competition Law, [Cal. Bus. & Prof. Code § 17200 et seq.](#), does not allow for an individual to recover disgorgement of profits allegedly obtained by means of an unfair business practice where those profits are neither money taken from a plaintiff nor funds in which the plaintiff has an ownership interest.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Civil Procedure > ... > Justiciability > Standing > Injury in Fact

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > Standing

Civil Procedure > ... > Justiciability > Standing > General Overview

## **HN11** [ ] **Regulated Practices, Trade Practices & Unfair Competition**

[Cal. Bus. & Prof. Code § 17204](#) provides that a party has standing to bring an action pursuant to the California Unfair Competition Law (UCL), [Cal. Bus. & Prof. Code § 17200 et seq.](#), if it has suffered injury in fact and has lost money or property as a result of a violation of the UCL.

Torts > ... > Defenses > Privileges > Statutory Privileges

## **HN12** [ ] **Privileges, Statutory Privileges**

See [Cal. Civ. Code § 47\(b\)](#).

Torts > ... > Defenses > Privileges > Statutory Privileges

## **HN13** [ ] **Privileges, Statutory Privileges**

The litigation privilege set out in [Cal. Civ. Code § 47\(b\)](#) applies to any communication: (1) made in judicial or quasi-judicial proceedings; (2) by litigants or other participants authorized by law; (3) to achieve the objects of the litigation; and (4) to have some connection or logical relation to the action.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

## **HN14** [ ] **Exemptions & Immunities, Noerr-Pennington Doctrine**

The Noerr-Pennington doctrine extends to all three branches of government, and thus exempts bringing a lawsuit--that is, petitioning a court--from antitrust liability.

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

### **HN15** [blue icon] Motions to Dismiss, Failure to State Claim

A district court ruling on a motion to dismiss may consider a document the authenticity of which is not contested, and upon which the plaintiff's complaint necessarily relies.

Torts > ... > Defenses > Privileges > Statutory Privileges

### **HN16** [blue icon] Privileges, Statutory Privileges

Pre-litigation demand letters are protected by the litigation privilege only when the statement is made in connection with a proposed litigation that is contemplated in good faith and under serious consideration.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

### **HN17** [blue icon] Noerr-Pennington Doctrine, Sham Exception

While Noerr-Pennington immunity is broad, it is not so broad as to cover all litigation: sham petitions do not fall within the protection of the doctrine. There are three circumstances when litigation might be sham. First, if the alleged anticompetitive behavior consists of bringing a single sham lawsuit (or a small number of such suits), the antitrust plaintiff must demonstrate that the lawsuit was (1) objectively baseless, and (2) a concealed attempt to interfere with the plaintiff's business relationships. Second, if the alleged anticompetitive behavior is the filing of a series of lawsuits, the question is not whether any one of them has merit--some may turn out to, just as a matter of chance--but whether they are brought pursuant to a policy of starting legal proceedings without regard to the merits and for the purpose of injuring a market rival. Finally, in the context of a judicial proceeding, if the alleged anticompetitive behavior consists of making intentional misrepresentations to the court, litigation can be deemed a sham if a party's knowing fraud upon, or its intentional misrepresentations to, the court deprive the litigation of its legitimacy.

**Counsel:** [\*1] For MGA Entertainment Inc, Plaintiff: Diana M Torres, Paula Elise Ambrosini, O'Melveny and Myers, Los Angeles, CA; Patricia L Glaser, Christensen Miller Fink Jacobs Glaser, Weil & Shapiro, Los Angeles, CA.

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**Judges:** Nora M. Manella, United States District Judge.

**Opinion by:** Nora M. Manella

## **Opinion**

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ORDER AND OPINION GRANTING IN PART AND DENYING IN PART DEFENDANT'S MOTION TO DISMISS AND STRIKE PORTIONS OF COMPLAINT

## I. INTRODUCTION

On April 13, 2005, plaintiff MGA Entertainment, Inc. ("MGA") initiated this action against rival toy doll maker, defendant Mattel, Inc. ("Mattel"). MGA contends that it "seeks by this action to halt Mattel's habitual and unfair tactics of competition-by-intimidation and serial copycatting of MGA's products." Compl. P 7. The Complaint asserts causes of action for: (1) False Designation of Origin or Affiliation in Violation of [15 U.S.C. § 1125\(a\)](#); (2) Unfair Competition in Violation of [15 U.S.C. § 1125\(a\)](#), [\*2] [Cal. Bus. & Prof. Code § 17200 et seq.](#), and [California Common Law](#); (3) Dilution in Violation of [15 U.S.C. § 1125\(c\)](#), [Cal. Bus. & Prof. Code § 14330](#), and California Common Law; and (4) Unjust Enrichment. On May 13, 2005, Mattel filed the instant Motion to Dismiss and Strike Portions of Complaint Pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#), [12\(f\)](#), and [12\(b\)\(1\)](#). For the reasons set forth below, Mattel's motion is GRANTED in part and DENIED in part.

## II. FACTUAL & PROCEDURAL BACKGROUND

1

MGA's Complaint is divided into four parts: (1) background factual allegations, [see](#) Compl. PP 7-30; (2) allegations regarding Mattel's "serial copycatting" of MGA's products, [See id.](#) PP 31-73; (3) allegations regarding Mattel's [\*3] "strong-arm tactics, and other illegitimate, unfair and anti-competitive" conduct, [Id.](#) PP 74-100; and (4) MGA's causes of action and claims for relief, [Id.](#) PP 101-25.

### **A. Background Factual Allegations**

In paragraphs 7 through 30 of the Complaint, MGA provides various background factual allegations. [See id.](#) PP 7-30. In particular, this section of the Complaint details how Mattel came to dominate the fashion doll market in the twentieth century through sales of its mainstay product, "Barbie"; how both the public's interest in Barbie and Mattel's success began to wane in the late 1990s; and how MGA's 2001 release of its new and "fresh-looking" doll line, the "Bratz," came at just the right time to take advantage of the public's growing apathy for Barbie. [See id.](#)<sup>2</sup> The Complaint uses these facts to set the scene for MGA's claim that Mattel was "in trouble," and had to do something to regain the market share it was losing to MGA. MGA then alleges that Mattel, rather than "respond . . . with a new, creative product of its own," decided to "wage[] war against MGA using a wide-array of tortious, unfair and anti-competitive practices including systematic, serial [\*4] copycatting and intellectual property infringement, aided by intimidation, threats and other acts of unfair competition and anti-competitive conduct." [Id.](#) P 32.

### **B. Serial Copycatting**

In the second section of the Complaint, paragraphs 33 through 73, MGA alleges that Mattel responded to the competition posed by the Bratz by creating and marketing various dolls and products that infringed on the trade dress of the Bratz and MGA's other products. [See id.](#) PP 33-73. In particular, MGA alleges that Mattel introduced a line of dolls in October 2002 called "My Scene" that infringed on the Bratz's trade dress. [Id.](#) MGA also contends that Mattel's "serial copycatting" "extended to MGA's packaging, themes, accessories, advertising and even other product lines." [Id.](#) Finally, MGA mentions a failed Mattel doll line called the "Flavas." [See id.](#) P 35. MGA suggests [\*5] that Mattel's My Scene dolls "may have been . . . intended to buy Mattel time while it worked to release . . . Flavas." [Id.](#) However, according to MGA, the Flavas failed in the market because they "took the urban, hip-hop' look too far, and were widely viewed as portraying a trampy, bad-girl' image." [Id.](#)

<sup>1</sup> The following facts from the Complaint are assumed true for purposes of this motion only.

<sup>2</sup> MGA describes the Bratz as "multi-ethnic fashion dolls that sport a fresh new urban and contemporary look and fashion." Compl. P 8.

### C. Unfair, Manipulative, and Anti-Competitive Conduct

In the third section of the Complaint, entitled "Mattel's additional unfair, manipulative, anti-competitive conduct," MGA alleges that Mattel has engaged in "strong-arm tactics, and other illegitimate, unfair and anti-competitive means . . . to manipulate the market and ensure that its control and domination of the industry can continue unabated." Id. P 74. See id. PP 74-100. Because Mattel's Motion focuses on this portion of the Complaint, a detailed description is in order.

MGA first alleges that "Mattel has sent threatening letters to several of its former employees who now work for MGA warning them not to disclose *even publicly available information* about Mattel, including the names and positions of Mattel employees." Id. P 75 (emphasis in original). Additionally, MGA alleges, "Mattel [\*6] even went so far as to sue one of its former senior executives, after he had the temerity to resign and join MGA in October 2004." Id. According to MGA, this lawsuit was dismissed with prejudice because Mattel's Complaint "fail[ed] to state a viable claim" and Mattel could not "muster up a shred of evidence sufficient to support an amended complaint." Id.

MGA next alleges that Mattel has intimidated various companies, such as publishing entities, into not doing business with MGA. Id. P 76.<sup>3</sup> Similarly, MGA alleges that "Mattel has used . . . intimidation to pressure distributors and retailers, particularly in foreign countries, not to distribute Bratz, to reduce shelf and display space for Bratz and to place Bratz in unfavorable locations at retail outlets." Id. P 77.

[\*7] MGA also alleges that Mattel has tried to lock MGA out of the market by buying up the supply of necessary products. In particular, MGA contends: "When MGA faced a shortage of doll hair in October 2002, MGA is informed and believes that the reason for that shortage was that Mattel had locked MGA out by buying up the supply from the two main hair supply companies." Id. P 78.

MGA further accuses Mattel of "manipulat[ing] the retail market." Id. P 79. For example, MGA asserts: "Mattel merchandisers have been caught tampering with MGA's retail displays, replacing favorably located MGA merchandise with Mattel merchandise." Id. P 79. Additionally, "Mattel . . . falsely told a major United States retailer that MGA was giving another major United States retailer below-market pricing and falsely told a United Kingdom retailer that MGA was discontinuing one of its lines, in order to make such line less attractive to buyers and thereby attempt to increase sales of the competitive Mattel product and improve its own sales, at MGA's expense." Id.

MGA then details how "[e]ven supposedly unbiased and impartial industry organizations have fallen prey to Mattel's abusive wield[ing] [\*8] of power, to MGA's detriment." Id. P 80. For example, MGA alleges:

NPD Funworld ("NPD") . . . is the leading supplier of sales statistics in the toy industry. Accurate NPD statistics are essential for efficient product-line management. Without these statistics, it is difficult, if not impossible, for toy companies to assess and measure the relative success of their products in key categories. It is, however, a subscription service, and NPD restricts the manner in which its subscribers may use the data it provides. Mattel has regularly ignored the restrictions. . . . Mattel generates substantially more annual subscription revenue for NPD than does MGA, and carries more clout. After MGA had subscribed to the service for more than 12 years, NPD terminated MGA's subscription in 2003 theoretically on the grounds that MGA misused NPD data in a press release. MGA is informed and believes that the termination was the result of pressure from Mattel, notwithstanding Mattel's own frequent violations of NPD's restrictions.

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<sup>3</sup> In particular, MGA alleges:

Mattel has . . . warned a number of companies, including the biggest publishing entity in the United Kingdom, not to license MGA products, or risk retribution. The threats are not idle. In May 2004, Mattel terminated one of its licensees, apparently in retribution for licensing "Bratz." While some companies have been courageous enough to take the risk, others have not, and MGA has lost valuable licensing opportunities as a result.

In addition to this, the market share numbers that NPD generates are heavily dependent on the category in which NPD places a particular product. MGA is informed [\*9] and believes that Mattel also pressured NPD into changing certain product classifications for its Bratz products in order to manipulate the data and preserve Mattel's market share rankings in the critical fashion doll category -- and thereby lower MGA's.

The Children's Advertising Review Unit ("CARU") is . . . is the toy industry's supposedly independent self-regulatory body in charge of maintaining standards in advertising. . . . CARU is heavily subsidized by Mattel. . . . Upon information and belief, Mattel has used its influence as a major contributor to CARU's budget to induce CARU to place onerous restrictions on MGA advertisements, and require MGA to amend aspects of commercials that have gone unchallenged in other parties' commercials. . . .

Even [the Toy Industry Association ("TIA")], the toy industry's trade association, is apparently not untainted by Mattel's influence and power. Each year, TIA presents the Toy-of-the-Year Awards, the most prestigious of which had been the award for Toy of the Year. Winning the Toy of the Year Award is a significant achievement that not only very likely increases the sales of the winning toy, but also denotes the winning company [\*10] as a leader in toy innovation and generates substantial goodwill with retailers, distributors, licensees, and customers.

For the years 2000 . . . , 2001 and 2002, the Toy of the Year award was chosen by consumer vote. . . . Leap Frog won the 2000 . . . Award and MGA won[in] 2001 and 2002. . . . With the 2003 . . . Award, however, the rules suddenly changed. Now, the award is selected by members of the industry. Upon information and belief, this change was orchestrated by a Fisher Price (a Mattel subsidiary) executive who, until recently, served as the Chairman of TIA. Perhaps not surprisingly given this change in the winner selection procedures, "Hokey Pokey Elmo" ("Elmo"), a Fisher Price toy, won for the year 2003 . . . , beating out the other leading nominee, "Bratz Formal Funk Super Stylin' Runway Disco."

TIA has refused to provide MGA with the vote count procedure and totals for this award, despite repeated requests.

MGA is also informed and believes that Mattel was instrumental in attempting to keep MGA from participating as a sponsor in this year's "Kids' Choice Awards."

Compl. PP 81-97.

Finally, MGA alleges:

Mattel has clearly engaged in tortious, [\*11] illegal and unethical behavior in its unfettered efforts to disrupt, if not destroy, MGA. Indeed, this is apparently Mattel's current *modus operandi* when it comes to "competing" in the industry. The once immensely successful "LeapFrog" interactive learning product, for example, has apparently been one of Mattel's other recent victims.

Id. P 98.

#### **D. Causes of Action and Claims for Relief**

In the last section of the Complaint, MGA asserts the following four causes of action: (1) "False Designation of Origin in Violation of [15 U.S.C. § 1125\(a\)](#)"; (2) "Unfair Competition in Violation of [15 U.S.C. § 1125\(a\)](#) and Unfair Competition and Unfair Business Practices in Violation of [Cal. Bus. & Prof. Code § 17200 et seq.](#) and California Common Law"; (3) "Dilution in Violation of [15 U.S.C. § 1125\(c\)](#); [Cal. Bus. & Prof. Code § 14330](#) and California Common Law"; and (4) "Unjust Enrichment." Among other remedies, MGA requests restitution and disgorgement. Id. P 118; Prayer P 3(b).

On April 13, 2005, MGA filed the Complaint against Mattel. [\*12] On May 13, 2005, Mattel filed the instant Motion to Dismiss and Strike Portions of Complaint Pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#), [12\(f\)](#), and [12\(b\)\(1\)](#).

### **III. LEGAL STANDARD**

**HN1** A [Rule 12\(b\)\(1\)](#) motion is a challenge to the court's jurisdiction over a matter. See [Fed. R. Civ. P. 12\(b\)\(1\)](#). The plaintiff bears the burden of establishing that the court has subject matter jurisdiction to hear the action. [Kokkonen v. Guardian Life Ins. Co.](#), 511 U.S. 375, 377, 128 L. Ed. 2d 391, 114 S. Ct. 1673 (1994); [Stock West v. Confederated Tribes](#), 873 F.2d 1221, 1225 (9th Cir. 1989).

**HN2** Under [Rule 12\(b\)\(6\)](#), a motion to dismiss should be granted only if it appears beyond a doubt that the plaintiff "can prove no set of facts in support of his claim which would entitle him to relief." [Conley v. Gibson](#), 355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 (1957). See also [Fed. R. Civ. P. 12\(b\)\(6\)](#). For purposes of such a motion, the complaint is construed in a light most favorable to the plaintiff and all properly pleaded [\*13] factual allegations are taken as true. [Jenkins v. McKeithen](#), 395 U.S. 411, 421, 23 L. Ed. 2d 404, 89 S. Ct. 1843 (1969); [Everest and Jennings, Inc. v. American Motorists Ins. Co.](#), 23 F.3d 226, 228 (9th Cir. 1994). All reasonable inferences are to be drawn in favor of the plaintiff. [Jacobson v. Hughes Aircraft](#), 105 F.3d 1288, 1296 (9th Cir. 1997).

**HN3** Finally, under [Rule 12\(f\)](#), the court has the discretion to strike a pleading or portions thereof. [Federal Sav. and Loan v. Gemini Management](#), 921 F.2d 241, 243 (9th Cir. 1990). See also [Fed. R. Civ. P. 12\(f\)](#). Rule 12(f) provides that a court "may order stricken from any pleading . . . any redundant, immaterial, impertinent or scandalous matter." [Fed. R. Civ. P. 12\(f\)](#). "Immaterial" matter is that which has no essential or important relationship to the claim for relief or the defenses being pleaded. [Fantasy, Inc. v. Fogerty](#), 984 F.2d 1524, 1527 (9th Cir. 1993) (citing 5 Charles A. Wright & Arthur R. Miller, [Federal Practice and Procedure](#) § 1382, at 706-07 (1990)), rev'd on other grounds, [510 U.S. 517, 127 L. Ed. 2d 455, 114 S. Ct. 1023 \(1994\)](#). [\*14] "Impertinent" matter consists of statements that do not pertain, and are not necessary, to the issues in question." *Id.* "[T]he function of a [Rule 12\(f\)](#) motion to strike is to avoid the expenditure of time and money that must arise from litigating spurious issues by dispensing with those issues prior to trial. . . ." [Sidney-Vinstein v. A.H. Robins Co.](#), 697 F.2d 880, 885 (9th Cir. 1983). Such motions are "generally not granted unless it is clear that the matter sought to be stricken could have no possible bearing on the subject matter of the litigation." [Rosales v. Citibank, Federal Sav. Bank](#), 133 F. Supp. 2d 1177, 1179 (N.D. Cal. 2001). Any doubt concerning the import of the allegations to be stricken weighs in favor of denying the motion to strike. See [In re 2TheMart.com, Inc. Secs. Litig.](#), 114 F. Supp. 2d 955, 965 (C.D. Cal. 2000).

## IV. ANALYSIS

Mattel argues that the court should dismiss and/or strike: (1) the majority of the first section of the Complaint, which consists of the background factual allegations; (2) the third section of the Complaint, entitled "Mattel's additional unfair, manipulative, anti-competitive conduct, [\*15]" as well as related parts of the Complaint, including MGA's request for restitution and disgorgement; (3) specifically paragraph 98 of the Complaint, which includes allegations regarding Mattel's "modus operandi" and LeapFrog; and (4) paragraph 75 of the Complaint, which alleges that Mattel has harassed employees who have left Mattel for MGA.

### A. First Section of Complaint -- Background Factual Allegations

Mattel argues that the court should strike the background factual allegations contained in paragraphs 11-20 and 30-31 of the Complaint. According to Mattel, these paragraphs, which primarily discuss Mattel's financial and corporate history, are immaterial to MGA's case. MGA responds that these paragraphs should not be stricken because they help elucidate Mattel's motive/intent in creating the My Scene dolls and the various other products that allegedly infringe upon the trade dress of the Bratz and MGA's other products, in violation of the Lanham Act, [15 U.S.C. § 1125\(a\)](#).

**HN4** In the Ninth Circuit, trade dress "refers to the total image of a product' and may include features such as size, shape, color, color combinations, texture or graphics." [International Jensen, Inc. v. Metrosound U.S.A., Inc.](#), 4 F.3d 819, 822 (9th Cir. 1993); [\*16] [Vision Sports, Inc. v. Melville Corp.](#), 888 F.2d 609, 613 (9th Cir. 1989). To

establish trade dress infringement, a plaintiff must show: (1) that its product design is non-functional, (2) that the design is inherently distinctive or has acquired a secondary meaning, and (3) that there is a likelihood of confusion. *Disc Golf Ass'n, Inc. v. Champion Discs, Inc.*, 158 F.3d 1002, 1005 (9th Cir. 1998); *Kendall-Jackson Winery, Ltd. v. E. & J. Gallo Winery*, 150 F.3d 1042, 1046-47 (9th Cir. 1998); *International Jensen, Inc. v. Metrosound U.S.A., Inc.*, 4 F.3d 819, 823 (9th Cir. 1993). The "intent" of the alleged infringer may be relevant to both the second and third elements of this test. See *Fuddruckers, Inc. v. Doc's B.R. Others, Inc.*, 826 F.2d 837, 844-45 (9th Cir. 1987) (evidence of deliberate copying may support inference of secondary meaning); *AMF, Inc. v. Sleekcraft Boats*, 599 F.2d 341, 348-49 (9th Cir. 1979) (factors considered in determining "likelihood of confusion" include intent of defendant in selecting allegedly infringing mark); *id. at 354* (when infringer knowingly [¶17] adopts mark, court can presume public will be deceived).

MGA's background factual allegations regarding Mattel's corporate and financial history set the scene and circumstantially bolster MGA's claim that Mattel intentionally copied MGA's trade dress. In particular, these allegations paint a picture of an industry giant which had recently fallen on hard times and was willing to do whatever was necessary to stop the hemorrhaging and eliminate the rising tide of competition stemming from a new company with a drastically different product. According to MGA, Mattel, because of its corporate culture and history, was unable to "nimbly respond . . . with a new, creative product of its own." Compl. ¶ 31. Instead, Mattel (intentionally) copied the Bratz and released its My Scene line. Mattel's financial and corporate history -- and, particularly, its vulnerability at the time of the Bratz's release -- play into MGA's theory that Mattel intentionally copied MGA's trade dress. Accordingly, paragraphs 11-20 and 30-31 of the Complaint are not "immaterial," and Mattel's motion to strike these paragraphs is denied.<sup>4</sup>

#### **[¶18] B. Third Section of Complaint -- "Mattel's Additional Unfair, Manipulative, Anti-Competitive Conduct"**

Mattel argues that the court should dismiss and/or strike the third section of the Complaint, entitled "Mattel's additional unfair, manipulative, anti-competitive conduct," as well as various other related allegations. According to Mattel, these allegations, contained in paragraphs 74-100, 113-114, and 118 of the Complaint, are not material to any of MGA's causes of action. Furthermore, Mattel contends that the court should strike MGA's request for restitution and disgorgement.

##### **1. Materiality and/or Relevance**

MGA responds to Mattel's first argument by asserting that the allegations in the third section of the Complaint are relevant and/or material to both its trade dress claims and its unfair competition claims.

###### **a. Relevance to Trade Dress Claims**

MGA argues that the allegations in the third section of the Complaint are relevant to its trade dress claims because they help elucidate Mattel's "intent."

**HN5** The relevant "intent" for purposes of a trade dress claim (and the likelihood of confusion analysis) is the defendant's "intent to deceive the public" or the [¶19] "intent of deriving benefit from the reputation of the [plaintiff's] trade-mark or trade name." *Brookfield Commc'n, Inc. v. West Coast Entm't Corp.*, 174 F.3d 1036, 1059 (9th Cir. 1999). See also *Toho Co., Ltd. v. Sears, Roebuck & Co.*, 645 F.2d 788, 791 n. 2 (9th Cir. 1981) ("In order to raise

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<sup>4</sup> For the same reason, the court denies Mattel's motion to strike paragraph 35 of the Complaint, which provides relevant background information regarding the purpose of Mattel's release of the My Scene dolls and its release of the "Flavas." See Compl. PP 35-36 ("[Mattel's My Scene dolls,] [the] confusingly similar Bratz imitators [,] may have been originally intended to buy Mattel time while it worked to release another product the following summer, called Flavas.' . . . The [Flavas] were not well-received. . . . Mattel has seemingly abandoned this line. Realizing that My Scene' was its best bet for riding MGA's successful coattails and capitalizing on the unique and inherently distinctive look that MGA had developed in its Bratz' dolls -- and MGA's substantial goodwill -- Mattel has systematically proceeded to modify the My Scene' dolls since their original release, particularly their eyes, to increase their similarity to Bratz' more and more over time.").

the inference of a likelihood of confusion, a plaintiff must show that the defendant intended to profit by confusing consumers."); J. Thomas McCarthy, *McCarthy on Trademarks and Unfair Competition* § 23:113 (2005) ("[W]hen the accused infringer's state of mind is introduced as relevant to the liability issue of the likelihood of confusion, . . . the only relevant intent is intent to confuse.").

The allegations contained in the third section of the Complaint do not help demonstrate that Mattel had this particular "intent" when it created the My Scene dolls or any other allegedly infringing product. For example, Mattel's alleged "intent to deceive the public" in creating the My Scene dolls or its intent to "derive benefit from the reputation" of MGA's Bratz is not evidenced by the fact that "Mattel has sent threatening letters to several of its former employees" or [\*20] has intimidated others into not dealing with MGA. These alleged facts, and the others asserted in the third section of the Complaint, demonstrate that Mattel is a fierce (and perhaps unfair) competitor, not that it acted with an "intent to deceive" in creating its products. Therefore, the third section of the Complaint cannot be sustained on the ground that it supports MGA's trade dress claims.<sup>5</sup>

#### *b. Relevance to Unfair Competition Claims*

MGA also argues that the allegations in the third section of the Complaint support its claim for "unfair competition" under *Cal. Bus. & Prof. Code § 17200 et seq.*

**HN6** [↑] *California Business and Professions Code section 17200 et seq.* [\*21] (the "Unfair Competition Law" or "UCL") prohibits, among other things, "unfair business acts or practices." *Id.* California courts have generally defined "unfair" broadly under the UCL in order to "provide the courts with the maximum discretion to prohibit new schemes to defraud." *National Rural Telecomm. Coop. v. DirectTV, Inc.*, 319 F. Supp. 2d 1059, 1075 (C.D. Cal. 2003) (Baird, J.) (citing *Motors, Inc. v. Times Mirror Co.*, 102 Cal. App. 3d 735, 740, 162 Cal. Rptr. 543 (1980)). See also *People ex rel. Renne v. Servantes*, 86 Cal. App. 4th 1081, 1095, 103 Cal. Rptr. 2d 870 (2001) ("The [UCL] is intentionally broad to give the court maximum discretion to control whatever new schemes may be contrived, even though they are not yet forbidden by law.").

In *Cel-Tech Communications, Inc. v. Los Angeles Cellular Telephone Co.* ("Cel-Tech"), 20 Cal. 4th 163, 83 Cal. Rptr. 2d 548, 973 P.2d 527 (1999), the California Supreme Court clarified the definition of "unfair" insofar as it applies to cases between direct competitors, such as that now before the court. In particular, the *Cel-Tech* court turned to *section 5 of the Federal Trade Commission Act* ("FTCA"), 15 U.S.C. § 45(a), [\*22] and stated:

**HN7** [↑] When a plaintiff who claims to have suffered injury from a direct competitor's "unfair" act or practice invokes *section 17200*, the word "unfair" in that section means conduct that threatens an incipient violation of an **antitrust law**, or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition.

*Id.* at 186-87.

Here, MGA claims that Mattel's conduct alleged in the third section of the Complaint "violated the policy or spirit" of the antitrust laws "because its effects were comparable" to a violation of those laws, and/or "otherwise significantly threatened or harmed competition." At this early stage in the proceedings, assuming all facts and all reasonable inferences in MGA's favor, the court agrees.

MGA alleges that Mattel has chosen to "compete" with MGA (and others in the industry) not by creating a better product or lowering its prices, but by using its extraordinary market power to unfairly preclude other companies and brands from entering and competing. For example, MGA alleges that Mattel has used its [\*23] massive influence to

<sup>5</sup> This same reasoning applies to defeat MGA's arguments that the third section of the Complaint supports MGA's claims for attorneys' fees, injunctive relief, and "unfair competition" under the Lanham Act, 15 U.S.C. § 1125(a). The relevant "intent" raised by each of these claims is the same as that raised by MGA's trade dress claims.

corruptively cause industry groups to discriminate against MGA even though MGA needs to be associated with these groups to exist, survive, and thrive in the industry. See Compl. PP 81-96. Similarly, MGA contends that Mattel has used its great market power, which included a 90% share of the fashion doll market in 1997, to intimidate others into not dealing with MGA. Id. PP 74-77. MGA also asserts that Mattel has intentionally engaged in schemes to buy up supplies to lock MGA (and others) out of the market. Id. P 78. Finally, Mattel employees have allegedly been caught tampering with MGA's displays, and have lied to others about MGA's products. Id. P 79.

At this early stage in the proceedings, the court cannot say that this collective conduct is consistent with the "policy and spirit" of the antitrust laws, and/or provides no "significant threat or harm" to competition. In Cel-Tech, itself, the California Supreme Court stated that "the purpose of the antitrust law is to foster and encourage competition' by prohibiting practices by which fair and honest competition is destroyed or prevented." Cel-Tech, 20 Cal. 4th at 186 (quoting [\*24] Cal. Bus. & Prof. Code § 17001). See also Northeast Airlines, Inc. v. World Airways, Inc., 262 F. Supp. 316, 319 (D. Mass. 1966) ("we believe that the purpose of destroying a competitor by means that are not within the area of fair and honest competition is a purpose that clearly subverts the goal of the [antitrust laws] "). Similarly, it is recognized that the federal antitrust laws were "designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade." See William Meade Fletcher, 10A Fletcher Cyclopedia f the Law of Private Corporations § 4981 (2004) (discussing the Sherman Act). Mattel, by its above-mentioned conduct, has prevented "fair competition" from occurring and has undermined "free and unfettered competition."

Additionally, the antitrust laws and the FTCA have been applied to enjoin conduct arguably similar to Mattel's. Compare Compl. PP 75-77 (alleging that Mattel, using its extraordinary market power, has intimidated employees, publishing entities, distributors, and retailers into not doing business with and discriminating against MGA), [\*25] with Federal Trade Commission ("FTC") v. Brown Shoe Co., 384 U.S. 316, 321, 16 L. Ed. 2d 587, 86 S. Ct. 1501 (1966) ("basic policies" of antitrust laws violated when second largest shoe manufacturer employed extremely attractive program that required retailers "substantially to limit their trade with [manufacturer's] competitors"); Adolph Coors Co. v. FTC, 497 F.2d 1178 (10th Cir. 1974) (affirming FTC finding that powerful supplier violated FTCA by coercing distributors and retailers into participating in a variety of anticompetitive conduct, including excluding products of supplier's competitor); Union Circulation Co. v. FTC, 241 F.2d 652, 655-56 (2d Cir. 1957) (affirming FTC finding that defendants violated FTCA by "coercing" others into not doing business with defendants' competitor); Hastings Mfg. Co. v. FTC, 153 F.2d 253, 42 F.T.C. 887 (6th Cir. 1946) (affirming FTC finding that defendant violated FTCA by using various means to induce distributors into refusing to handle competitors' products); Carter Carburetor Corp. v. FTC, 112 F.2d 722, 734-36, 31 F.T.C. 1793 (8th Cir. 1940) (affirming FTC finding that powerful supplier violated FTCA by "inducing, coercing and compelling" [\*26] many independent [retailers] to cancel existing sales contracts with . . . competitor and to cease and refuse to deal in the products of such competitor"); FTC v. Wallace, 75 F.2d 733, 20 F.T.C. 713 (8th Cir. 1935) (affirming FTC finding that defendant coal dealers violated FTCA by intimidating and threatening to boycott suppliers that dealt with competitors); Amarel v. Connell, 202 Cal. App. 3d 137, 142, 145, 248 Cal. Rptr. 276 (1988) (plaintiff rice growers stated antitrust claim against powerful vertically-integrated competitors, in part, because competitors refused to do business with those who dealt with plaintiffs' customers); Kolling v. Dow Jones & Co., Inc., 137 Cal. App. 3d 709, 187 Cal. Rptr. 797 (1982) (violation of antitrust laws for supplier to threaten, intimidate, and coerce distributor into participating in anticompetitive conduct); R.E. Spriggs Co., Inc. v. Adolph Coors Co., 94 Cal. App. 3d 419, 425, 156 Cal. Rptr. 738 (1979) (violation of antitrust laws for supplier to force distributors into anticompetitive behavior "through suggestions which the distributors could not refuse"). Compare Compl. P 78 (alleging Mattel bought up supply of doll hair from two largest suppliers [\*27] to lock MGA out of market), with Amarel, 202 Cal. App. 3d at 142, 145 (plaintiff rice growers stated antitrust claim against integrated competitors, in part, because competitors locked plaintiffs' customers out of ports necessary for business). Compare Compl. P 79 (alleging Mattel manipulated market by lying about MGA's products), with Northeast Airlines, Inc., 262 F. Supp. at 319 ("[W]e believe that the purpose of destroying a competitor by means that are not within the area of fair and honest competition is a purpose that clearly subverts the goal of the [anti-trust laws]. . . . The making of false and disparaging statements about a competitor . . . [is] not within the area of fair and honest competition.").

Thus, at least at this stage in the proceedings, the court finds that the allegations in the third section of MGA's Complaint support a claim for "unfair competition" under the UCL.<sup>6</sup> [\*28] Accordingly, the court denies Mattel's motion to strike paragraphs 74-100, 113-114, and 118 of the Complaint.<sup>7</sup>

## 2. Request for Restitution and Disgorgement

Mattel argues that regardless, the court should strike MGA's request for restitution and disgorgement insofar as it relates to MGA's UCL claim. Mattel's argument is rejected. First, it is undisputed that MGA's request for restitution and disgorgement will remain in the Complaint regardless, because the request is potentially relevant to MGA's other claims. Compare Opp. at 21 ("[Restitution and disgorgement] [are] entirely proper [forms of relief] under the Lanham Act and California common law, and Mattel does not contest this."), with Rep. at 10 (failing to respond to this argument). Second, and more important, HN9 restitution and disgorgement are sometimes appropriate remedies under the UCL. See Korea Supply Co. v. Lockheed Martin Corp., 29 Cal. 4th 1134, 1148, 131 Cal. Rptr. 2d 29, 63 P.3d 937 (2003) (under UCL, "an individual may recover profits unfairly obtained to the extent that these profits represent monies given to the [\*29] defendant or benefits in which the plaintiff has an ownership interest."); Id. at 1144, 1148 (UCL allows for "disgorgement" of profits that is "restitutionary in nature"). See also Inline, Inc. v. Apace Moving Systems, Inc., 125 Cal. App. 4th 895, 903, 23 Cal. Rptr. 3d 216 (2005) ("The [California Supreme] [C]ourt has further specified that [t]he only nonpunitive monetary relief available . . . is the disgorgement of money that has been wrongfully obtained or, in the language of the statute, an order restor[ing] . . . money . . . which may have been acquired by means of . . . unfair competition."") (quoting Bank of the West v. Superior Court, 2 Cal. 4th 1254, 1266, 10 Cal. Rptr. 2d 538, 833 P.2d 545 (1992)). Here, MGA's UCL claim survives, and it is too early in these proceedings to determine definitively whether MGA might be entitled to restitution and disgorgement based upon its UCL-related allegations.<sup>8</sup> Accordingly, the court denies Mattel's motion to strike MGA's request for restitution and disgorgement.

### **[\*30] C. Paragraph 98 -- "LeapFrog"**

Mattel asserts that the court should strike paragraph 98 of the Complaint, which provides:

Mattel has clearly engaged in tortious, illegal and unethical behavior in its unfettered efforts to disrupt, if not destroy, MGA. Indeed, this is apparently Mattel's current *modus operandi* when it comes to "competing" in the

<sup>6</sup> Mattel attempts to avoid this result by relying upon Cel-Tech's statement that HN8 "the antitrust laws were enacted for the protection of competition, not competitors." Cel-Tech, 20 Cal. 4th at 186 (internal quotation marks omitted) (emphasis omitted) (quoting Cargill, Inc. v. Monfort of Colorado, Inc., 479 U.S. 104, 115, 93 L. Ed. 2d 427, 107 S. Ct. 484 (1986)). Although true, this statement does not aid Mattel because MGA's UCL claim does seek to protect "competition," not just "competitors." The essence of MGA's claim is that Mattel has engaged in conduct stifling fair "competition," not that competitors can only compete with Mattel (when Mattel is competing fairly) with court assistance. That MGA may benefit from fair "competition" does not imply that MGA seeks only the protection of "competitors." See Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328, 352-53, 109 L. Ed. 2d 333, 110 S. Ct. 1884 (1990) (Stevens, J., dissent) ("The antitrust laws were enacted for the protection of competition, not competitors. This proposition . . . cannot be read to deny all remedial actions by competitors. When competitors are injured by [conduct that violates the antitrust laws] rather than by the free play of market forces, the antitrust laws protect competitors precisely for the purpose of protecting competition.") (citations and quotation marks omitted). Mattel additionally argues that MGA's UCL claim fails because MGA has not alleged that Mattel's conduct harmed "consumers." However, by contending that Mattel's conduct inappropriately hindered inter-brand competition, MGA has necessarily alleged harm to consumers. See generally Amarel, 202 Cal. App. 3d at 142 (consumers benefit from "full and unrestricted competition").

<sup>7</sup> Because of this holding, the court need not address MGA's other arguments as to why these paragraphs should not be stricken.

<sup>8</sup> The court notes, however, that HN10 the UCL does not allow for an individual to recover "disgorgement of profits allegedly obtained by means of an unfair business practice . . . where [those] profits are neither money taken from a plaintiff nor funds in which the plaintiff has an ownership interest." Korea Supply Co., 29 Cal. 4th at 1140.

industry. The once immensely successful "LeapFrog" interactive learning product, for example, has apparently been one of Mattel's other recent victims.

Compl. P 98. Mattel argues that this paragraph should be stricken because MGA lacks standing to assert a UCL claim on behalf of LeapFrog and because the allegations are immaterial.

Mattel's arguments fail. First, MGA is not attempting to assert a claim on behalf of LeapFrog. Instead, MGA proffers its allegation regarding LeapFrog as an example of how Mattel treats its competition, of which MGA is a part. Therefore, MGA need not have "standing" with respect to this allegation. Moreover, at this stage of the proceedings, it would be premature to conclude that the allegation is necessarily immaterial. Accordingly, the court denies Mattel's motion to strike paragraph [\*31] 98 of the Complaint.

#### **D. Paragraph 75 -- Suing and Sending Demand Letters to Former Employees**

Finally, Mattel argues that the court should strike paragraph 75 (and related allegations in paragraph 113) of the Complaint. Paragraph 75 provides:

[W]ielding the litigation privilege as a potential shield for intimidating conduct, Mattel has sent threatening letters to several of its former employees who now work for MGA warning them not to disclose even *publicly available information* about Mattel, including the names and positions of Mattel employees. Mattel even went so far as to sue one of its former senior executives, after he had the temerity to resign and join MGA in October 2004. Not only was Mattel's lawsuit dismissed for failure to state a viable claim, but Mattel thereafter seemingly could not muster up a shred of evidence sufficient to support an amended complaint. As a result, Mattel's case against its former executive was dismissed with prejudice.

Compl. P 75 (emphasis in original). As mentioned, these allegations, while not capable of supporting MGA's trade dress claims, arguably support MGA's UCL claim. See supra Part IV.B.1. Mattel [\*32] argues that these allegations should nevertheless be stricken because: (1) MGA lacks standing under the UCL to assert such allegations; and (2) the conduct alleged in paragraph 75 is rendered actionable by California's "litigation privilege" and the Noerr-Pennington doctrine.

##### **1. Standing**

HN11 [↑] Section 17204 of the California Business and Professions Code provides that a party has standing to bring an action pursuant to the UCL if it "has suffered injury in fact and has lost money or property as a result of a violation [of the UCL]." MGA specifically alleges that as a result of Mattel's conduct, including that alleged in paragraph 75, MGA's "ability to attract, hire, and retain employees has been affected." Compl. P 100. See also id. P 113 (Mattel has . . . used its power and influence to attempt to, if not actually, intimidate and threaten MGA's current and potential employees so as to cause MGA competitive injury."). Therefore, even if it is necessary for MGA to demonstrate it has "standing" to assert the allegations in paragraph 75, MGA has adequately alleged that it "has suffered injury in fact and has lost money or property as a result" of Mattel's alleged conduct. [\*33] See Lujan v. Defenders of Wildlife, 504 U.S. 555, 561, 119 L. Ed. 2d 351, 112 S. Ct. 2130 (1992) (where 12(b) motion to dismiss is based on lack of standing, court must defer to plaintiff's factual allegations, and must "presume that general allegations embrace those specific facts that are necessary to support the claim") (quotation marks omitted). Therefore, MGA has "standing" under the UCL to assert the allegations contained in paragraph 75.

##### **2. The Litigation Privilege and the Noerr-Pennington Doctrine**

Mattel argues that regardless, the conduct alleged in paragraph 75 is actionable under California's litigation privilege and the Noerr-Pennington doctrine.

California's litigation privilege is codified at section 47(b) of the California Civil Code, which provides that HN12 [↑] "[a]privileged publication or broadcast is one made . . . in any judicial proceeding." Cal. Civ. Code § 47(b). HN13 [↑] This privilege applies to "any communication (1) made in judicial or quasi-judicial proceedings; (2) by litigants or other participants authorized by law; (3) to achieve the objects of the litigation; and (4) to have some connection or

logical relation to the action." *Silberg v. Anderson*, 50 Cal. 3d 205, 212, 266 Cal. Rptr. 638, 786 P.2d 365 (1990). [\*34]

The Noerr-Pennington doctrine is a federal court creation. Originally, it was "[t]he First Amendment aspect of antitrust law." *Freeman v. Lasky, Haas & Cohler*, 410 F.3d 1180, 1183-84 (9th Cir. 2005). The doctrine was announced in *Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 5 L. Ed. 2d 464, 81 S. Ct. 523 (1961), where the Supreme Court interpreted the Sherman Act, in view of "the right of the people . . . to petition the Government for a redress of grievances," to not cover political lobbying:

To hold that the government retains the power to act in [its] representative capacity [to make laws that operate to restrain trade] and yet hold, at the same time, that the people cannot freely inform the government of their wishes would impute to the Sherman Act a purpose to regulate, not business activity, but political activity, a purpose which would have no basis whatever in the legislative history of that Act. . . . [S]uch a construction of the Sherman Act would [also] raise important constitutional questions. The right of petition is one of the freedoms protected by the Bill of Rights, and we cannot, of course, lightly impute [\*35] to Congress an intent to invade these freedoms.

*Noerr Motor Freight, Inc.*, 365 U.S. at 137-38. [HN14](#)↑ "The doctrine extends to all three branches of government, and thus also exempts bringing a lawsuit -- that is, petitioning a court -- from antitrust liability." *Freeman*, 410 F.3d at 1183 (citing *Cal. Motor Transp. Co. v. Trucking Unlimited*, 404 U.S. 508, 510, 30 L. Ed. 2d 642, 92 S. Ct. 609 (1972)). To date, some courts have even applied this doctrine to immunize pre-litigation demand letters from lawsuits unrelated to antitrust law. See, e.g., *Directv, Inc. v. Lewis*, 2005 U.S. Dist. LEXIS 8187, No. 03-CV-6241-CJS-JWF, 2005 WL 1006030, at 5-7 (W.D.N.Y. Apr. 29, 2005).

These doctrines apply differently to MGA's allegations regarding Mattel's suing one of its former employees and its allegations regarding Mattel sending demand letters to its former employees.

#### a. The Brewer Litigation

In the second part of paragraph 95, MGA refers to a lawsuit filed by Mattel against one of its former senior executives, Ronald Brewer, who left Mattel for MGA. In that lawsuit, Mattel sought declaratory relief that certain information allegedly possessed by Brewer was confidential to Mattel [\*36] and that Brewer did not have the "ability . . . to undertake the responsibilities inherent in his new position with MGA without disclosing or using the confidential . . . [i]nformation that [he] learned while employed by Mattel." See Mot., Ex. A (*Mattel, Inc. v. Brewer*, Compl. PP 47,48).<sup>9</sup> The Los Angeles Superior Court dismissed Mattel's case against Brewer with prejudice, and the decision is currently on appeal. Mot. at 5.

Despite MGA's arguments to the contrary, its allegations regarding the Brewer litigation are rendered actionable by California's litigation privilege. The Complaint essentially asserts that the Brewer lawsuit was meritless and that Mattel instituted the suit simply [\*37] to harass Brewer and intimidate others who might consider leaving Mattel for MGA. The initiation of such a lawsuit and the statements made therein are clearly protected by the litigation privilege. See *Rubin v. Green*, 4 Cal. 4th 1187, 1195, 17 Cal. Rptr. 2d 828, 847 P.2d 1044 (1993) ("filing the complaint and subsequent pleadings in the litigation" is protected by the litigation privilege); *Abraham v. Lancaster Community Hospital*, 217 Cal. App. 3d 796, 822, 266 Cal. Rptr. 360 (1990) ("[I]t cannot be disputed that the filing of a lawsuit is a publication in the course of a judicial proceeding."); *Microsoft Corp. v. BEC Computer Co., Inc.*, 818 F. Supp. 1313, 1319 (C.D. Cal. 1992) (Kenyon, J.) ("the filing of improper or meritless pleadings . . . is privileged").

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<sup>9</sup>The court takes judicial notice of this document. See *Parrino v. FHP Inc.*, 146 F.3d 699, 706 (9th Cir. 1998) [HN15](#)↑ ("a district court ruling on a motion to dismiss may consider a document the authenticity of which is not contested, and upon which the plaintiff's complaint necessarily relies").

Thus, MGA's allegations regarding the Brewer litigation are based upon privileged conduct, and such allegations are ordered stricken from the Complaint.<sup>10</sup>

[\*38] b. Demand Letters

Paragraph 75 also includes the allegation that "Mattel has sent threatening letters to several of its former employees who now work for MGA[,] warning them not to disclose even publicly available information about Mattel, including the names and positions of Mattel employees." Compl. P 75 (emphasis in original). At least at this stage in the proceedings, neither the litigation privilege nor the Noerr-Pennington doctrine provides a basis for striking this allegation.

First, because this allegation relates to "pre-litigation conduct," the scope of the litigation privilege is narrowed. In particular, HN16<sup>11</sup> pre-litigation demand letters are "protected by the litigation privilege [only] when the statement is made in connection with a proposed litigation that is contemplated in good faith and under serious consideration." Blanchard v. DIRECTV, Inc., 123 Cal. App. 4th 903, 919, 20 Cal. Rptr. 3d 385 (2004) (quoting Aronson v. Kinsella, 58 Cal. App. 4th 254, 262, 68 Cal. Rptr. 2d 305 (1997)) (citing Silberg, 50 Cal. 3d at 212; Laffer v. Levinson, Miller, Jacobs & Phillips, 34 Cal. App. 4th 117, 124, 40 Cal. Rptr. 2d 233 (1995); Fuhrman v. California Satellite Systems, 179 Cal. App. 3d 408, 420-21, 225 Cal. Rptr. 140, 231 Cal. Rptr. 113 (1986), [\*39] overruled on other grounds by Silberg v. Anderson, 50 Cal. 3d 205, 212, 266 Cal. Rptr. 638, 786 P.2d 365 (1990)). Here, it is at least arguable that Mattel's demand letters did not meet the "good faith" requirement because they allegedly threatened to sue former employees even if the employees disclosed only "publicly available information." Cf. Herzog v. "A" Company, Inc., 138 Cal. App. 3d 656, 188 Cal. Rptr. 155 (1982) ("good faith" requirement not met when employer sends demand letter to former employee threatening suit if employee engages in conduct not barred by agreement between employer and former employee). See also Aronson v. Kinsella, 58 Cal. App. 4th 254, 270, 68 Cal. Rptr. 2d 305 (1997) (must determine whether party writing demand letter "honestly believed he had a viable legal claim"). In any event, this determination is not one that should be made on the pleadings. See, e.g., Fuhrman, 179 Cal. App. 3d at 422 (whether demand letters were sent in good faith and serious contemplation of litigation is factual question that cannot be decided on demurrer). Therefore, the litigation privilege cannot be used as a basis at this time to strike the allegations regarding Mattel's demand letters.

[\*40] Second, the Noerr-Pennington doctrine, even if applicable, does not provide a basis at this time for striking the allegations regarding Mattel's demand letters, because MGA's allegations suggest that these letters fall within the "sham" exception to the doctrine. As stated by the Ninth Circuit:

<sup>10</sup> MGA attempts to avoid this result by arguing that the Brewer litigation does not provide a "basis" for its UCL claim, but merely "evidence" of Mattel's unfair business practices. See Opp. at 20-21 (citing White v. Western Title Ins. Co., 40 Cal. 3d 870, 888, 221 Cal. Rptr. 509, 710 P.2d 309 (1985) ("[T]here is] a careful distinction between a cause of action based squarely on a privileged communication, such as an action for defamation, and one based upon an underlying course of conduct evidenced by the communication."); Stacy & Witbeck, Inc. v. City and County of San Francisco, 36 Cal. App. 4th 1074, 1091, 44 Cal. Rptr. 2d 472 (1995) ("[A]lthough **section 47, subdivision (b)**, bars certain tort causes of action predicated on a judicial statement or publication, it does not create an evidentiary privilege for those statements. Thus, as an example, those statements can be used for evidentiary purposes to determine a person's intent."); Oren Royal Oaks Venture v. Greenberg, Bernhard, Weiss & Karma, 42 Cal. 3d 1157, 232 Cal. Rptr. 567, 728 P.2d 1202 (1986) (in abuse of process action, plaintiff may use statements made during settlement negotiations in prior suit as "evidence" of defendant's improper "ulterior" purpose in initiating prior suit)). MGA, however, misrepresents the nature of its Complaint. Reading the Complaint as a whole, it is clear that the allegations in paragraph 75 provide one of the "bases" upon which MGA rests its claim that Mattel engaged in "unfair competition." The allegations in paragraph 75 are not mere "evidence" tending to show an element of some other cause of action, such as malicious prosecution or abuse of process. Indeed, MGA itself appears to admit as much in a separate portion of its opposition. See Opp. at 1-2 (describing its allegations, including those based upon the Brewer litigation, as being "at the heart of Mattel's anti-competitive behavior"). Consequently, MGA's allegations regarding the Brewer litigation are subject to the litigation privilege. See Dong v. Board of Trustees of Leland Stanford Junior University, 191 Cal. App. 3d 1572, 1594, 236 Cal. Rptr. 912 (1987) (documents subject to litigation privilege if they provide "the nuclei" for causes of action); Block v. Sacramento Clinical Labs, Inc., 131 Cal. App. 3d 386, 392-93, 182 Cal. Rptr. 438 (1982) (privilege applies where litigation-related conduct is "the actionable wrong").

**HN17**[] While Noerr-Pennington immunity is broad, it is not so broad as to cover all litigation: "Sham" petitions don't fall within the protection of the doctrine. We have recognized three circumstances when litigation might be sham:

First, if the alleged anticompetitive behavior consists of bringing a single sham lawsuit (or a small number of such suits), the antitrust plaintiff must demonstrate that the lawsuit was (1) objectively baseless, and (2) a concealed attempt to interfere with the plaintiff's business relationships.

Second, if the alleged anticompetitive behavior is the filing of a series of lawsuits, "the question is not whether any one of them has merit -- some may turn out to, just as a matter of chance -- but whether they are brought pursuant to a policy of starting legal proceedings without regard to the merits and for the purpose of injuring a market rival. [\*41]"

Finally, in the context of a judicial proceeding, if the alleged anticompetitive behavior consists of making intentional misrepresentations to the court, litigation can be deemed a sham if "a party's knowing fraud upon, or its intentional misrepresentations to, the court deprive the litigation of its legitimacy."

Freeman, 410 F.3d at 1183-84 (citations omitted).

Here, MGA's allegations suggest that the first exception is applicable: the requests in Mattel's demand letters were "objectively baseless," and the demand letters were a "concealed attempt to interfere" with MGA's business relationships. Therefore, at least at this stage in the proceedings, the court cannot say that the Noerr-Pennington doctrine, even if applicable, serves as a basis for striking MGA's allegations regarding Mattel's demand letters. Accordingly, the court denies Mattel's motion to strike MGA's allegations regarding Mattel's demand letters.

## V. CONCLUSION

For the reasons set forth above, Mattel's Motion is GRANTED in part and DENIED in part. Mattel's Motion is granted insofar as it requests that MGA's allegations regarding the Brewer litigation be stricken; otherwise, [\*42] Mattel's Motion is denied. No later than September 19, 2005, Mattel shall file an Amended Answer.

IT IS SO ORDERED.

DATED: August 25, 2005

Nora M. Manella

United States District Judge



## Mpt, Inc. v. Marathon Labels, Inc.

United States District Court for the Northern District of Ohio, Eastern Division

August 25, 2005, Decided ; August 26, 2005, Filed

CASE NO. 1:04 CV 2357

**Reporter**

2005 U.S. Dist. LEXIS 18270 \*; 2005 WL 2086069

MPT, Inc., Plaintiff, Vs. Marathon Labels, Inc., et al., Defendants.

**Subsequent History:** Motion granted by [MPT, Inc. v. Marathon Labels, Inc., 2005 U.S. Dist. LEXIS 29278 \(N.D. Ohio, Nov. 22, 2005\)](#)

**Disposition:** [\*1] Defendants Marathon Labels and Polymeric Converting's Motion for Leave of Court to Amend their Answers granted.

## Core Terms

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bad faith, infringed, Labels, counterclaims, patents, unfair competition, patent infringement, defendants', baseless, Amend, marketplace, customers, patentee, invalid, affirmative defense, motion to dismiss, motion for leave, leave to amend, patent law, cease-and-desist, communications, preempted, placards, argues, futile

## LexisNexis® Headnotes

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Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

Civil Procedure > Pleading & Practice > Pleadings > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

### [HN1](#) [down arrow] Amendment of Pleadings, Leave of Court

Under [Fed. R. Civ. P. 15\(a\)](#), leave to amend a pleading shall be freely given "when justice so requires." In determining whether to grant leave to amend, the trial court must consider several factors. Undue delay in filing, lack of notice to the opposing party, bad faith by the moving party, repeated failures to cure deficiencies by previous amendments, undue prejudice to the opposing party, and futility of amendment are all factors which may affect the decision. To deny a motion for leave to amend, a district court cannot base its decision on delay alone and, instead, must determine whether the amendment will cause significant prejudice to the nonmoving party. However, when an amendment is sought at a late stage in the litigation, there is an increased burden to show justification on the part of the party requesting the amendment. Lastly, a motion for leave to amend may be denied for futility if the trial court concludes that the pleading as amended could not withstand a motion to dismiss.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Trademark Law > ... > Unfair Competition > Federal Unfair Competition Law > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

## **HN2** [down arrow] **Inequitable Conduct, Anticompetitive Conduct**

Before a patentee may be held liable under § 43(a) of the Lanham Act, [15 U.S.C.S. § 1125\(a\)](#), for marketplace activity in support of its patent, and thus be deprived of the right to make statements about potential infringement of its patent, the marketplace activity must have been undertaken in bad faith. The "bad faith" prerequisite is a function of the interaction between the Lanham Act and patent law, and is in addition to the elements required by § 43(a) itself, as § 43 alone does not require bad faith.

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > Bad Faith

Constitutional Law > Supremacy Clause > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Torts > Business Torts > Unfair Business Practices > General Overview

## **HN3** [down arrow] **Bad Faith, Fraud & Nonuse, Bad Faith**

A state unfair competition claim based on a patentholder's marketplace activity in support of a patent is not preempted by the patent laws if the claimant can allege and ultimately prove that the patentholder acted in bad faith.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Constitutional Law > Supremacy Clause > General Overview

Torts > ... > Commercial Interference > Contracts > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > Bad Faith

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

#### [\*\*HN4\*\*](#) [down] Inequitable Conduct, Anticompetitive Conduct

State tortious interference with contractual relations claims are not preempted by the patent laws where the claims involved allegations of bad faith marketplace conduct by the patentee.

Constitutional Law > Supremacy Clause > General Overview

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Torts > Procedural Matters > Preemption > General Overview

Patent Law > Infringement Actions > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

#### [\*\*HN5\*\*](#) [down] Constitutional Law, Supremacy Clause

Federal patent law preempts state-law tort liability for a patent-holder's good faith conduct in communications asserting infringement of its patent and warning about potential litigation. State-law claims can survive federal preemption only to the extent that such claims are based on a showing of "bad faith" action in asserting infringement. Accordingly, to avoid preemption, bad faith must be alleged and ultimately proven, even if bad faith is not otherwise an element of the tort claim.

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Patent Law > ... > Defenses > Inequitable Conduct > Burdens of Proof

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Patent Law > Infringement Actions > General Overview

#### [\*\*HN6\*\*](#) [down] Defenses, Bad Faith Enforcement

Bad faith must be demonstrated by a showing of objective baselessness, i.e., clear and convincing evidence that the patentee had no reasonable basis to believe that the accused product infringed the patents at issue.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Civil Procedure > ... > Pleadings > Counterclaims > General Overview

Patent Law > Infringement Actions > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Bad Faith Enforcement

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

## **HN7** [L] Inequitable Conduct, Anticompetitive Conduct

The initiation of an infringement suit is clearly not covered by the text of § 43(a) of the Lanham Act, [15 U.S.C. § 1125\(a\)](#), while a communication to the customers of the accused infringer, in certain circumstances, may be.

**Counsel:** For MPT, Inc., Plaintiff: Kyle B. Fleming, David E. Kitchen, Baker & Hostetler, Cleveland, OH; Thomas H. Shunk, Baker & Hostetler, LLP, Cleveland, OH.

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For Marathon Labels, Inc., Counter-Claimant: Richard E. Gaum, Hahn Loeser & Parks LLP, Akron, OH.

For MPT, Inc., Counter-Defendant: Thomas H. Shunk, Baker & Hostetler, LLP, Cleveland, OH.

For Polymeric Converting LLC, Sunbelt Consulting Group, Inc., Counter-Claimants: Richard M. Klein, Christopher B. Fagan, Fay, Sharpe, Fagan, Minnich & McKee, Cleveland, OH; James V. Costigan, John F. Volpe, Kathleen A. Costigan, Hedman & Costigan, New York, NY.

**Judges:** PATRICIA A. GAUGHAN, United States District Judge.

**Opinion by:** PATRICIA A. GAUGHAN

## **Opinion**

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### **Memorandum of Opinion & Order**

#### **Introduction**

This matter is before the Court upon the Motion and Memorandum of Defendants Marathon Labels and Polymeric Converting for [\*2] Leave of Court to Amend their Answers (Doc. 50). The issue presently before the Court is whether defendants should be permitted to amend their Answers to assert additional defenses and counterclaims relating to a federal claim of unfair competition under the Lanham Act, [15 U.S.C. § 1125\(a\)](#), as well as state law claims for unfair competition and tortious interference with contract and business relations. For the following reasons, the Court grants defendants' Motion.

#### **Facts**

On November 29, 2004, plaintiff MPT, Inc. ("MPT") filed a complaint in this Court against defendant Marathon Labels, Inc., ("Marathon Labels") alleging infringement of its Patent No. 5,417,790 ("the '790 patent") and Patent No. RE 37, 164 E ("the '164 patent").<sup>1</sup> Defendant Marathon Labels filed its Answer on February 1, 2005, in which it asserted various affirmative defenses and alleged two counterclaims against plaintiff MPT. These counterclaims sought a declaratory judgment that (1) defendant Marathon Labels "has not infringed, and is not infringing,

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The '790 and '164 patents relate to label systems for reusable containers. The patents were issued by the United States Patent and Trademark Office to Robert J. Petrou on May 23, 1995 and May 8, 2001, respectively. Plaintiff MPT is the assignee of all rights in both the '790 and '164 patents.

contributorily infringing, or inducing infringement of any claim of the '790 and '164 patents;" and (2) that the '790 and '164 [\*3] patents are invalid and/or unenforceable under federal patent laws.

Thereafter, on April 8, 2005, plaintiff MPT filed its First Amended Complaint for Patent Infringement. This Amended Complaint also alleged infringement of the '790 and '164 patents, and added as defendants the following parties: Marathon Durable Labeling Systems LLC ("MDLS"), Polymeric Converting LLC ("Polymeric"), and Sunbelt Consulting Group, Inc. ("Sunbelt"). In addition, the First Amended Complaint alleged that Marathon Labels, MDLS, Polymeric and Sunbelt are jointly engaged in the manufacture and/or marketing of placards and labels for use in labeling reusable containers ("Reusable Labels"), and are "thereby jointly engaged in inducing purchasers [\*4] of the Reusable Labels in wrongfully practicing the methods of the" '790 and '164 patents. (First Am. Compl. at P7).

Defendants Marathon Labels and Polymeric filed their Answers on April 18, 2005 and April 21, 2005, respectively. As before, these Answers asserted various affirmative defenses and sought declaratory judgments of non-infringement and of the invalidity of the '790 and '164 patents.

Meanwhile, defendants claim that, by letter dated April 21, 2005, Seaway Bolt and Specials Corp. (a customer of defendant Marathon Labels) (hereinafter "Seaway") returned a purchase of labels, which had been supplied by defendant Polymeric. The basis for returning the purchase was an April 11, 2005 letter from counsel for plaintiff MPT to Seaway. This letter provides, in part, as follows:

You should know that MPT, Inc., which licenses The Kennedy Group to make and sell placards for container re-labeling applications, is the owner of U.S. Patent 5,417,790 and U.S. Patent Re. 37, 164, and is currently suing Marathon Labels, Inc., for patent infringement based on Marathon Labels' sale of its Smart Surface Placards.

If your company purchases placards from Marathon Labels and uses the placards [\*5] in the way described in the patents, it may be infringing on the patented process.

See Exh. C to defendants' Motion to Amend Answers.

In response to this letter, defendants Marathon Labels and Polymeric filed the instant Motion for Leave of Court to Amend Their Answers. As discussed below, in this Motion, these defendants seek leave to assert additional counterclaims for unfair competition under [Section 43\(a\) of the Lanham Act](#), as well as state law claims for unfair competition and tortious interference with contract and business relations. Plaintiff MPT filed a Brief in Opposition, and defendants have filed a Reply in Support.

### **Standard of Review**

**HN1** [↑] Under [Federal Rule of Civil Procedure 15\(a\)](#), leave to amend a pleading shall be freely given "when justice so requires." [Fed. R. Civ. Pro. 15\(a\)](#); See also [Wade v. Knoxville Utilities Board, 259 F.3d 452 \(6th Cir. 2001\)](#). In determining whether to grant leave to amend, this Court must consider several factors. "Undue delay in filing, lack of notice to the opposing party, bad faith by the moving party, repeated failures to cure [\*6] deficiencies by previous amendments, undue prejudice to the opposing party, and futility of amendment are all factors which may affect the decision." [Id. at 458](#). To deny a motion for leave to amend, a district court cannot base its decision on delay alone and, instead, must determine whether the amendment will cause significant prejudice to the nonmoving party. [Duggins v. Steak 'N Shake, 195 F.3d 828, 834 \(6th Cir. 1999\)](#). However, when an amendment is sought at a late stage in the litigation, there is an increased burden to show justification on the part of the party requesting the amendment. [Wade, 259 F.3d at 459](#); See also [Duggins, 195 F.3d at 834](#). Lastly, a motion for leave to amend may be denied for futility "if the court concludes that the pleading as amended could not withstand a motion to dismiss." [Martin v. Associated Truck Lines, Inc., 801 F.2d 246, 249 \(6th Cir. 1986\)](#). See also [Midkiff v. Adams County Regional Water District, 409 F.3d 758, 767 \(6th Cir. 2005\)](#).

### **Discussion**

Defendants Marathon Labels and Polymeric argue that they should be granted leave to amend their [\*7] Answers in response to plaintiff MPT's April 11, 2005 cease-and-desist letter for the following reasons. First, defendants argue that there has been no undue delay since their Motion to Amend was filed less than two months after the Court's April 8, 2005 Pleading Amendment date and the filing of plaintiff's Amended Complaint. Further, defendants maintain that plaintiff cannot claim prejudice since "this action is in its infancy." (Motion to Amend at 5).<sup>2</sup> In addition, defendants note that their proposed amendment is motivated by plaintiff's conduct in sending its cease-and-desist letter, and not by any bad faith or delay on the part of defendants.

[\*8] Lastly, defendants argue that the Federal Circuit has recognized the viability of the federal and state common law claims defendants now seek to assert and, thus, their proposed amendments are not futile. In support of this argument, defendants rely principally on *Zenith Electronics Corp. v. Exzec, Inc.*, 182 F.3d 1340 (Fed. Cir. 1999). In that case, plaintiffs Zenith Electronics ("Zenith") and Elo Touchsystems, Inc. ("Elo Touch") sued defendant Exzec, Inc. for patent infringement. Defendant Exzec then asserted counterclaims against plaintiffs for unfair competition under both § 43(a) of the Lanham Act and Illinois common law. The basis for Exzec's counterclaims was its allegation that Elo Touch had falsely stated to potential customers of Exzec that Exzec's product infringed plaintiffs' patents and that Exzec could not manufacture or sell a non-infringing product. Exzec further alleged that Elo Touch's "bad faith" conduct in so communicating with Exzec's potential customers was done willfully and with the intent to deceive. Zenith, 182 F.3d at 1343-1344.

Elo Touch moved to dismiss pursuant to Fed. R. Civ. Proc. 12(b)(6) [\*9]. The district court denied Elo Touch's motion, finding that Exzec's pleading adequately alleged viable claims for unfair competition under both the Lanham Act and Illinois common law. Elo Touch moved to reconsider, arguing that Exzec's unfair competition claims were pre-empted by federal patent and/or antitrust law. The district court denied Elo Touch's motion for reconsideration, but granted its alternative motion to certify the court's order for immediate appeal pursuant to 28 U.S.C. § 1292(b).

On immediate appeal, the Federal Circuit held as follows. First, with regard to Exzec's Lanham Act unfair competition claim, the court found (after a detailed discussion and analysis of its prior precedent) that HN2 [↑] "before a patentee may be held liable under § 43(a) of the Lanham Act for marketplace activity in support of its patent, and thus be deprived of the right to make statements about potential infringement of its patent, the marketplace activity must have been undertaken in bad faith." Id. at 1353. This "bad faith" prerequisite, the court noted, is "a function of the interaction between the Lanham Act and patent law, and is in addition to [\*10] the elements required by § 43(a) itself, as § 43 alone does not require bad faith." Id.

Applying this conclusion to the facts of the case before it, the court then found that both of the allegedly false statements at issue (i.e., that Exzec's product infringed plaintiffs' patents and that Exzec could not manufacture a non-infringing product) "if made in bad faith, can be reached by § 43(a) (assuming the elements of such a claim are otherwise made out) without conflicting with the patent or antitrust laws." Id. at 1354.

With regard to Exzec's state law claim, the court similarly found that HN3 [↑] a state unfair competition claim based on a patentholder's marketplace activity in support of a patent is not preempted by the patent laws if the claimant can allege and ultimately prove that the patentholder acted in bad faith. Id. at 1355. This conclusion was based in large part on the court's previous decisions in *Dow Chemical v. Exxon Corp.*, 139 F.3d 1470 (Fed. Cir. 1998) and *Hunter Douglas, Inc. v. Harmonic Design, Inc.*, 153 F.3d 1318 (Fed. Cir. 1998) overruled on other grounds by *Midwest Industries, Inc. v. Karavan Trailers, Inc.*, 175 F.3d 1356 (Fed. Cir. 1999), [\*11] in which the court held that HN4 [↑] state tortious interference with contractual relations claims were not preempted by the patent laws where the claims involved allegations of bad faith marketplace conduct by the patentee. On this basis, the court found that both of the allegedly false statements at issue in the case before it, if made in bad faith, could state a claim for unfair competition under Illinois law.

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<sup>2</sup> As of the date of the filing of defendants' Motion, the non-expert discovery and Markman brief deadline was September 1, 2005, and the expert discovery and dispositive motion deadline was January 15, 2006. On August 24, 2005, however, this Court granted the parties' joint motion to extend the discovery deadlines by forty-five days. Thus, although the Court does not agree that "this action is in its infancy," the Court does agree that discovery has not yet been concluded.

Finally, the court noted that "what constitutes bad faith remains to be determined on a case by case basis." *Id. at 1354*. However, the court did note that, "obviously, if the patentee knows that the patent is invalid, unenforceable, or not infringed, yet represents to the marketplace that a competitor is infringing the patent, a clear case of bad faith representations is made out." *Id.*

Based on the above, the Federal Circuit affirmed the district court's order denying Elo Touch's [Rule 12\(b\)\(6\)](#) motion to dismiss Exzec's federal and state law unfair competition claims.<sup>3</sup>

**[\*12]** Pursuant to *Zenith*, defendants Marathon Labels and Polymeric argue herein that their proposed amended counterclaims are not futile since they specifically allege that plaintiff MPT made false representations of patent infringement **in bad faith** when it sent its April 11, 2005 cease-and-desist letter to Seaway.<sup>4</sup> See Marathon Labels, Inc.'s Amended Answer to MPT's First Amended Complaint and Counterclaims at PP37-39; Amended Answer, Affirmative Defenses and Counterclaims of Defendant Polymeric Converting LLC at PP35-38.<sup>5</sup> Thus, defendants claim that their proposed federal and state common law unfair competition claims are not preempted and are adequately pled as a matter of law.

**[\*13]** In response, plaintiff MPT argues that defendants' Motion for Leave should be denied "because the causes of action sought to be added by them are, on their face, not properly assertable in this action and will only serve to add expense to the parties." (Brief in Opp. at 1). Specifically, MPT argues that the "bad faith" test set forth in *Zenith* is no longer the test for determining the viability of federal and state common law unfair competition counterclaims in the context of a patent infringement suit. Rather, MPT maintains that, in the recent case of [Globetrotter Software, Inc. v. Elan Computer Group, Inc.](#), 362 F.3d 1367 (Fed. Cir. 2004), the Federal Circuit adopted an "objectively baseless" standard for such claims, which requires a showing that the patentee had no reasonable basis to believe that the accused product infringed the patents at issue. MPT then argues that defendants herein fail to plead that the cease-and-desist letter at issue was objectively baseless, and that no facts are pled which support such a claim. Moreover, even if the Court were to find that "bad faith" is the proper test, MPT maintains that defendants plead no facts which suggest in **[\*14]** what way MPT's assertion of its claims to Seaway constitutes "bad faith." Thus, MPT argues that the Federal Circuit's decision in *Globetrotter* prohibits defendants' federal and state law unfair competition claims as a matter of law and, therefore, defendants' Motion for Leave should be denied.<sup>6</sup>

In *Globetrotter*, plaintiff Globetrotter sued Elan Computer Group ("Elan") and its CEO Ken Greer for patent infringement. Defendant Greer then asserted state law counterclaims for tortious interference and unfair competition based on the following circumstances. Greer claimed that Rainbow Technologies ("Rainbow") was negotiating to purchase all the outstanding shares of Elan for a price **[\*15]** of \$ 4,000,000. While these negotiations were pending, plaintiff Globetrotter sent two letters and an e-mail to Rainbow, alleging infringement of Globetrotter's patents by Elan. Defendant Greer alleged that Globetrotter in bad faith notified Rainbow of alleged patent infringement solely to cause Rainbow to abandon the planned purchase, which Rainbow did, with the result that Rainbow later acquired Elan for a much lower price. [Globetrotter](#), 362 F.3d at 1370. The district court granted

<sup>3</sup> In so doing, the circuit court noted that the district court's determination that Exzec had adequately pled bad faith was not before it.

<sup>4</sup>

In their Motion, defendants assert that MPT's cease-and-desist letter was sent in bad faith because the accused products do not, in fact, infringe the '790 and '164 patents. Specifically, defendants claim that the patents at issue (1) are invalid over prior art not considered by the U.S. PTO and (2) only claim methods of using the products. (Motion at 3).

<sup>5</sup> Marathon Labels and Polymeric's proposed Amended Answers and Counterclaims are attached as Exhibits A and B to defendants' Motion for Leave to Amend.

<sup>6</sup> Significantly, MPT does not argue that leave to amend should be denied on grounds of undue delay and/or prejudice. Further, MPT does not argue that defendants' proposed counterclaims fail to adequately allege the specific elements of an unfair competition claim under either [§ 43\(a\) of the Lanham Act](#) or Ohio common law.

summary judgment in Globetrotter's favor with respect to defendant Greer's state law counterclaims, and Greer appealed.

The Federal Circuit began its analysis by reaffirming the "bad faith" standard announced in *Zenith*:

We have held that [HNS](#) federal patent law preempts state-law tort liability for a patent-holder's good faith conduct in communications asserting infringement of its patent and warning about potential litigation. See e.g. [\*Zenith Elecs. Corp. v. Exzec, Inc.\*, 182 F.3d 1340, 1355 \(Fed. Cir. 1999\)](#). State-law claims such as Greer's can survive federal preemption only to the extent that such claims are based on a showing of 'bad faith' action in asserting [\*16] infringement. *Id.* Accordingly, to avoid preemption, 'bad faith must be alleged and ultimately proven, even if bad faith is not otherwise an element of the tort claim.' *Id.*

[\*Globetrotter\*, 362 F.3d at 1374](#). The court then noted that Greer endeavored to show bad faith only through attempts to demonstrate **subjective** bad faith on Globetrotter's part. *Id. at 1375*. However, he had "made no effort to establish that the claims asserted by Globetrotter with respect to the [patents at issue] were objectively baseless, either because those patents were obviously invalid or plainly not infringed." *Id.* Thus, the court framed the issue before it as "whether the bad faith standard of *Zenith* can be satisfied in the absence of a showing that the claims asserted were objectively baseless." *Id.*

After a detailed analysis, the court determined that Zenith's bad faith standard required a showing of objective baselessness in the context of state law claims based on pre-litigation communications alleging patent infringement. Specifically, the court found that, to show bad faith, a claimant must offer clear and convincing evidence that the [\*17] patentee had no reasonable basis to believe that the accused infringing product infringed the patents at issue. *Id. at 1377*. See also [\*Golan v. Pingel Enter., Inc.\*, 310 F.3d 1360 \(Fed. Cir. 2002\)](#). Because defendant Greer had "not even attempted to make such a showing here," the court affirmed the district court's granting of summary judgment in Globetrotter's favor with respect to Greer's state law counterclaims. *Id.*

Based on the above, the Court rejects plaintiff MPT's argument that "bad faith is not really the test" in evaluating the viability of federal and state common law unfair competition claims based on pre-litigation communications alleging patent infringement. As set forth above, [\*Globetrotter\*](#) expressly discusses and applies Zenith's bad faith test. Nowhere in *Globetrotter* does the Federal Circuit overrule, vacate, or even question that test. Rather, *Globetrotter* elaborates on the showing necessary to satisfy Zenith's bad faith test in the context of state common law claims based on pre-litigation communications alleging patent infringement. Specifically, the *Globetrotter* court explains that, in this context, [HNS](#) "bad faith" [\*18] must be demonstrated by a showing of objective baselessness, i.e., clear and convincing evidence that the patentee had no reasonable basis to believe that the accused product infringed the patents at issue.

Notably, *Globetrotter* discusses and applies the "objectively baseless" requirement in the summary judgment context; i.e., the court determined that the defendant therein had failed to offer sufficient evidence of objective baselessness to survive summary judgment. However, as defendants herein correctly note, *Globetrotter* did not involve (and does not address) the issue of the nature and quality of the allegations that must be pled with regard to this issue in order to survive a motion to dismiss under [\*Fed. R. Civ. Proc. 12\(b\)\(6\)\*](#). As this is essentially the issue before the Court herein,<sup>7</sup> the Court concludes that *Globetrotter* does not require a finding herein that defendants' proposed Amendments fail to state a claim as a matter of law.

[\*19] To the contrary, the Court finds that defendants have adequately pled "bad faith" sufficient to survive a [\*12\(b\)\(6\)\*](#) motion to dismiss and, thus, it would not be futile to allow defendants leave to amend their Answer to assert the federal and state counterclaims at issue herein. Defendants' proposed Answers and Counterclaims specifically discuss the April 11, 2005 cease-and-desist letter sent by MPT to Seaway herein; allege that that letter makes false representations of patent infringement; and further allege that these representations were made in bad

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<sup>7</sup> This is the case because MPT is essentially arguing that defendants' motion for leave should be denied on the grounds that defendants' proposed federal and state law unfair competition claims are not "properly assertable" as a matter of law and, thus, it would be futile to allow amendment.

faith. See Marathon Labels, Inc.'s Amended Answer to MPT's First Amended Complaint and Counterclaims at PP37-39; Amended Answer, Affirmative Defenses and Counterclaims of Defendant Polymeric Converting LLC at PP35-38. Moreover, defendants specifically assert counterclaims seeking a declaratory judgment that the patents at issue herein are invalid, void and/or unenforceable. See Marathon Labels, Inc.'s Amended Answer to MPT's First Amended Complaint and Counterclaims at P35; Amended Answer, Affirmative Defenses and Counterclaims of Defendant Polymeric Converting LLC at P33.

While plaintiff MPT is correct that an eventual finding of invalidity [\*20] or unenforceability may not in and of itself necessarily demonstrate objective baselessness, the Court finds that defendants' allegations, taken as a whole, are sufficient at this stage in the litigation to satisfy the "bad faith" requirement set forth in *Zenith*. Whether defendants will ultimately be able to demonstrate by clear and convincing evidence that MPT's communication to Seaway was "objectively baseless" is another matter, one that is not before the Court today. Accordingly, the Court rejects plaintiff MPT's argument on this issue.

Finally, MPT argues that defendants' Motion for Leave should be denied because there is no legal basis for the assertion of a federal unfair competition claim based on the allegedly fraudulent procurement of a patent where such a claim is premised solely on a patentee's conduct of sending a cease and desist letter to a customer of an alleged infringer.

The Court finds that this argument is without merit. In *Zenith*, the Federal Circuit acknowledged prior precedent which explained that "there is no legal basis for a holding that inequitable conduct, or the assertion of a patent procured through inequitable conduct, constitutes unfair competition" [\*21] under [§ 43\(a\) of the Lanham Act](#). [Zenith, 182 F.3d at 1348](#) (discussing [Pro-Mold and Tool Co. v. Great Lakes Plastics, Inc., 75 F.3d 1568 \(Fed. Cir. 1996\)](#)). However, the court then noted that the federal unfair competition claim at issue in *Zenith* was not premised on the filing of a patent infringement suit based on alleged inequitable conduct but, instead, was "based on alleged marketplace statements, i.e., the alleged Elo Touch statements to potential Exzec customers that Exzec's product is infringing. . ." [Id. at 1349](#). This difference, the *Zenith* court held, was critical because [HN7](#) [↑] "the initiation of an infringement suit is clearly not covered by the text of [§ 43\(a\)](#), while a communication to the customers of the accused infringer, in certain circumstances, may be." *Id.*

In the instant case, defendants' proposed federal unfair competition counterclaim is not premised upon the filing of a patent infringement suit based on inequitable conduct. Rather, as was the case in *Zenith*, the basis of defendants' proposed counterclaim is an allegedly bad faith marketplace statement, i.e., MPT's statement to Seaway (a customer of defendants) that [\*22] defendants' product is infringing MPT's patents. Thus, the instant case falls squarely within the circumstances identified by *Zenith* which may support a claim under [§ 43\(a\)](#). Accordingly, the Court rejects plaintiff's argument on this issue.

Accordingly, for the reasons set forth above and in light of the fact that plaintiff MPT does not oppose defendants' arguments regarding the lack of undue delay and prejudice, the Court grants defendants Marathon Labels and Polymeric Converting's Motion for Leave of Court to Amend their Answers.

IT IS SO ORDERED.

PATRICIA A. GAUGHAN

United States District Judge

Dated: 8/25/05



## *Reifert v. S. Cent. Wis. MLS Corp.*

United States District Court for the Western District of Wisconsin

August 25, 2005, Decided

04-C-969-S

### **Reporter**

2005 U.S. Dist. LEXIS 23431 \*; 2005-2 Trade Cas. (CCH) P74,919

JAY REIFERT, Plaintiff, v. SOUTH CENTRAL WISCONSIN MLS CORPORATION, REALTORS ASSOCIATION OF SOUTH CENTRAL WISCONSIN, INC., ROBERT L. COURTER, SUSAN MATHEWS, DAVID STARK, ROBERT WEBER, THOMAS BUNBURY, MAURICE W. HILL, PETER SVEUM, MARSHALL ZWYGART and DAVID MCGRATH, Defendants.

**Subsequent History:** Affirmed by [\*Reifert v. S. Cent. Wis. MLS Corp., 2006 U.S. App. LEXIS 14327 \(7th Cir. Wis., June 12, 2006\)\*](#)

**Prior History:** [\*Reifert v. S. Cent. Wis. MLS Corp., 2005 U.S. Dist. LEXIS 9741 \(W.D. Wis., May 20, 2005\)\*](#)

## **Core Terms**

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membership, associations, real estate professional, substitutes, join, summary judgment, tie, buyer, multiple listing service, brokers, organizations, foreclosed, markets, south central, anti-competitive, commerce, provide a service, tied product, annual

## **LexisNexis® Headnotes**

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Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule

### **HN1[] Tying Arrangements, Per Se Rule**

A per se tying violation requires proof of four elements: (1) a tying arrangement between two distinct products or services, (2) sufficient market power in the tying market to restrain free competition in the tied product market, (3) a substantial effect on interstate commerce, (4) the tying company has an economic interest in the sales of the tied product.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

### **HN2[] Summary Judgment, Entitlement as Matter of Law**

Summary judgment is appropriate when, after both parties have the opportunity to submit evidence in support of their respective positions and the Court has reviewed such evidence in the light most favorable to the nonmovant, there remains no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. [Fed.](#)

R. Civ. P. 56(c). A fact is material only if it might affect the outcome of the suit under the governing law. Disputes over unnecessary or irrelevant facts will not preclude summary judgment. A factual issue is genuine only if the evidence is such that a reasonable factfinder, applying the appropriate evidentiary standard of proof, could return a verdict for the nonmoving party.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

### HN3 **Summary Judgment, Burdens of Proof**

Under Fed. R. Civ. P. 56(e) it is the obligation of the nonmoving party to set forth specific facts showing that there is a genuine issue for trial.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule

### HN4 **Tying Arrangements, Per Se Rule**

A tying arrangement is a violation of antitrust law only if a substantial volume of commerce is foreclosed by the tie. Similarly, when a purchaser is "forced" to buy a product he would have otherwise bought even from another in the tied-product market, there can be no adverse impact on competition because no portion of the market which would otherwise have been available to other sellers has been foreclosed.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule

### HN5 **Tying Arrangements, Per Se Rule**

Merely establishing that customers purchased an unwanted product does not establish foreclosure of competition. When there are no rival sellers of a tied product, then the alleged tie-in might affect a substantial volume of commerce in the tied product and yet not foreclose anyone.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule

Evidence > Burdens of Proof > Allocation

### HN6 **Tying Arrangements, Per Se Rule**

In the context of tying arrangements, services are in the same market when they are good substitutes for one another. That is, when there is interchangeability of use or the cross elasticity of demand between the product and the substitutes for it. A plaintiff bears the burden to prove by econometric evidence that the products are good substitutes. Observing things that to the untutored eye seem to be substitutes need not mean they are good substitutes.

Civil Procedure > Discovery & Disclosure > Discovery > Misconduct During Discovery

### HN7 **Discovery, Misconduct During Discovery**

It is inappropriate to introduce expert testimony on an element of a claim under the guise of "rebuttal" simply because a defendant has denied the existence of the element. Under such circumstances exclusion is mandated by [Fed. R. Civ. P. 37\(c\)\(1\)](#) unless the delay was harmless.

Antitrust & Trade Law > ... > Per Se Rule & Rule of Reason > Practices Governed by Per Se Rule > Boycotts

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule

## **HN8** [down arrow] Practices Governed by Per Se Rule, Boycotts

To sustain a group boycott claim, a plaintiff must demonstrate that a tie-in requirement has an adverse impact on competition in the relevant market.

**Counsel:** [\*1] For JAY REIFERT, Plaintiffs: DAVID BARRY, STEVEN FINLEY.

For SOUTH CENTRAL WISCONSIN MLS CORPORATION, REALTORS ASSOCIATION OF SOUTH CENTRAL WISCONSIN, INC., ROBERT L. COURTER, SUSAN MATHEWS, DAVID STARK, ROBERT WEBER, THOMAS BUNBURY, MAURICE W. HILL, PETER SVEUM, MARSHALL ZWYGART, DAVID MCGRATH, Defendants: BRADY C. WILLIAMSON, LA FOLLETTE, GODFREY & KAHN, S.C., MADISON, WI.

**Judges:** JOHN C. SHABAZ, District Judge.

**Opinion by:** JOHN C. SHABAZ

## **Opinion**

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### MEMORANDUM AND ORDER

Plaintiff Jay Reifert commenced this anti-trust action alleging that defendant South Central Wisconsin MLS Corp. ("SCWMLS") unlawfully ties the sale of its services to the purchase of services from its corporate parent, defendant Realtors Association of South Central Wisconsin, Inc. ("Realtors"). Plaintiff also alleges that conditioning access to MLS services on membership in Realtors is an unlawful group boycott. Plaintiff named as defendants the individual directors of SCWMLS (collectively, "individual defendants"). Jurisdiction is based on [28 U.S.C. § 1331](#). The matter is presently before the Court on cross motions for summary judgment. The following is a summary of relevant undisputed facts.

### FACTS

[\*2] Defendant Realtors is a real estate professionals trade association and the owner of 100% of SCWMLS' stock. It offers services to its members including arbitration and mediation, enforcement of a code of ethics, education courses, professional recognition, referral programs, contract forms, legal information, conventions, publications, lobbying, website, and social functions. As a condition of membership Realtors requires members to join the Wisconsin Association of Realtors ("WAR") and the National Association of Realtors ("NAR"). NAR offers additional services including use of the "Realtors" trademark, an annual conference, a magazine and membership discounts. Defendant Realtors generally accepts as a member any licensed real estate professional who agrees to abide by the NAR code of ethics and pays the fees.

In 2005, annual fees to join all three associations are \$ 441. Realtor dues are established by members who are elected to the board of directors. Dues are set solely to cover anticipated cost of operations and there is no attempt to make a profit. On March 18, 2005 RASCW had 2419 members, including 2306 real estate licensees and 113 appraisers.

Defendant SCWMLS operates a [\*3] multiple listing service which includes a computerized data base of homes and properties for sale in south central Wisconsin. To participate in the multiple listing service members must pay \$ 90 per quarter. Fees are set by members elected to the board of directors. Fees are set solely to cover anticipated cost of operations and there is no attempt to make a profit. Licensed real estate brokers who are members of any local association of Realtors may participate in the SCWMLS multiple listing service. A high percentage of broker represented residential property sold in south central Wisconsin is listed in defendant's MLS. On March 18, 2005 only 84 of the 2306 real estate professionals who were Realtor members did not use SCWMLS. On March 18, 2005 SCWMLS gave access to 331 members of local Realtor associations other than defendant Realtors. SCWMLS operates the only multiple listing service primarily within Dane, Sauk and Columbia Counties.

Plaintiff is a licensed real estate broker in south central Wisconsin and the principal of Excel Exclusive Buyer Agency since 1997. He has been a member of Realtors and a participant in SCWMLS since 1988. He wants to continue his participation in [\*4] SCWMLS but does not want to continue his membership in Realtors. He has continued his membership in Realtors solely to gain access to the multiple listing service.

According to a survey by plaintiff's expert Riddle, between 19 and 24% of Dane county SCWMLS users would not join Realtors if they were not required to join to gain access to the multiple listing service. In Massachusetts and Alaska where multiple listing service access does not require membership in a local Realtors association more than 20% of MLS users do not belong to a Realtors association.

The National Association of Exclusive Buyer Agents ("NAEBA"), Colorado Exclusive Buyer Agents Association ("CEBAA"), and Massachusetts Association of Buyers Agents ("MABA") are associations of real estate professionals who are exclusive buyer agents. Plaintiff is a member of NAEBA, which offers services specific to representations of buyers. He knows of only one other exclusive buyer agent in Wisconsin eligible to join. CEBAA and MABA offer membership in Colorado and Massachusetts, respectively.

The Appraisal Institute ("AI"), National Association of Independent Fee Appraisers ("NAIFA"), and National Association of Real Estate [\*5] Appraisers ("NAREA") are associations of professional real estate appraisers. They offer certifications, professional standards, education, appraisal databases, software, insurance, legislative monitoring, membership directories, conferences and commercial discounts. Annual membership fees for AI are \$ 740. AI Membership requires payment of local chapter dues which are \$ 110 in Wisconsin. NAIFA dues are \$ 400 per year. NAREA dues are \$ 215 per year.

The Asian Real Estate Agent Association ("AREAA"), Chinese Real Estate Association of America ("CREAA"), Chinese American Real Estate Professional Association ("CAREPA") and the National Association of Hispanic Real Estate Professionals ("NAHREP") are associations of real estate professionals which promote the advancement and interests of ethnic communities. They offer networking, education, websites, lobbying, information resources and community service events. CREAA and CAREPA are headquartered and hold meetings in California. CAREPA is supported by the California Association of Realtors and NAR. Annual dues for these organizations are as follows: AREAA \$ 100, CREAA \$ 30, CAREPA \$ 100, NAHREP \$ 99.

The National Association of Independent [\*6] Real Estate Brokers ("NAIREB") is open exclusively to brokers who are not affiliated with a franchised real estate company. NAIREB offers referrals, education networking and a magazine. It encourages members to join Realtor associations. NAIREB annual dues are \$ 79.

## MEMORANDUM

**HN1** A per se tying violation requires proof of four elements: (1) a tying arrangement between two distinct products or services, (2) sufficient market power in the tying market to restrain free competition in the tied product market, (3) a substantial effect on interstate commerce, (4) the tying company has an economic interest in the sales of the tied product. [Carl Sandburg Village Ass'n No. 1 v. First Condominium Development Co., 758 F.2d 203, 207 \(7th Cir. 1985\)](#). Plaintiff argues that each of the elements has been established as a matter of law. Defendants contend that plaintiff has failed as a matter of law to adequately establish the third or fourth elements and that

factual disputes preclude summary judgment on the other elements. Additionally, defendants seek summary judgment based on a statute of limitations defense and the absence of antitrust injury.

**HN2** Summary judgment is appropriate [\*7] when, after both parties have the opportunity to submit evidence in support of their respective positions and the Court has reviewed such evidence in the light most favorable to the nonmovant, there remains no genuine issue of material fact and the moving party is entitled to judgment as a matter of law. *Rule 56(c), Fed. R. Civ. P.* A fact is material only if it might affect the outcome of the suit under the governing law. Disputes over unnecessary or irrelevant facts will not preclude summary judgment. A factual issue is genuine only if the evidence is such that a reasonable factfinder, applying the appropriate evidentiary standard of proof, could return a verdict for the nonmoving party. *Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 254, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986).* **HN3** Under *Rule 56(e)* it is the obligation of the nonmoving party to set forth specific facts showing that there is a genuine issue for trial.

Viewing the facts and drawing inferences most favorable to plaintiff, there is insufficient evidence for a fact finder to find that a tie between the defendant's multiple listing service and Realtor membership has had an effect on interstate commerce as that element has been defined by [\*8] the Supreme Court. **HN4** A tying arrangement is a violation of **antitrust law** only if a substantial volume of commerce is foreclosed by the tie. *Jefferson Parish Hospital District No. 2 v. Hyde, 466 U.S. 2, 16, 80 L. Ed. 2d 2, 104 S. Ct. 1551 (1984)*. "Similarly, when a purchaser is "forced" to buy a product he would have otherwise bought even from another in the tied-product market, there can be no adverse impact on competition because no portion of the market which would otherwise have been available to other sellers has been foreclosed." *Id.*

Two courts of appeal have considered this requirement in the context of a tie between MLS access and Realtor association membership. In *Wells Real Estate, Inc. v. Greater Lowell Board of Realtors, 850 F.2d 803, 815 (1st Cir. 1988)* the Court upheld a directed verdict dismissing the claim, reasoning as follows:

However, Wells' action is indeed fatally affected by the excerpt from *Hyde* quoted above. Wells has failed to demonstrate the slightest market for membership in real estate boards that might have been affected by the defendants' alleged tying arrangement. There is no evidence that any other broker would have "purchased" membership [\*9] in any other board but for the power exerted by the lure of the defendants' MLS. There is no evidence that a substantial volume of "commerce" in board membership was foreclosed by the tie-in.

In contrast, the Eleventh Circuit found a substantial effect on commerce resulting from an MLS-Realtor board tie. *Thompson v. Metropolitan Multi-List, Inc., 934 F.2d 1566 (11th Cir. 1991)*. One of the plaintiffs in *Thompson*, Empire Real Estate Board, provided services similar to the defendant real estate board. Empire was established in 1939 to serve African American real estate professionals at a time when the local Realtor association excluded them. Both boards continue to exist and to provide a similar range of services to members. Evidence established that 400 members of Metropolitan would have been members of Empire but for the MLS-Realtor board tie. The Court found a substantial foreclosure of competition based on the facts.

The issue before this Court is whether plaintiff has brought forth sufficient evidence from which a fact finder could conclude that competition in the south central Wisconsin real estate services market has been foreclosed by the SCWMLS tie to [\*10] defendant Realtors. In an effort to meet its burden plaintiff has presented survey evidence from Wisconsin and statistical analysis from other markets, that supports the finding fewer real estate professionals would join defendant Realtors in the absence of the tie. This evidence suggests that about 20% of Realtor members would not join if they could obtain MLS services without membership. The law is clear, however, that **HN5** merely establishing that customers purchased an unwanted product does not establish foreclosure of competition. *Jefferson Parish, 466 U.S. at 16*. "When there are no rival sellers of the tied product, then the alleged tie-in might affect a substantial volume of commerce in the tied product and yet not foreclose anyone." 9 Phillip A. Areeda, et. al., **Antitrust Law**, P 1723 (2d ed. 2004).

In an effort to demonstrate foreclosure plaintiff has produced a laundry list of entities that he asserts are competitors in the market for the services provided by defendant Realtors. However, examination of the undisputed facts about these entities and the related expert report does not suggest that they are in the same product market with

defendant Realtors. While [\*11] it is true that there is superficial overlap in the offerings of these associations - conventions, websites, education, publications, lobbying - these similarities do little to establish that any are competing in the same product market with Realtors. Virtually all professional organizations offer such services while undoubtedly serving different product markets.

**HNG<sup>↑</sup>** Services are in the same market when they are good substitutes for one another. That is, when there is "interchangeability of use or the cross elasticity of demand between the product and the substitutes for it." *Brown Shoe Co. v. United States*, 370 U.S. 294, 325, 8 L. Ed. 2d 510, 82 S. Ct. 1502 (1962). Furthermore, plaintiff bears the burden to prove by econometric evidence that the products are good substitutes. *Menasha Corp. v. News America Marketing In-Store, Inc.*, 354 F.3d 661, 664 (7th Cir. 2004). "Observing things that to the untutored eye seem to be substitutes need not mean they are good substitutes." *Id.* Not only has plaintiff failed to bring forth econometric evidence, its proffered competitive associations do not appear to be good substitutes even to the "untutored eye."

Three of the associations, NAEBA, [\*12] CEBAA and MABA, serve only exclusive buyer agents. The latter two serve agents in Colorado and Massachusetts and are therefore unlikely to be substitutes for services provided in Wisconsin even if the services offered were similar. Plaintiff, who is a member of NAEBA, has testified that the Realtors and NAEBA offer distinctly different services because NAEBA is directed specifically to the concerns of buyer agents. He testified that he joined NAEBA without regard to his membership in Realtors and that he knew of only one other real estate professional in Wisconsin eligible to join NAEBA.

Three other associations, AI, NAIFA and NAREA are devoted to providing services to real estate appraisers.. An unlikely substitute for the far more general services offered to real estate professionals by Realtors.

Four additional associations which plaintiff suggests as substitutes, AREAA, CREAA, CAREPA and NAHREP, serve distinct ethnic communities and have as their purpose the advancement of those communities and real estate professionals within them. It seems unlikely that their services would be substitutes for Realtors. This inference is further supported by the fact that one of the organizations, [\*13] CAREPA, is affiliated with the California Association of Realtors and NAR thereby dispelling any suggestion that they are competitors. Similarly, NAIREB is devoted to the needs of independent brokers apparently providing services unique to their needs while encouraging membership in Realtor associations.

Not only do none of these associations appear to be good substitutes, plaintiff has not offered evidence of a single real estate professional who has joined one of these organizations instead of Realtors or who has declined to join because he or she is a member of Realtors. The lack of such evidence is in stark contrast to the evidence in *Thompson* that 400 brokers fell into those categories. Furthermore, the dramatic differences in membership costs between the organizations and Realtors belies the suggestion that they are substitutes in the same product market.

On June 30, 2005 plaintiff offered a supplemental expert testimony of Riddle in the form of an analysis of non-random markets throughout the United states which purports to demonstrate that some of the alleged substitutes have higher membership rates in areas where there is no MLS tie ("open MLS") than in areas where there [\*14] is such a tie ("closed MLS"). Defendants have objected to this evidence as untimely and inadmissible under *Rule 702*.

The supplemental report is untimely. The existence of competing real estate service providers in the relevant product market whose sales were foreclosed is an essential element of plaintiff's claim. Yet the initial expert report, filed within the time requirement of *Rule 26(a)(2)(C)*, included nothing that would support this element. In fact, when he was deposed after issuing the report Riddle denied any opinion concerning whether other providers were in the same product market as Realtors. Riddle deposition of June 23, 2005 at 26-27. In light of the prevailing law it was apparent that this element would be critical to proving the claim. **HNZ<sup>↑</sup>** It is inappropriate to introduce expert testimony on this element under the guise of "rebuttal" simply because defendants subsequently denied the existence of the element. Under such circumstances exclusion is mandated by *Rule 37(c)(1)* unless the delay was harmless, an argument not made by plaintiff and unlikely to be sustained based on the prior deposition responses indicating that the expert would have no opinion on the topic.

[\*15] Even if the belatedly disclosed expert testimony was admitted there appears to be little relevant, probative value in the analysis. It is likely that markets for professional real estate services are different in California, Georgia, Alaska and Massachusetts and Wisconsin. For example, the proffered competing organizations are directed at specific ethnic communities yet there is no apparent effort to control for the significant differences in populations between markets. Comparison of the data indicates great disparities in membership rates within the open and closed markets which suggest that other factors, far more than open or closed status, impact membership rates.

Whatever minimal value the survey might have it is certainly not evidence that the organizations included in the survey are in the same product market as Realtors. Riddle, who conducted the analysis and offered the evidence, expressly testified at his deposition that the comparison of membership rates between open MLS and closed MLS markets does not demonstrate that the associations are in the same product market as defendant Realtors and that he has not done any analysis that would support such a conclusion. Riddle [\*16] deposition of June 23, at 31. He further testified that demonstrating that the associations competed in the same product market would require an analysis of comparative prices and price movements and an analysis of specific services offered by the compared providers. *Id. at 30*. No such analysis has been proffered even in the belated supplemental report.

Viewing the facts most favorable to plaintiff, he has failed to offer evidence sufficient to sustain a finding that there are competing providers of services in the tied product market whose sales have been foreclosed by the tie between MLS and Realtors. Accordingly, summary judgment must be granted in favor of defendants. The Court does not address the merits of the additional independent bases for judgment offered by defendants.

Plaintiff offers far less evidence or argument in support of his group boycott claim. *HN8* To sustain such a claim plaintiff must demonstrate that the anti-competitive effects of the membership requirement outweigh any anti-competitive effects of the membership rule. Initially, plaintiff must demonstrate that the membership requirement has an adverse impact on competition in the relevant market. *Bi-Rite Oil Co., Inc. v. Indiana Farm Bureau Co-op. Ass'n, Inc.*, 908 F.2d 200, 203 (7th Cir. 1990). [\*17] Plaintiff has not demonstrated that he or any other real estate professional was denied access to the MLS. His evidence in support of anticompetitive effect consists of referencing arguments made in support of the tying claim which have previously been rejected as establishing an anti-competitive effect.

In opposition to summary judgment plaintiff merely argues that defendants have failed to meet their burden to prove the absence of anti-competitive effects. This argument misapprehends the summary judgment process which permits a defendant to put the plaintiff to its proof merely by asserting the absence of evidence to support a particular element of plaintiff's claim. *Outlaw v. Newkirk*, 259 F.3d 833, 837 (7th Cir. 2001). For the reasons set forth in the analysis of the tying claim, plaintiff has failed to provide evidence sufficient to sustain a finding of anti-competitive effect from the membership requirement. Accordingly, there is no need to proceed to a balancing of pro-competitive effects of the rule. Defendants are entitled to summary judgment on the group boycott claim.

## ORDER

IT IS ORDERED that plaintiff's motion for summary judgment is DENIED.

IT IS FURTHER [\*18] ORDERED that defendants' motion for summary judgment is GRANTED.

IT IS FURTHER ORDERED that judgment is entered against plaintiff in favor of defendants dismissing plaintiff's complaint with prejudice and costs.

Entered this 25th day of August, 2005.

BY THE COURT:

JOHN C. SHABAZ

District Judge

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End of Document



## [\*Andrx Pharms., Inc. v. Elan Corp., PLC\*](#)

United States Court of Appeals for the Eleventh Circuit

August 29, 2005, Decided ; August 29, 2005, Filed

No. 03-13605

### **Reporter**

421 F.3d 1227 \*; 2005 U.S. App. LEXIS 18580 \*\*; 76 U.S.P.Q.2D (BNA) 1295 \*\*\*; 2005-2 Trade Cas. (CCH) P74,906; 18 Fla. L. Weekly Fed. C 936

ANDRX PHARMACEUTICALS, INC., Plaintiff-Appellant, versus ELAN CORPORATION, PLC, Defendant-Appellee, SKYEPHARMA, INC., Defendant.

**Prior History:** [\[\\*\\*1\]](#) Appeal from the United States District Court for the Southern District of Florida. D. C. Docket No. 00-03481-CV-AJ.

[\*Elan Corp., PLC v. Andrx Pharms., Inc., 366 F.3d 1336, 2004 U.S. App. LEXIS 8850 \(Fed. Cir., 2004\)\*](#)

## **Core Terms**

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naproxen, district court, antitrust, allegations, generic, medication, immunity, sham, patent infringement, pleadings, patent, manufacture, amend, settlement agreement, proceedings, competitors, antitrust violation, antitrust liability, motion for judgment, infringement, monopolize, initiated, further proceedings, amended complaint, license agreement, motion for leave, leave to amend, marketing, triggered, baseless

## **LexisNexis® Headnotes**

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Civil Procedure > Appeals > Standards of Review > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

Civil Procedure > Judgments > Pretrial Judgments > General Overview

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

## **[HN1](#) [down arrow] Appeals, Standards of Review**

When an appeal arises from the district court's grant of a defendant's motion for judgment on the pleadings, the facts are derived from the allegations in the plaintiff's complaint, which the appellate court must accept as true, and are presented in the light most favorable to the plaintiff. The appellate court need not accept as true, however, conclusory legal allegations made in the complaint.

Business & Corporate Compliance > ... > Governments > Agriculture & Food > Federal Food, Drug & Cosmetic Act

## [\*\*HN2\*\*](#) [down] Agriculture & Food, Federal Food, Drug & Cosmetic Act

The Food and Drug Administration (FDA) must give its approval before any new drug can be marketed or sold in the United States. [21 U.S.C.S. § 355\(a\)](#). Under [§ 355](#), different FDA approval standards apply depending on the drug the applicant is attempting to market. To gain approval for a drug that has not been introduced previously to the market, an applicant must file a new drug application (NDA) and must meet the requirements outlined in [§ 355\(b\)](#). [Section 355\(b\)](#) requires the submission of exhaustive information about the drug, including reports about the safety and efficacy of the drug. To gain approval for a generic, bioequivalent version of a drug which has already gained approval under [§ 355\(b\)](#), however, an applicant may file an abbreviated new drug application (ANDA), in which the applicant must satisfy the less exhaustive requirements outlined in [§ 355\(j\)](#).

Business & Corporate Compliance > ... > Governments > Agriculture & Food > Federal Food, Drug & Cosmetic Act

Patent Law > Infringement Actions > General Overview

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Experimental Use & Testing

## [\*\*HN3\*\*](#) [down] Agriculture & Food, Federal Food, Drug & Cosmetic Act

While [21 U.S.C.S. § 355\(j\)](#) allows an abbreviated new drug application (ANDA) applicant to satisfy its burden by demonstrating a certain bioequivalency between its drug and a drug approved under [§ 355\(b\)](#), [§ 355\(j\)](#) does require the ANDA applicant to certify that the manufacture and sale of its drug would not violate any patents held on the drug approved under [§ 355\(b\)](#). [21 U.S.C.S. § 355\(j\)\(2\)\(A\)\(vii\)](#). If an ANDA applicant certifies that its generic drug would not violate an existing patent, or would only violate a patent on a [§ 355\(b\)](#)-approved drug which is invalid, [21 U.S.C.S. § 355\(j\)\(2\)\(A\)\(vii\)\(IV\)](#), the ANDA applicant must notify the patentholder, which is then given 45 days to initiate patent infringement proceedings against the ANDA applicant. [21 U.S.C.S. § 355\(j\)\(5\)\(B\)\(iii\)](#). If the patentholder timely initiates such litigation, Food and Drug Administration approval for the generic drug will be stayed for up to 30 months, unless the patent being litigated expires or a final determination on the patent's validity is reached at an earlier date.

Business & Corporate Compliance > ... > Governments > Agriculture & Food > Federal Food, Drug & Cosmetic Act

Patent Law > Infringement Actions > Exclusive Rights > Manufacture, Sale & Use

## [\*\*HN4\*\*](#) [down] Agriculture & Food, Federal Food, Drug & Cosmetic Act

As an incentive for drug manufacturers to submit abbreviated new drug application (ANDA) applications for the production of generic drugs, [21 U.S.C.S. § 355](#) grants the first manufacturer to file an ANDA application for a generic drug using the type of certification outlined in [§ 355\(j\)\(2\)\(A\)\(vii\)\(IV\)](#) an exclusive 180-day period to market the generic drug before another ANDA application is approved for a similar generic drug. [21 U.S.C.S. § 355\(j\)\(5\)\(B\)\(iv\)\(I\)](#). This 180-day exclusivity period begins to run after the date of the first commercial marketing of the drug.

Civil Procedure > Appeals > Standards of Review > De Novo Review

421 F.3d 1227, \*1227L<sup>2005 U.S. App. LEXIS 18580, \*\*1L</sup>6 U.S.P.Q.2D (BNA) 1295, \*\*\*1295

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

Civil Procedure > Judgments > Pretrial Judgments > General Overview

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

#### **HN5** Standards of Review, De Novo Review

The appellate court reviews de novo the district court's ruling on a motion for judgment on the pleadings pursuant to [Fed. R. Civ. P. 12\(c\)](#). The application of the Noerr-Pennington doctrine is a question of law, and therefore also reviewed de novo. Judgment on the pleadings is proper when no issues of material fact exist, and the moving party is entitled to judgment as a matter of law based on the substance of the pleadings and any judicially noticed facts.

Antitrust & Trade Law > Sherman Act > General Overview

International Law > Authority to Regulate > Anticompetitive Activities

Antitrust & Trade Law > ... > Intellectual Property > Bad Faith, Fraud & Nonuse > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Assignments

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

#### **HN6** Antitrust & Trade Law, Sherman Act

The Sherman Anti-Trust Act, [15 U.S.C.S. § 1 et seq.](#), provides in part that every contract in restraint of trade or commerce among the several States, or with foreign nations, is illegal. [15 U.S.C.S. § 1](#). The Act also proscribes acts which seek to monopolize any part of the trade or commerce among the several States, or with foreign nations. [15 U.S.C.S. § 2](#). The Florida antitrust statutes, Fla. Stat. chs. 542.18, 542.19, closely track the language of the Sherman Act and are analyzed under the same rules and case law.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom to Petition

Torts > Public Entity Liability > Immunities > Judicial Immunity

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Labor > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

421 F.3d 1227, \*1227L<sup>2005 U.S. App. LEXIS 18580, \*\*1L</sup>6 U.S.P.Q.2D (BNA) 1295, \*\*\*1295

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

## **HN7** Regulated Practices, Price Fixing & Restraints of Trade

While the Sherman Anti-Trust Act, [15 U.S.C.S. § 1 et seq.](#), proscribes activity in restraint of trade, its reach has been tempered when its invocation would impair the exercise of constitutional rights. Recognizing that the [First Amendment](#) guarantees the right to petition the Government for a redress of grievances and that this guarantee overrides the effect of a contrary federal statute, and not wanting to impute to Congress an intent to invade the [First Amendment](#) right to petition, the United States Supreme Court has held that a defendant is immune from Sherman Act liability for concerted efforts to petition government to pass legislation which has the effect of restraining or monopolizing trade in favor of the defendant. Subsequent precedent has extended Noerr-Pennington immunity to defendants who exercise their right to petition government by resorting to administrative and/or judicial proceedings. Noerr-Pennington immunity thus shields a defendant from antitrust liability for resorting to litigation to obtain from a court an anticompetitive outcome.

Antitrust & Trade Law > Sherman Act > Scope > Exemptions

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Sham Exception

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity

Evidence > Burdens of Proof > General Overview

## **HN8** Scope, Exemptions

An exception to the Noerr-Pennington doctrine exists where the defendant engages in "sham litigation." To prevail on the argument that Noerr-Pennington immunity should be abrogated based on the sham litigation exception, a litigant must establish that: (1) the lawsuit is objectively baseless in the sense that no reasonable litigant could realistically expect success on the merits; and (2) the party bringing the allegedly baseless suit did so with a subjective motivation to interfere directly with the business relationships of a competitor. The existence of probable cause to bring a lawsuit is sufficient to thwart a claim that litigation was objectively baseless. Moreover, a winning lawsuit is by definition a reasonable effort at petitioning for redress and therefore not a sham.

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity

Antitrust & Trade Law > Sherman Act > General Overview

421 F.3d 1227, \*1227L<sup>2005 U.S. App. LEXIS 18580, \*\*1L</sup>6 U.S.P.Q.2D (BNA) 1295, \*\*\*1295

Antitrust & Trade Law > ... > US Department of Justice Actions > Civil Actions > General Overview

Constitutional Law > Congressional Duties & Powers > Copyright & Patent Clause

Constitutional Law > Bill of Rights > Fundamental Freedoms > General Overview

Constitutional Law > Bill of Rights > Fundamental Freedoms > Freedom to Petition

## **HN9** [blue] Antitrust & Trade Law, Exemptions & Immunities

The United States Constitution expressly permits the government to grant exclusive monopolies in the form of patents, [U.S. Const. art. I, § 8, cl. 8](#), and therefore the Sherman Antitrust Act, [15 U.S.C.S. § 1 et seq.](#), cannot be read to impede a litigant from seeking to defend constitutionally-permitted patent rights. Moreover, engaging in litigation to seek an anticompetitive outcome from a court is [First Amendment](#) activity that is immune from antitrust liability.

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Business & Corporate Compliance > ... > Ownership > Conveyances > Licenses

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > Licenses

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

Civil Procedure > Judgments > Pretrial Judgments > Judgment on Pleadings

Patent Law > ... > Specifications > Description Requirement > General Overview

Patent Law > Infringement Actions > General Overview

## **HN10** [blue] Antitrust & Trade Law, Exemptions & Immunities

Under the Federal Rules of Civil Procedure, the plaintiff is required in the complaint to make a short and plain statement of the claim showing that the plaintiff is entitled to relief. [Fed. R. Civ. P. 8\(a\)\(2\)](#). While courts had previously applied a heightened pleading requirement in antitrust cases, this view has subsequently been rejected in favor of applying [Rule 8\(a\)](#)'s notice pleading standard. Accordingly, absent some doctrine which immunizes the conduct alleged, such as the Noerr-Pennington doctrine, dismissals on the pleadings are particularly disfavored in fact-intensive antitrust cases.

Antitrust & Trade Law > Sherman Act > Claims

International Trade Law > General Overview

Patent Law > Infringement Actions > Burdens of Proof

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Settlements > Settlement Agreements > General Overview

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Settlement Agreements

Evidence > Burdens of Proof > General Overview

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Patent Law > Infringement Actions > General Overview

## [HN11](#) [blue document icon] Sherman Act, Claims

Section 1 of the Sherman Act, [15 U.S.C.S. § 1](#), provides that every contract in restraint of trade or commerce among the several States, or with foreign nations, is illegal. To prevail on a claim that a patent infringement settlement agreement violates [§ 1](#) of the Sherman Act, a plaintiff must prove: (1) the scope of the exclusionary potential of the patent; (2) the extent to which the agreement exceed that scope; and (3) the resulting anticompetitive effects in the relevant market.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Elements

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > Sherman Act > Scope > General Overview

Antitrust & Trade Law > Sherman Act > Scope > Monopolization Offenses

Evidence > Burdens of Proof > General Overview

## [HN12](#) [blue document icon] Attempts to Monopolize, Elements

Section 2 of the Sherman Act, [15 U.S.C.S. § 2](#), outlaws conduct which seeks to monopolize any part of the trade or commerce among the several States, or with foreign nations. To state a claim for attempted monopolization, plaintiff must show specific intent on the part of the defendant to bring about a monopoly and a dangerous probability of success.

Civil Procedure > Appeals > Standards of Review > Abuse of Discretion

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

## [HN13](#) [blue document icon] Standards of Review, Abuse of Discretion

The appellate court reviews the district court's denial of a motion for leave to amend for clear abuse of discretion. Under the Federal Rules of Civil Procedure, after a responsive pleading has been filed, a litigant must obtain leave to amend the complaint, which shall be freely given when justice so requires. *Fed. R. Civ. P. 15(a)*. Leave may be denied because of undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, or futility of amendment.

**Counsel:** For Andrx Pharmaceuticals, Inc., Appellant: Gerald J. Houlihan, Houlihan and Partners, P.A., Miami, FL.

For Elan Corporation, PLC, Appellee: Michael J. Flibbert, Finnegan, Henderson, Farabow, Garrett & Dunner, L.L.P., WASHINGTON, DC.

For Skyepharma, Inc., Appellee: Paul W. Browning, James B. Monroe, Finnegan, Henderson, Farabow, Garrett & Dunner, L.L.P., WASHINGTON, DC.

**Judges:** Before BIRCH and WILSON, Circuit Judges, and DOWD \*, District Judge.

**Opinion by:** BIRCH

## Opinion

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[\*\*\*1296] [\*1230] BIRCH, Circuit Judge:

In this appeal, we address whether the district court properly granted a patentholder's motion for judgment on the pleadings in a competitor's antitrust suit. The district court granted the motion because it found that the *Noerr-Pennington* doctrine immunized Defendant-appellee Elan Corporation, PLC ("Elan") from the maintenance of an antitrust suit based on the allegations of Plaintiff-appellant Andrx Pharmaceuticals, Inc. ("Andrx") that Elan [\*\*2] engaged in patent infringement proceedings to improperly protect its monopoly on the market for a controlled release naproxen medication. In addition, the district court found that Andrx's allegations regarding a licensing agreement entered into [\*\*\*1297] by Elan and another competitor to settle a separate infringement suit were insufficient to support an antitrust action under the Sherman Anti-Trust Act, 15 U.S.C. §§ 1 and 2. Finally, the district court denied Andrx's motion for leave to amend its complaint. For the reasons discussed more fully in this opinion, we conclude the district court properly construed the *Noerr-Pennington* doctrine to immunize Elan from liability for its infringement suits, and did not abuse its discretion in denying leave to amend. The district court erred, however, in dismissing Andrx's claims regarding its settlement agreement with one of Andrx's competitors. Accordingly, the district court's order is **AFFIRMED** in part, **REVERSED** in part, and **REMANDED** for further proceedings.

### I. BACKGROUND

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\* Honorable David D. Dowd, Jr., United States District Judge for the Northern District of Ohio, sitting by designation.

<sup>1</sup> **HN1** Because this appeal arises from the district court's grant of Elan's motion for judgment on the pleadings, the facts are derived from the allegations in Andrx's complaint, which we must accept as true, and are presented in the light most favorable to Andrx. See *Ortega v. Christian*, 85 F.3d 1521, 1524 (11th Cir. 1996). We need not accept as true, however, conclusory legal allegations made in the complaint. See *Green Leaf Nursery v. E.I. DuPont de Nemours & Co.*, 341 F.3d 1292, 1304 n.12 (11th Cir. 2003), cert. denied 541 U.S. 1037, 124 S. Ct. 2094, 158 L. Ed. 2d 723 (2004). Because the district court denied Andrx leave to file a second amended complaint, see R2-73 at 11, our inquiry is limited to the allegations in the first amended complaint.

[\*\*3] At its core, this litigation concerns the right to manufacture and sell the drug naproxen, an analgesic medication prescribed to treat pain and other disorders. Because the complex statutory regulations which govern the manufacture and sale of drugs in the United States provide context for the facts in this case, we will begin by briefly summarizing the relevant statutory provisions, after which we will recount the relevant facts specific to the parties.

**HN2** [↑] The Food and Drug Administration ("FDA") must give its approval before any new drug can be marketed or sold in the United States. [21 U.S.C. § 355\(a\)](#). Under [§ 355](#), different FDA approval standards apply depending on the drug the applicant is attempting to market. See [Valley Drug Co. v. Geneva Pharms., 344 F.3d 1294, 1296 \(11th Cir. 2003\)](#), cert. denied 543 U.S. 939, 160 L. Ed. 2d 248, 125 S. Ct. 308 (2004). To gain approval for a drug that has not been introduced previously to the market, an applicant must file a new drug application ("NDA") and must meet the requirements outlined in [§ 355\(b\)](#). *Id.* [Section 355\(b\)](#) requires the submission of "exhaustive information [\*\*4] about the drug," including reports about the safety and efficacy of the drug. *Id.* To gain approval for a generic, bioequivalent version of a drug which has already gained approval under [§ 355\(b\)](#), however, an applicant may file an abbreviated new drug application ("ANDA"), in which the applicant must satisfy the less exhaustive requirements outlined in [§ 355\(j\)](#). See *id.* **HN3** [↑] [\*1231] While [§ 355\(j\)](#) allows an ANDA applicant to satisfy its burden by demonstrating a certain bioequivalency between its drug and a drug approved under [§ 355\(b\)](#), [§ 355\(j\)](#) does require the ANDA applicant to certify that the manufacture and sale of its drug would not violate any patents held on the drug approved under [§ 355\(b\)](#). See [§ 355\(j\)\(2\)\(A\)\(vii\)](#). If an ANDA applicant certifies that its generic drug would not violate an existing patent, or would only violate a patent on a [§ 355\(b\)](#)-approved drug which is invalid, see [§ 355\(j\)\(2\)\(A\)\(vii\)\(IV\)](#),<sup>2</sup> the ANDA applicant must notify the patentholder, which is then given forty-five days to initiate patent infringement proceedings against the ANDA applicant, see [§ 355\(j\)\(5\)\(B\)\(iii\)](#). If the patentholder timely initiates such litigation, FDA approval for [\*\*5] the generic drug will be stayed for up to thirty months, unless the patent being litigated expires or a final determination on the patent's validity is reached at an earlier date. *Id.*

Against this background of information on drug approval procedures, we proceed to the facts relevant to the parties on appeal. Elan was the owner of U.S. Patent No. 5,637,320 ("the '320 patent"), which granted it the exclusive right to manufacture and sell in the United States a controlled release naproxen [\*\*6] medication. In 1998, SkyePharma Inc. ("SkyePharma")<sup>3</sup> filed an ANDA application pursuant to [§ 355\(j\)](#) to manufacture and sell a [\*\*\*1298] generic version of Elan's controlled release naproxen medication. In making its application, SkyePharma certified pursuant to [§ 355\(j\)\(2\)\(A\)\(vii\)\(IV\)](#) that its activity would not constitute patent infringement. Consequently, pursuant to [§ 355\(j\)\(5\)\(B\)\(iii\)](#), Elan initiated patent infringement proceedings against SkyePharma. According to Andrx's complaint, Elan and SkyePharma settled the litigation by entering into an agreement in which SkyePharma admitted to infringing the '320 patent in exchange for a license from Elan to manufacture a generic controlled release naproxen medication. Because SkyePharma was the first filing ANDA applicant, pursuant to [§ 355\(j\)\(5\)\(B\)\(iv\)\(I\)](#), the license agreement effectively would have given SkyePharma an exclusive 180-day period to market a generic naproxen medication. According to Andrx's complaint, however, SkyePharma had no intention of marketing its generic drug and therefore would never trigger the running of the 180-day exclusivity period. Accordingly, the settlement agreement had the effect of preventing any generic [\*\*7] competition in the controlled release naproxen market and constituted a conspiracy to restrain trade.

In addition to SkyePharma's alleged attempt to seek FDA approval for a generic controlled release naproxen medication, Andrx contends that it also sought to introduce a generic naproxen to the market. After Andrx filed

<sup>2</sup> **HN4** [↑] As an incentive for drug manufacturers to submit ANDA applications for the production of generic drugs, [§ 355](#) grants the first manufacturer to file an ANDA application for a generic drug using the type of certification outlined in [§ 355\(j\)\(2\)\(A\)\(vii\)\(IV\)](#) an exclusive 180-day period to market the generic drug before another ANDA application is approved for a similar generic drug. [§ 355\(j\)\(5\)\(B\)\(iv\)\(I\)](#). This 180-day exclusivity period begins to run "after the date of the first commercial marketing of the drug." *Id.*

<sup>3</sup> Although SkyePharma was also a named defendant in Andrx's first amended complaint, Andrx settled and voluntarily dismissed its claims against SkyePharma. See R2-73 at 1.

notice of non-infringement as required by [§ 355\(j\)\(2\)\(B\)\(ii\)](#), however, Elan filed patent infringement proceedings against Andrx. According to Andrx's complaint, Elan initiated this litigation "despite the absence of any reasonable belief that the claim might fairly be [\*1232] held to be valid upon adjudication." R1-3 P 29, at 5. Andrx alleged that Elan could not maintain its suit because the '320 patent had not been "validly issued because of *inter alia*, the SCRIP publication of June 22, 1988 which advertised its controlled [\*\*8] release naproxen in the United States more than one year prior to the filing of the application which resulted in the '320 patent." *Id.* P 27.<sup>4</sup> Moreover, Andrx alleged that "Elan's goal and intention in bringing [the infringement proceedings] was solely to . . . cause Andrx damage from the automatic administrative delay in the approval process" pursuant to [§ 355\(j\)\(5\)\(B\)\(iii\)](#). *Id.* P 29, at 5-6. In addition to these allegations, Andrx alleged that "Elan has engaged in a pattern and practice of baseless and sham litigation" against companies seeking to complete ANDAs for generic controlled release naproxen medications. *Id.* P 26, at 5. According to Andrx, Elan sought through this behavior to preserve its monopoly over the controlled release naproxen market in the United States. *Id.* P 39, at 7.

[\*\*9] Based on these allegations, Andrx filed suit against Elan and SkyePharma and alleged violations of the Sherman Anti-Trust Act, [15 U.S.C. §§ 1](#) and [2](#), and the Florida antitrust laws, [FLA. STAT. ch. 542.18](#) and [ch. 542.19](#). Citing the *Noerr-Pennington* doctrine and precedent which allowed for the licensing settlement reached by Elan and SkyePharma, the district court granted Elan's motion for judgment on the pleadings. In addition, the district court denied Andrx's motion to amend its complaint on account of Andrx's undue delay. On appeal, Andrx argues that the district court erred in dismissing with prejudice its suit against Elan because the district court misconstrued the *Noerr-Pennington* doctrine and its sham litigation exception. In addition, Andrx argues that the district court erred by denying its motion for leave to amend its complaint. [\*\*\*1299]

## II. DISCUSSION

### A. Judgment on the Pleadings

**HN5** [↑] "We review *de novo* the district court's ruling on a motion for judgment on the pleadings pursuant to *Federal Rule of Civil Procedure 12(c)*." *Horsley v. Rivera*, 292 F.3d 695, 700 (11th Cir. 2002). [\*\*10] The application of the *Noerr-Pennington* doctrine is a question of law, and therefore also reviewed *de novo*. See *Tec Cogeneration Inc. v. Fla. Power & Light Co.*, 76 F.3d 1560, 1567 (11th Cir. 1996), modified in part on other grounds, 86 F.3d 1028 (11th Cir. 1996) (per curiam). Judgment on the pleadings is proper when no issues of material fact exist, and the moving party is entitled to judgment as a matter of law based on the substance of the pleadings [\*1233] and any judicially noticed facts. See *Horsley*, 292 F.3d at 700.

**HN6** [↑] The Sherman Anti-Trust Act provides that "every contract . . . in restraint of trade or commerce among the several States, or with foreign nations, is . . . illegal." [15 U.S.C. § 1](#). The Act also proscribes acts which seek "to monopolize any part of the trade or commerce among the several States, or with foreign nations." [15 U.S.C. § 2](#).<sup>5</sup>

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<sup>4</sup> Patent law provides that a patent shall not be granted if the invention was "described in a printed publication in this or a foreign country or in public use or on sale in this country, more than one year prior to the date of the application for patent in the United States." [35 U.S.C. § 102](#). This statutory provision is termed the "on-sale bar" to patent validity. See *Ferag AG v. Quipp Inc.*, 45 F.3d 1562, 1566 (Fed. Cir. 1995). Because Elan purportedly advertised its controlled release naproxen for sale in the publication SCRIP World Pharmaceutical News, Andrx argued that the on-sale bar was triggered, thereby invalidating the '320 patent. Andrx's arguments notwithstanding, the district court found that the SCRIP publication did not trigger the on-sale bar. See *Elan Corp., PLC v. Andrx Pharms., Inc.*, 272 F. Supp. 2d 1325, 1340 (S.D. Fla. 2002). The district court did find, however, that a letter written by Elan to Lederle Laboratories in 1987 triggered the on-sale bar and invalidated the '320 patent. *Id. at 1349*. This latter finding was reversed by the Federal Circuit, which remanded Elan's patent infringement suit for further proceedings. See *Elan Corp., PLC v. Andrx Pharms., Inc.*, 366 F.3d 1336, 1342 (Fed. Cir. 2004).

<sup>5</sup> As the district court noted, the Florida antitrust statutes, [FLA. STAT. ch. 542.18](#) and [ch. 542.19](#), closely track the language of the Sherman Act and are analyzed under the same rules and case law. See *All Care Nursing Serv. v. High Tech Staffing Servs., Inc.*, 135 F.3d 740, 745 n.11 (11th Cir. 1998). Accordingly, our discussion of federal **antitrust law** applies with equal force to the Florida statutory provisions.

Citing the Sherman Act and the Florida antitrust statutes, Andrx alleges that Elan improperly sought to monopolize the controlled release naproxen market and prevent competition by: (1) initiating sham patent infringement litigation against [\\*\\*11](#) Andrx; and (2) entering into a settlement agreement with SkyePharma which granted SkyePharma exclusive licensing rights to manufacture and sell a generic controlled release naproxen medication. We will examine each set of allegations in turn.

## 1. Patent Infringement Proceedings

[HN7](#) While the Sherman Anti-Trust Act does proscribe activity in restraint of trade, its reach has been tempered when its invocation would impair the exercise of constitutional rights. Recognizing that the [First Amendment](#) guarantees the right to "petition the Government for a redress of grievances," [U.S. CONST. I<sup>\\*\\*121</sup> amend I](#), and that this guarantee overrides the effect of a contrary federal statute, see [Marbury v. Madison, 5 U.S. 137, 177-78, 2 L. Ed. 60 \(1803\)](#), and not wanting to "impute to Congress an intent to invade the [First Amendment](#) right to petition," [Prof'l Real Estate Investors v. Columbia Pictures Indus., Inc., 508 U.S. 49, 56, 113 S. Ct. 1920, 1926, 123 L. Ed. 2d 611 \(1993\)](#) (internal quotations omitted), the Supreme Court has held that a defendant is immune from Sherman Act liability for concerted efforts to petition government to pass legislation which has the effect of restraining or monopolizing trade in favor of the defendant. See [E. R.R. Presidents Conf. v. Noerr Motor Freight, Inc., 365 U.S. 127, 136, 81 S. Ct. 523, 529, 5 L. Ed. 2d 464 \(1961\)](#) (granting antitrust immunity for publicity campaign designed to spur the adoption of monopoly-facilitating legislation); [United Mine Workers v. Pennington, 381 U.S. 657, 670, 85 S. Ct. 1585, 1593, 14 L. Ed. 2d 626 \(1965\)](#) (noting that Noerr shielded a defendant from antitrust liability for "efforts to influence public officials . . . even though intended to eliminate [\\*\\*13](#) competition"). Subsequent precedent has extended *Noerr-Pennington* immunity to defendants who exercise their right to petition government by resorting to administrative and/or judicial proceedings. See [Cal. Motor Transp. Co. v. Trucking Unlimited, 404 U.S. 508, 510, 92 S. Ct. 609, 611-12, 30 L. Ed. 2d 642 \(1972\)](#). *Noerr-Pennington* immunity thus shields a defendant from antitrust liability for resorting to litigation to obtain from a court an anticompetitive outcome.

[HN8](#) An exception to the *Noerr-Pennington* doctrine exists, however, where the defendant engages in "sham litigation." [Prof'l Real Estate Investors, 508 U.S. at 56, 113 S. Ct. at 1926](#); see [Noerr, 365 U.S. at 144, 81 S. Ct. at 533](#) (finding Sherman Act immunity inappropriate where the exercise of the right to petition was "a mere sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of a competitor"). [\[\\*1234\]](#) To prevail on the argument that *Noerr-Pennington* immunity should be abrogated based on the sham litigation exception, a litigant must establish that: (1) "the lawsuit [is] objectively baseless in the sense [\\*\\*14](#) that no reasonable litigant could realistically expect success on the merits"; and (2) the party bringing the allegedly baseless suit did so with a "subjective motivation . . . to interfere *directly* with the business relationships of a competitor." [\[\\*\\*\\*1300\] Prof'l Real Estate Investors, 508 U.S. at 60-61, 113 S. Ct. at 1928](#). Construing the first prong of the sham litigation exception test, the Court noted that the existence of probable cause to bring a lawsuit is sufficient to thwart a claim that litigation was objectively baseless. See [Prof'l Real Estate Investors, 508 U.S. at 62, 113 S. Ct. at 1929](#). Moreover, the Court noted that "[a] winning lawsuit is by definition a reasonable effort at petitioning for redress and therefore not a sham." [Prof'l Real Estate Investors, 508 U.S. at 60 n.5, 113 S. Ct. at 1928 n.5](#).

Based on this precedent, we agree with the district court that the [Noerr-Pennington](#) doctrine shields Elan from antitrust liability for filing two patent infringement suits against Andrx in relation to the manufacture and sale of controlled release naproxen. [HN9](#) The United States Constitution expressly permits the government [\\*\\*15](#) to grant exclusive monopolies in the form of patents, see [U.S. CONST. art. I, § 8, cl. 8](#), and therefore the Sherman Act cannot be read to impede a litigant from seeking to defend constitutionally-permitted patent rights. See [Prof'l Real Estate Investors, 508 U.S. at 56, 113 S. Ct. at 1926](#) (declining to impute an unconstitutional purpose to Sherman Anti-Trust Act). Moreover, as the Supreme Court has noted, engaging in litigation to seek an anticompetitive outcome from a court is [First Amendment](#) activity that is immune from antitrust liability. See [Cal. Motor Transp. Co., 404 U.S. at 510, 92 S. Ct. at 611-12](#). Thus, we conclude *Noerr-Pennington* immunity was triggered by Elan's filing suit against Andrx. In addition, we conclude that the sham litigation exception is inapplicable. Andrx's main contention in its complaint that the patent litigation was a sham hinged on its claim that the on-sale bar found in [35 U.S.C. § 102](#) was triggered by Elan's naproxen advertisement in the publication SCRIP World Pharmaceutical

News. Two courts have subsequently rejected that argument. See *Elan Corp., PLC*, 272 F. Supp. 2d at 1340 [\*\*16] (rejecting argument that the SCRIP advertisement triggered on-sale bar); *Elan Corp., PLC*, 366 F.3d at 1342 (rejecting the argument that the on-sale bar was triggered). Thus, while Elan may not have won its infringement lawsuit at this point, it certainly has made a winning argument against Andrx's contentions of patent invalidity. Cf. *Pro'l Real Estate Investors*, 508 U.S. at 60 n.5, 113 S. Ct. at 1928 n.5. Thus, it is manifest that Elan's patent infringement proceedings were not objectively baseless, and therefore not a sham. Accordingly, because the *Noerr-Pennington* doctrine applies, and the sham litigation exception is inapplicable, the district court properly found that Elan was immunized from antitrust liability for filing infringement proceedings against Andrx.

## 2. Elan-SkyePharma Settlement Agreement

In contrast, we conclude that the district court erred in finding that Andrx had not sufficiently pled an antitrust violation in relation to the licensing agreement which Elan signed with SkyePharma to terminate patent infringement litigation. [HN10](#) Under the Federal Rules of Civil Procedure, the plaintiff is required in the complaint to make "a [\*\*17] short and plain statement of the claim showing that the [plaintiff] is entitled to relief." [Fed. R. Civ. P. 8\(a\)\(2\)](#). While [\*1235] courts had previously applied a heightened pleading requirement in antitrust cases, this view has subsequently been rejected in favor of applying [Rule 8\(a\)](#)'s notice pleading standard. *Quality Foods de Centro America, S.A. v. Latin American Agribusiness Dev. Corp., S.A.*, 711 F.2d 989, 995 (11th Cir. 1983); see *Spanish Broad. Sys. of Fla., Inc. v. Clear Channel Communications, Inc.*, 376 F.3d 1065, 1077 (11th Cir. 2004) (concluding that the "liberal pleading regime" outlined by [Fed. R. Civ. P. 8\(a\)\(2\)](#) applies to allegations of antitrust violations); *Covad Communications Co. v. BellSouth Corp.*, 299 F.3d 1272, 1279 (11th Cir. 2002) (describing the threshold requirements for properly pleading an antitrust violation as "exceedingly low"), vacated on other grounds by 540 U.S. 1147, 124 S. Ct. 1143, 157 L. Ed. 2d 1040 (2004). Accordingly, absent some doctrine which immunizes the conduct alleged, such as the *Noerr-Pennington* doctrine, "dismissals [\*\*18] [on the pleadings] are particularly disfavored in fact-intensive antitrust cases." *Covad Communications Co.*, 299 F.3d at 1279. Against this background, we examine whether Andrx's allegations sufficiently state a claim under [§ 1](#) and/or [§ 2 of the Sherman Anti-Trust Act](#).

As we noted previously, [HN11](#) [Section 1 of the Sherman Act](#) provides that "every contract . . . in restraint of trade or commerce among the several States, or with foreign nations, is . . . illegal." [15 U.S.C. § 1](#). To prevail on a claim that a patent infringement settlement [\*\*1301] agreement violates [§ 1 of the Sherman Act](#), a plaintiff must prove "(1) the scope of the exclusionary potential of the patent; (2) the extent to which the agreements exceed that scope; and (3) the resulting anticompetitive effects" in the relevant market. *Schering-Plough Corp. v. FTC*, 402 F.3d 1056, 1066 (11th Cir. 2005) (citing *Valley Drug Co.*, 344 F.3d at 1312). With regard to the first element, the allegations in Andrx's complaint demonstrated that the '320 patent was necessary to the manufacture and sale of a controlled release naproxen medication, and that its owner could effectively [\*\*19] exclude competitors from making other controlled release naproxen medications. See R1-3 PP 22-23, 33-35. With regard to the second element, Andrx alleged that the Elan-SkyePharma licensing agreement, coupled with SkyePharma's putative agreement to refrain from ever marketing a generic controlled release naproxen medication, "effectively barred any generic competitors from entering the market. *Id.* PP 22-23. If true, this dynamic would exceed the scope of exclusion intended by the '320 patent. See [21 U.S.C. § 355\(j\)](#) (outlining criteria for drug manufacturers to enter the market with a generic version of previously-approved patented products). With regard to the third element, Andrx described the relevant market as the "controlled release naproxen" market. See R1-3 P 17. Andrx alleged that Elan had sufficient market power to affect the controlled release naproxen market because it was the only supplier of naproxen in the United States. See *id.* P 16. Finally, demonstrating the anticompetitive effects, Andrx alleged that Elan's licensing agreement with SkyePharma, and SkyePharma's putative agreement to refrain from marketing its generic drug, would [\*\*20] "prevent competition in the market for controlled release naproxen." *Id.* PP 22-23; see also *id.* P 44 (stating that the conduct of Elan and SkyePharma "foreclosed" entry by competitors into the relevant market and "precluded" competition). Additionally, Andrx alleged that the agreement had the result of depriving the general public of a less expensive generic product. See *id.* P 43. Thus, Andrx sufficiently pled facts for a [§ 1](#) claim that the Elan-SkyePharma settlement agreement constituted an antitrust violation.

**HN12** [+] [\*1236] [Section 2 of the Sherman Act](#) outlaws conduct which seeks "to monopolize any part of the trade or commerce among the several States, or with foreign nations." [15 U.S.C. § 2](#). "To state a claim for attempted monopolization, plaintiff must show specific intent on the part of the defendant to bring about a monopoly and a dangerous probability of success." [Quality Foods de Centro America, S.A., 711 F.2d at 996](#). In its complaint, Andrx alleged that Elan had the "specific intent to monopolize and preserve a monopoly in the controlled release naproxen market." R1-3 P 49. In addition, as we already noted, Andrx alleged that Elan was [\*21] the only supplier of naproxen in the United States, see *id.* P 16, and therefore had "achieved a probability of success," *id.* P 56. Accordingly, we conclude that Andrx sufficiently pled a violation of [§ 2 of the Sherman Act](#).

In sum, then, while the allegations regarding Elan's infringement suits against Andrx were immunized under the *Noerr-Pennington* doctrine, Andrx did sufficiently state a claim under both [§ 1](#) and [§ 2 of the Sherman Anti-Trust Act](#) that Elan's settlement agreement with SkyePharma, coupled with SkyePharma's putative agreement not to market, violated [antitrust law](#). Accordingly, we remand this case for further proceedings as to those allegations. Our conclusion as to the sufficiency of the complaint does not preclude, however, Andrx's claims from being challenged at the summary judgment stage. See [Quality Foods de Centro America, S.A., 711 F.2d at 999](#) (reversing a district court's dismissal of antitrust claims on the pleadings, but noting that the claims "may very well wash out on summary judgment"). Our determination recognizes that antitrust cases are "fact-intensive," [Covad Communications Co., 299 F.3d at 1279](#), and require [\*22] appropriate market analysis, see [Schering-Plough Corp., 402 F.3d at 1065-66](#), and therefore are typically inappropriate for a [Rule 12](#) dismissal in the absence of an applicable immunity doctrine. Accordingly, with regard to Andrx's allegations that the Elan-SkyePharma settlement agreement and SkyePharma's alleged agreement to refrain from marketing a generic controlled release naproxen medication violated [§§ 1](#) and [2](#) of the Sherman Anti-Trust Act, the case is remanded for further proceedings.

#### B. Motion to Amend

**HN13** [+] We review the district court's denial of a motion for leave to amend for clear abuse of discretion. See [Lowe's Home Ctrs., Inc. v. Olin](#) [\*1302] [Corp., 313 F.3d 1307, 1315 \(11th Cir. 2002\)](#). Under the Federal Rules of Civil Procedure, after a responsive pleading has been filed, a litigant must obtain leave to amend the complaint, which "shall be freely given when justice so requires." [FED. R. CIV. P. 15\(a\)](#). Leave may be denied because of "undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing [\*23] party by virtue of allowance of the amendment, [or] futility of amendment." [Foman v. Davis, 371 U.S. 178, 182, 83 S. Ct. 227, 230, 9 L. Ed. 2d 222 \(1962\)](#).

Based on the foregoing precedent and the facts of this case, we discern no abuse of discretion in the district court's denial of Andrx's motion for leave to amend. As the district court noted, Andrx filed its first amended complaint in March 2001, and was put on notice that its "sham litigation exception" theory was insufficient at least by March 2002. However, Andrx did not move to amend until it appeared in the district court in April 2003 to argue Elan's motion for judgment on the pleadings. See [Smith v. Duff & Phelps, Inc., 5 F.3d 488, 493 \(11th Cir. 1993\)](#) (finding no abuse of discretion where litigant waited [\*1237] more than a year to seek leave to amend after it was put on notice that its claim was defective). Moreover, we note that in its second amended complaint, Andrx purported to advance a "sham litigation exception" theory based on [Walker Process Equipment, Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172, 86 S. Ct. 347, 15 L. Ed. 2d 247 \(1965\)](#), a theory not pled in the [\*24] first amended complaint. See [Burger King Corp. v. Weaver, 169 F.3d 1310, 1319 \(11th Cir. 1999\)](#) (finding no abuse of discretion where plaintiff attempted to introduce new theory of recovery in amended complaint). Finally, we agree with the district court that Andrx's explanations for its delay in filing for leave to amend do not demonstrate that justice required the grant of the motion to amend. See [Carruthers v. BSA Adver., Inc., 357 F.3d 1213, 1218 \(11th Cir. 2004\)](#) (per curiam). Accordingly, even though Andrx was motivated to amend its complaint to avoid the court's grant of Elan's motion for judgment on the pleadings, Andrx's undue delay in moving for leave to amend, its attempt to inject a new theory of recovery, and its failure to show that justice required the grant of its motion demonstrate that the district court did not clearly abuse its discretion in denying Andrx's motion for leave to amend. See [Lowe's Home Ctrs., Inc., 313 F.3d at 1315](#).

### III. CONCLUSION

In this appeal, we were called upon to determine whether Andrx, a drug manufacturer seeking to introduce to the market a generic controlled release naproxen medication, **[\*\*25]** could maintain suit against Elan, the owner of the patent for controlled release naproxen, for its initiation of patent infringement proceedings against Andrx and for its settlement agreement with SkyePharma which purportedly shielded Elan from generic competition in the naproxen market.

Because the *Noerr-Pennington* doctrine immunized Elan from antitrust liability as to the former allegations, the district court properly found that the allegations could not state a claim for relief under antitrust law. But, because the latter allegations sufficiently pled antitrust violations, the district court erred by granting Elan's motion for judgment on the pleadings, and therefore the case must be remanded for further proceedings in relation to the alleged antitrust violations stemming from the Elan-SkyePharma settlement agreement. On remand, because the district court did not clearly abuse its discretion in denying Andrx's motion for leave to amend, the district court's inquiry should be limited to the allegations of antitrust violations contained in Andrx's first amended complaint. Accordingly, the district court's grant of Elan's motion for judgement on the pleadings is **AFFIRMED** **[\*\*26]** in part and **REVERSED** in part, and **REMANDED** for further proceedings.

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## In re Wireless Tel. Servs. Antitrust Litig.

United States District Court for the Southern District of New York

August 29, 2005, Decided ; August 30, 2005, Filed

02 Civ. 2637 (DLC)

### **Reporter**

385 F. Supp. 2d 403 \*; 2005 U.S. Dist. LEXIS 18293 \*\*; 2005-2 Trade Cas. (CCH) P74,909; 2005 WL 2086031

IN RE WIRELESS TELEPHONE SERVICES ANTITRUST LITIGATION; This Document Relates to: ALL ACTIONS

**Subsequent History:** As Amended September 2, 2005.

Related proceeding at [Freeland v. AT&T Corp., 2006 U.S. Dist. LEXIS 57394 \(S.D.N.Y., Aug. 17, 2006\)](#)

**Prior History:** [In re Wireless Tel. Servs. Antitrust Litig., 2004 U.S. Dist. LEXIS 19977 \(S.D.N.Y., Oct. 6, 2004\)](#)

## **Core Terms**

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handsets, market power, consumers, wireless service, Wireless, manufacturers, carriers, percent, defendants', prices, tying arrangement, anticompetitive, effects, network, providers, market share, tied product, summary judgment, features, plaintiffs', seller, technology, digital, brand, tying product, spectrum, locking, retail, costs, customers

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Discovery > Methods of Discovery > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

Civil Procedure > ... > Summary Judgment > Supporting Materials > General Overview

### **HN1 [+] Discovery, Methods of Discovery**

Summary judgment may be granted only if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#).

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

385 F. Supp. 2d 403, \*403LÁ2005 U.S. Dist. LEXIS 18293, \*\*18293

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

## **HN2** **Summary Judgment, Burdens of Proof**

The burden of showing that no genuine factual dispute exists rests on the party seeking summary judgment, and in assessing the record to determine whether there is a genuine issue as to a material fact, the court is required to resolve all ambiguities and draw all permissible factual inferences in favor of the party against whom summary judgment is sought.

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

## **HN3** **Summary Judgment, Opposing Materials**

When the moving party has asserted facts showing that it is entitled to summary judgment, the opposing party must set forth specific facts showing that there is a genuine issue for trial, and cannot rest on the mere allegations or denials of the movant's pleadings. Fed. R. Civ. P. 56(e). If there is evidence, however, from which a reasonable inference could be drawn in favor of the opposing party, summary judgment is improper.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > Judgments > Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

## **HN4** **Entitlement as Matter of Law, Appropriateness**

In the realm of **antitrust law**, summary judgment serves a vital function, by avoiding wasteful trials and prolonged litigation that may have a chilling effect on procompetitive market forces. If the plaintiff's theory is economically senseless, no reasonable jury could find in its favor, and summary judgment should be granted. Nevertheless, no special burden is imposed on a plaintiff opposing summary judgment in an antitrust case.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

#### **HN5** [down] Antitrust & Trade Law, Sherman Act

See [15 U.S.C.S. § 1](#).

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Sherman Act Violations

#### **HN6** [down] Antitrust & Trade Law, Sherman Act

Among the activities prohibited by [§ 1](#) of the Sherman Act, [15 U.S.C.S. § 1](#) are restraints of trade in the form of an agreement by a party to sell one product but only on the condition that the buyer also purchase a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier. Such agreements are known as tying arrangements. Courts have repeatedly emphasized that the essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of the tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

#### **HN7** [down] Antitrust & Trade Law, Sherman Act

When a consumer is forced to purchase a tied product when the consumer would not do so in a competitive market, a tying arrangement is unlawful. In essence, a seller may not use its market power in one market to impair competition on the merits in another market. Competition in the tied market can be impaired by injuring existing businesses in the market or creating barriers to entering the market. The consumer is injured when her freedom to select the best bargain is impaired by her need to purchase the tying product. She may also be injured when she is unable to evaluate the true cost of either product when they are only available as a package.

Antitrust & Trade Law > Sherman Act > Claims

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Sherman Act Violations

Antitrust & Trade Law > Sherman Act > General Overview

#### **HN8** [down] Sherman Act, Claims

The United States Court of Appeals for the Second Circuit has required proof of five specific elements to state an unlawful tying claim: first, a tying and a tied product; second, evidence of actual coercion by the seller that forced the buyer to accept the tied product; third, sufficient economic power in the tying product market to coerce purchaser acceptance of the tied product; fourth, anticompetitive effects in the tied market; and fifth, the involvement of a "not insubstantial" amount of interstate commerce in the tied market.

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Defenses](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

[Antitrust & Trade Law > Sherman Act > General Overview](#)

## [\*\*HN9\*\*\[\] Tying Arrangements, Defenses](#)

Certain tying arrangements pose an unacceptable risk of stifling competition and therefore are unreasonable "per se." Analysis under the per se rule is, by definition, without inquiry into actual market conditions. Put another way, where a tying arrangement may be condemned as illegal per se, plaintiffs need not allege, let alone prove, facts addressed to the fourth element of the Second Circuit test for an unlawful tying claim. If a plaintiff succeeds in establishing the existence of sufficient market power to create a per se violation, the plaintiff is also relieved of the burden of rebutting any justifications the defendant may offer for the tie.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Per Se Rule](#)

## [\*\*HN10\*\*\[\] Antitrust & Trade Law, Sherman Act](#)

A tying arrangement may be condemned as illegal per se only if the existence of forcing is probable because there is a substantial potential for impact on competition.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > ... > Market Definition > Relevant Market > Product Market Definition](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

## [\*\*HN11\*\*\[\] Antitrust & Trade Law, Sherman Act](#)

Where the plaintiff has alleged a tying violation, and the showing of market power is insufficient to find a per se violation of ***antitrust law***, courts apply a rule of reason analysis at the fact-finding stage through a burden-shifting scheme. Specifically, the plaintiffs bear an initial burden to demonstrate the defendants' challenged behavior had an actual adverse effect on competition as a whole in the tied product market. Whether an actual adverse effect has occurred is determined by examining factors like reduced output, increased prices and decreased quality. So too may a demonstration of significant barriers to entry into a particular market show an actual adverse effect on competition. If the plaintiff fulfills this preliminary burden, however, the burden shifts to the defendants to offer evidence of the pro-competitive effects of their agreement. Assuming defendants can provide such proof, the

burden shifts back to the plaintiffs to prove that any legitimate competitive benefits offered by defendants could have been achieved through less restrictive means.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Patent Law > ... > Defenses > Inequitable Conduct > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

#### **HN12** [ ] [Antitrust & Trade Law, Sherman Act](#)

The third element of a tying claim -- market power in the tying product market -- requires that the plaintiff prove that the defendant has the power to force a purchaser to do something that he would not do in a competitive market, which is often equated with the ability of a single seller to raise price and restrict output. A seller's market power ordinarily is inferred from its possession of a predominant share of the market. Nevertheless, market power may also exist in other circumstances, such as where the government has granted the seller a patent or similar monopoly over a product, or when the seller offers a unique product that competitors are not able to offer.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

#### **HN13** [ ] [Antitrust & Trade Law, Sherman Act](#)

The United States Court of Appeals for the Second Circuit requires proof of market power in all tying cases. Without evidence that defendants are using market power to force consumers to purchase the product or service in the tied market, there is no basis to view the arrangement as unreasonably restraining competition. This is so, because only if consumers are forced to purchase the tied product as a result of the defendants' market power would the arrangement have anticompetitive consequences.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

#### **HN14** [ ] [Antitrust & Trade Law, Sherman Act](#)

A single branded product may, in rare cases, constitute its own relevant market. Entrenched buyer preferences for established brands can also create significant barriers to entry. Yet the mere existence of a brand and brand identification in the marketplace are not synonymous with market power. In general, where interbrand competition exists it provides a significant check on the exploitation of interbrand market power because of the ability of consumers to substitute a different brand of the same product.

[Antitrust & Trade Law > Sherman Act > General Overview](#)

[Civil Procedure > ... > Jury Trials > Jury Instructions > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview](#)

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > Sherman Act Violations

## [\*\*HN15\*\*](#) [L] Antitrust & Trade Law, Sherman Act

Market share data serves as strong, perhaps presumptive, evidence of the presence or absence of market power, but careful analysis of market share, and the structure of the market, including the activities of the defendant and others within the market, is necessary to ascertain whether a defendant has monopoly power.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > Price Fixing

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [\*\*HN16\*\*](#) [L] Antitrust & Trade Law, Sherman Act

Although liability may be imposed on the basis of conscious parallelism in certain antitrust contexts, our the Second Circuit's tying case law lends no support for an inference of market power to be drawn from defendants' parallel behavior. Indeed, unless the plaintiff has alleged a conspiracy, it is inappropriate to assess one defendant's market power by measuring the cumulative power of all defendants practicing tying.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [\*\*HN17\*\*](#) [L] Antitrust & Trade Law, Sherman Act

The test for market power is not whether a defendant can raise its prices somewhat, but whether the defendant has the power to control prices or exclude competition.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [\*\*HN18\*\*](#) [L] Antitrust & Trade Law, Sherman Act

In order to show market power from a defendant's practice of selling its products above marginal cost, a plaintiff must accurately measure price and all appropriate costs. Moreover, the test for the existence of market power is the ability to control price or exclude competition, not simply pricing a product above marginal cost when that price differential can be explained by the existence of economic realities entirely separate from the existence of market power, for instance, the presence of high fixed costs.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > General Overview

Antitrust & Trade Law > ... > Per Se Rule & Rule of Reason > Per Se Rule Tests > Manifestly Anticompetitive Effects

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [\*\*HN19\*\*](#) [ ] **Antitrust & Trade Law, Sherman Act**

The United States Supreme Court has long recognized the interrelationship between market power and anticompetitive effects. Indeed, at the heart of the per se rule of tying is the intuition that where a seller has significant market power, one may presume unreasonableness without the necessity of any analysis of the market context in which the alleged tying arrangement may be found. As a consequence, where a defendant's market power is sufficiently great that its tie qualifies as a per se violation, a plaintiff is relieved of the separate burden of showing an anticompetitive effect from the tying in the tied product market. Conversely, the tying case law also reflects the understanding that where market power is not present, an alleged tying violation cannot be a threat to competition in the tied product market. A seller must have power in the tying product market. Absent such power, tying cannot conceivably have any adverse impact in the tied product market and can only be pro-competitive in the tying product market.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## [\*\*HN20\*\*](#) [ ] **Antitrust & Trade Law, Sherman Act**

To demonstrate anticompetitive effects, a plaintiff must demonstrate that the tie as it actually operates in the market harmed competition in the tied product market. For a tie to create an anticompetitive effect there must be a substantial threat that the tying seller will acquire market power in the tied product market. No such threat exists if the tied product market is occupied by many stable sellers who are not likely to be driven out by tying, or if entry barriers in the tied product market are low. Speculation about anticompetitive effects is not enough. At no time may expert testimony rooted in hypothetical assumptions substitute for actual market data.

Evidence > Admissibility > Expert Witnesses

Evidence > Types of Evidence > Testimony > General Overview

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN21\*\*](#) [ ] **Admissibility, Expert Witnesses**

Fed. R. Civ. P. 702 provides that expert testimony concerning technical or specialized knowledge is admissible to assist the trier of fact if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case.

Evidence > Admissibility > Expert Witnesses > Daubert Standard

Evidence > Admissibility > Scientific Evidence > General Overview

Evidence > Admissibility > Scientific Evidence > Standards for Admissibility

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN22\*\*](#) [+] **Expert Witnesses, Daubert Standard**

A court has an obligation to act as a gatekeeper to ensure the reliability and relevancy of expert testimony presented to a jury. Specifically, the court must determine that an expert employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field.

Evidence > ... > Testimony > Expert Witnesses > General Overview

## [\*\*HN23\*\*](#) [+] **Testimony, Expert Witnesses**

Where an expert conducts a regression analysis and fails to incorporate major independent variables, such analysis may be excluded as irrelevant.

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**Judges:** DENISE COTE, United States District Judge.

**Opinion by:** DENISE COTE

## **Opinion**

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### **[\*405] AMENDED OPINION AND ORDER**

DENISE COTE, District Judge:

On February 25, 2005, the defendants in this action, the five largest carriers of wireless telephone services in the U.S. market,<sup>1</sup> moved for summary judgment on plaintiffs' claim that each defendant's practice of requiring

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<sup>1</sup>The defendants are AT&T Wireless Services, Inc.; Cellular Telephone Company; AT&T Wireless PCS, LLC; AT&T Cellular Services, Inc.; Claircom Communications Group, Inc.; and Bay Area Cellular Telephone Company (collectively, "AT&T Wireless"); Cingular Wireless LLC; Pacific Telesis Mobile Services, LLC; Southwestern Bell Mobile Systems, LLC; Texas Rsa 18 Limited Partnership; Cingular Wireless Spectrum Sub B LLC; and Corpus Christi SMSA Limited Partnership (collectively

customers to purchase an approved handset in order to subscribe to the defendant's wireless telephone services constitutes an unlawful tying arrangement in violation of Section 1 of the Sherman Act, [15 U.S.C. § 1](#). Specifically, defendants collectively move for summary judgment on three grounds: 1) that none of them has sufficient economic power in the market for wireless services to coerce the purchase of wireless handsets, 2) that the plaintiffs have offered no evidence of anticompetitive effects in the market for wireless handsets; and 3) that the plaintiffs have supplied no evidence of antitrust damages. Four of the defendants, Verizon Wireless, Cingular, T-Mobile, and Sprint, have also submitted separate supplemental briefs, asserting, *inter alia*, that they each are entitled to summary judgment on the [\[\\*\\*3\]](#) ground that as a matter of law, none of them tie the sale of handsets to the sale of wireless service. Because the plaintiffs have not presented sufficient evidence to prove that any one defendant has the degree of market power necessary to sustain a tying claim or to show that any of the defendants' alleged tying arrangements has an actual adverse effect on competition in the U.S. market for wireless handsets, defendants' motion is granted.

#### [\[\\*\\*4\]](#) Facts

The plaintiffs bring this action on behalf of themselves and other persons who have purchased cellular or Personal Communications Services ("PCS") (collectively "wireless") telephone services from the defendants from 1998 to the present. They allege that beginning in 1998, the defendants [\[\\*406\]](#) have unlawfully tied the sale of handsets to the sale of wireless services. None of the defendants manufactures handsets, but each of them purchases handsets for direct resale to consumers through their retail stores or for sale to their respective retail agents.

This summary judgment motion requires an understanding of the evolution of the wireless telephone services industry. The facts recited here are either undisputed or as shown by the plaintiffs, unless otherwise identified. A brief description of the history of this litigation and the context for the summary judgment motions precedes the factual recitation.

#### Procedural History

The background and procedural history of this action have been set forth in several prior Opinions, which are incorporated by reference.<sup>2</sup> Familiarity with these Opinions is assumed, and only the procedural history relevant to the instant motion [\[\\*\\*5\]](#) is described here.

On April 5, 2002, the plaintiffs in an action captioned *Brook v. AT&T Cellular Servs. Inc.*, No. 02 Civ. 2637, filed suit in this District, alleging that several wireless services providers violated federal [antitrust law](#). On November 19, 2002, a conference was held in the *Brook* action, at which it was agreed that the defendants' motions to dismiss would be dismissed as moot and that plaintiffs could amend their complaint on the understanding that [\[\\*\\*6\]](#) such amended pleading would essentially be the last. On January 9, 2003, the *Brook* plaintiffs filed an amended complaint, which alleged that each defendant individually ties the sale of handsets to the provision of wireless

"Cingular"); Sprint Spectrum, L.P.; Wirelessco, L.P.; and Sprintcom, Inc. (collectively "Sprint"); T-Mobile USA, Inc., f/k/a VoiceStream Wireless Corporation; Omnipoint NY MTA License, LLC; Omnipoint New York D License, LLC; Omnipoint Facilities Spectrum 2 LLC; Omnipoint Boston Area DE License, LLC; Omnipoint Boston D License, LLC; VoiceStream GSM I License Co., LLC; VoiceStream GSM II, LLC; VoiceStream PCS BTA I License Corp.; VoiceStream PCS II License Corp.; Cook Inlet/VS GSM IV PCS, LLC; and Omnipoint Holdings, Inc. (collectively "T-Mobile"); and Celco Partnership d/b/a Verizon Wireless; New York SMSA Limited Partnership d/b/a Verizon Wireless; San Antonio MTA, LP; Chicago SMSA Limited Partnership; and GTA Mobilenet of California Limited Partnership (collectively "Verizon Wireless").

<sup>2</sup> See, e.g., [In re Wireless Tel. Servs. Antitrust Litig., 2003 U.S. Dist. LEXIS 13886, No. 02 Civ. 2637 \(DLC\), 2003 WL 21912603 \(S.D.N.Y. Aug. 12, 2003\)](#); [In re Wireless Tel. Servs. Antitrust Litig., 2004 U.S. Dist. LEXIS 5949, No. 02 Civ. 2637 \(DLC\), No. 02 Civ. 2637 \(DLC\), 2004 WL 764833 \(S.D.N.Y. Apr. 9, 2004\)](#); [In re Wireless Tel. Servs. Antitrust Litig., 2004 U.S. Dist. LEXIS 8607, No. 02 Civ. 2637 \(DLC\), 2004 WL 1087262 \(S.D.N.Y. May 17, 2004\)](#); [In re Wireless Tel. Servs. Antitrust Litig., 2004 U.S. Dist. LEXIS 19977, No. 02 Civ. 2637 \(DLC\), 2004 WL 2244502 \(S.D.N.Y. Oct. 6, 2004\)](#).

services and that each of the five defendants monopolizes the market for wireless handsets compatible with its wireless services. The defendants jointly moved to dismiss the amended complaint on February 21, 2003. Shortly thereafter, the Judicial Panel on Multidistrict Litigation ("JPMDL") transferred four putative class actions raising similar claims as *Brook* to this Court.

Through an August 11, 2003 Order, and with the agreement of the parties, the *Brook* action and the four transferred actions were consolidated for pretrial purposes. The August 11 Order noted that any action relating to the same subject matter as these five actions would be consolidated with them and provided that the amended complaint filed in the *Brook* litigation would serve as the Consolidated Amended Class Action Complaint for all actions "alleging antitrust claims against national wireless services carriers and assigned to the undersigned which is subsequently filed in or [\*\*7] transferred to this Court." [Brook v. AT&T Cellular Servs., 2003 U.S. Dist. LEXIS 13796, Nos. 02 Civ. 2637, 03 Civ. 1712 \(DLC\), 03 Civ. 1713 \(DLC\), 03 Civ. 1714 \(DLC\), 03 Civ. 1715 \(DLC\), 2003 WL 21911123, at \\*1 \(S.D.N.Y. Aug. 11, 2003\)](#). The August 11 Order further provided that the consolidated actions would be collectively referred to as *In re Wireless Telephone Services Antitrust Litigation*. *Id.*

An Opinion and Order issued the subsequent day, August 12, 2003, addressed the defendants' joint motion to dismiss. [In re Wireless, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603](#) ("Motion to Dismiss Opinion"). The Motion to Dismiss Opinion dismissed all of the plaintiffs' monopolization claims on the ground that the plaintiffs failed to define properly the relevant [\*407] market. [2003 U.S. Dist. LEXIS 13886, \[WL\] at \\*9-10](#). In declining to dismiss the tying claim, however, the Motion to Dismiss Opinion first observed that the plaintiffs had not alleged that the defendants "engaged in a conspiracy to tie or to raise handset prices, []or that they have entered into any kind of an agreement with each other regarding bundling or handset pricing." [2003 U.S. Dist. LEXIS 13886, \[WL\] at \\*6](#). Instead, the Opinion noted, "each Defendant is alleged to have independently [\*\*8] violated the *Sherman Act* by virtue of the tying arrangement of its own services and handsets." *Id.* Given that, the Motion to Dismiss Opinion concluded that the plaintiffs failed to state a *per se* tying claim as none of the defendants were alleged to "dominate the wireless service market." [2003 U.S. Dist. LEXIS 13886, \[WL\] at \\*7](#).

As the plaintiffs alleged that "each of the Defendants possesses sufficient market power such that its tying arrangement adversely affects competition in the tied market," the Motion to Dismiss Opinion held, however, that plaintiffs had sufficiently stated a tying claim under the rule of reason doctrine. *Id.* The Motion to Dismiss Opinion further explained that "at trial, the plaintiffs will have the burden to show that each Defendant's market power and tying arrangement had an anticompetitive impact on the handset market." [2003 U.S. Dist. LEXIS 13886, \[WL\] at \\*8](#). Plaintiffs never objected to this description of their claims, nor did they move for reconsideration of the Motion to Dismiss Opinion. Consequently, fact discovery proceeded on the basis that plaintiffs' tying claim was separately pled against each defendant.

On July 30, 2004, with the close of fact discovery just two months away, plaintiffs [\*\*9] moved for leave to amend their amended complaint. Plaintiffs' proposed second amended complaint included a tying claim, *inter alia*, which alleged that the defendants, both collectively and individually, have significant market power in the tying and tied product markets. Through an October 6, 2004 Opinion and Order, plaintiffs' motion for leave to amend was denied. [In re Wireless, 2004 U.S. Dist. LEXIS 19977, 2004 WL 2244502, at \\*1](#). The October 6 Opinion explained that the plaintiffs' proposed second amended complaint would "transform the lawsuit from one asserting five tying claims against each of the defendants individually to a lawsuit alleging collective action on the tying claim." [2004 U.S. Dist. LEXIS 19977, \[WL\] at \\*6](#). The October 6 Opinion further noted that having included conspiracy allegations in its original complaint, which they then chose to drop, the plaintiffs' decision to "reassert the conspiracy allegations they initially abandoned" could not constitute the good cause needed for "a substantial and untimely amendment" that would significantly delay the resolution of the litigation.<sup>3</sup> *Id.*

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<sup>3</sup> On August 17, 2004, while the motion to amend was being briefed, plaintiffs' counsel, representing a separate plaintiff, also brought an action in the Northern District of California captioned *Freeland v. AT&T Corp.* The *Freeland* action, which was transferred to this Court by the JPMDL in November 2004 and is now captioned 04 Civ. 8653 (DLC), not only alleges that the defendants in this action have engaged in collective action to tie the sale of handsets to wireless services, but also charges that by engaging in certain practices, the defendants have entered into a conspiracy to restrain trade and contracts in restraint of

[\*\*10] Fact discovery in this action closed on October 8, 2004, and expert discovery ended on January 21, 2005. The defendants jointly moved for summary judgment on February 28, 2005, and briefing was complete on this motion, including the related [\*408] motions to strike certain declarations and expert testimony, on June 17, 2005.  
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The parties have made extensive submissions in connection with this motion and the associated motions *in limine* and motions to strike. Because of the analysis that follows, it is only essential to set forth a small portion of the factual material presented through these motions. The essential facts as shown through the evidence presented with these motions include the following.

#### *The Evolution of Wireless Services in the U.S.*

Wireless telephone service was first introduced in the U.S. in the early 1980s. At that time, the [\*\*11] Federal Communications Commission ("FCC") allocated spectrum such that only two companies could provide service in any given market. Beginning in 1995, however, the FCC auctioned new spectrum for PCS, which ultimately consisted of more than twice the amount of spectrum previously allocated to wireless telephone service. The allocation of PCS spectrum enabled as many as eight competitors to operate within a single market.<sup>5</sup> As PCS providers began operating their networks, the number of wireless subscribers rose from under 25 million in 1994 to 86 million in 1999. In 2003, over 160 million people subscribed to wireless service.

The mid-1990s increase in the amount of spectrum allocated paralleled and enabled another significant change in the wireless industry: the switch from analog to digital technology. Although the FCC had maintained a specific technological standard for [\*\*12] analog service, it decided not to do so for digital service. Consequently, multiple digital technologies were introduced in the mid-1990s, among them CDMA, which is used by Sprint and Verizon Wireless; and GSM, which is used by T-Mobile and to which Cingular and AT&T Wireless are in the process of converting their networks.<sup>6</sup> The parties dispute the compatibility of these technologies. While the defendants assert that these technologies are mutually incompatible, the plaintiffs state that they are only incompatible to the extent that the carriers have manipulated them so as to inhibit a consumer's ability to use her wireless telephone, or handset, with multiple carriers and to heighten the costs of switching from one carrier to another.

While the defendants employ varying digital protocols, each defendant has captured similar benefits [\*\*13] from the advent of digital service. Digital service not only expanded the types of services wireless carriers can provide, enabling, among other things, caller ID, text messaging, and e-mail, but it also eradicated some of the security problems, such as service theft and eavesdropping, associated with analog service. Most importantly, however, digital service enabled wireless service providers to accommodate more users within any given amount of spectrum, thereby reducing their need to set up additional transmitters or cell sites.

Digital technology has also wrought major changes in consumer use and the providers' revenue. In 1994, the average [\*409] monthly usage per subscriber was 119 minutes. This figure rose to 185 minutes in 1999 and skyrocketed to 507 minutes by 2003. During the same time frame, the providers' average revenue per minute fell from 47 cents to 10 cents with a 66 percent drop alone from 1998 to 2003.

trade in violation of [Section 1 of the Sherman Act](#), and a conspiracy to monopolize in violation of [Section 2 of the Sherman Act](#). Plaintiffs' motion for an order setting a pretrial schedule in the *Freeland* action is pending, as is defendants' cross-motion to dismiss the *Freeland* action as duplicative.

<sup>4</sup> On February 25, 2005, the plaintiffs moved for class certification. Because of the resolution of the instant motion, it is unnecessary to rule on that motion.

<sup>5</sup> Since the mid-to-late 1990s, another frequency block, referred to as SMR spectrum, has also been used for wireless telephone services.

<sup>6</sup> The two other digital technologies are TDMA, which is now obsolete and from which Cingular and AT&T Wireless are switching, and iDEN, the technology used by non-party Nextel.

### *The Development of Handsets and How They've Changed*

Because wireless service providers cannot implement more efficient service unless subscribers are using handsets that operate on their respective networks, handsets sold for use in the U.S. wireless services [\*\*14] market are developed by manufacturers in collaboration with the wireless service providers. The quality of handsets available to subscribers is particularly important to the service providers because the use of "outmoded" handsets not only affects the quality of that subscriber's service, but also diminishes the quality of service to other subscribers. As a result, at least two of the defendants, Verizon Wireless and AT&T Wireless, subject or have subjected handset models to an approval process involving testing and maintain a list of models approved for use with their respective services.

It is undisputed that the handset manufacturers compete with one another to offer the highest quality, maximum spectral efficiency, and lowest prices to the wireless service providers who purchase their handsets. The parties dispute, however, whether certain companies have manufactured or currently do manufacture wireless telephones, and more importantly, whether the handset market has been "dynamic" since 1999.<sup>7</sup> In addition, while the parties agree that certain companies, including Sony, Palm, Hewlett Packard, Danger, and RIM, have entered the U.S. handset market during the relevant time frame, [\*\*15] the plaintiffs argue that these entrants collectively account for an insignificant portion of the U.S. handset market.

In 1995, just three percent of handsets sold in the U.S. were digital. By contrast, by 2000, essentially all handsets sold in the U.S. were digital. Today's digital handsets feature many improvements over their predecessors, such as enhanced battery life, smaller size and diminished weight, and a host of improved features, including automatic redial, speed dial, alarm clocks, address books, speakerphones, voice-activated dialing, and color screens. All of the defendants also currently sell handsets equipped with cameras as well as data [\*\*16] services, such as text messaging, the downloading of ring tones, music, and games. Even as handsets have become increasingly more sophisticated, the cost of handsets has dropped.<sup>8</sup>

Just as the parties dispute the inherent compatibility of the various digital technologies with one another, they also dispute whether a handset designed to work on one digital network can function on another network. The plaintiff argues, for example, that certain handsets are designed to operate across multiple protocols, but that the defendants program the handsets used in conjunction with their respective [\*410] service so as to prevent such [\*\*17] usage. In addition, the parties dispute the extent to which consumers desire the innovations now featured on handsets and disagree as to whether handsets offered in the U.S. sufficiently incorporate other emerging technologies.

### *The Distribution and Sale of Handsets in the U.S.*

It is undisputed that since the inception of wireless service in the U.S., wireless service providers have sold their respective service and handsets as a package, and that in doing so, the carriers have subsidized the cost of handsets to make initial entry into the wireless services market "more palatable." Although wireless handsets have become much more affordable over the last fifteen years, wireless service providers continue to package service and handsets, subsidizing the latter, "to continue to open up markets and make it affordable" for consumers to obtain wireless service.

The plaintiffs allege that in an effort to prevent customers from switching carriers, each of the defendants requires that handsets sold for use with its respective network are programmed, or "locked," to prevent the use of such

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<sup>7</sup> The parties dispute which entities can appropriately be called handset manufacturers. The defendants contend that companies that develop and build handsets and then sell them under different brand names should be considered manufacturers. The plaintiffs, by contrast, argue that only the company listed as a handset's manufacturer should be considered as such.

<sup>8</sup> The plaintiffs argue, by way of citation to the expert report of Nicholas Economides, that even though the wholesale prices for digital handsets have dropped since 2000, they were artificially inflated between 1999 and 2003 as a direct result of the defendants' tying arrangements. For reasons that will be described below, Economides's analysis of handset prices cannot be admitted into evidence.

handsets with another carrier.<sup>9</sup> [\*\*19] The defendants deal with this assertion in varying [\*\*18] ways. Verizon Wireless, for example, contends that it does not lock handsets on the ground that its "post-pay"<sup>10</sup> handsets are set to a widely-known default equivalent to leaving a handset unlocked. By contrast, T-Mobile acknowledges that since the mid-1990s, the handsets sold for use on its network have featured locked SIM cards, hardware chips embedded in handsets that identify a particular user and allow her access to a specific network. T-Mobile contends that it employs handset locking to prevent retailers from selling and/or activating T-Mobile-subsidized handsets on other networks and to deter theft on the basis that it can deactivate the SIM card of a stolen handset.<sup>11</sup> T-Mobile further asserts that it has a policy of unlocking any handset at a subscriber's request.

The parties also dispute the extent to which the defendants' sales of wireless service are tied to that of handsets and whether aside from their direct handset sales, the defendants also dominate the purchase and distribution of handsets that are sold subsequently to consumers through other, non-carrier-owned retail channels. This Opinion does not reach the legal issue most closely associated with these disputes: whether as a condition of receiving wireless services from a particular defendant, consumers are required to purchase a handset from that defendant as well. Nevertheless, so as to provide a full picture of the wireless services industry, it is necessary to illustrate how the distribution and sale of handsets in the U.S. function.

The following paragraph uses Verizon Wireless, which, as of 2003, possessed the largest market share among U.S. wireless service providers and among the defendants, as an example of how the defendants [\*\*20] sell and/or distribute handsets. Like other carriers, Verizon Wireless not only operates its own retail stores, but it also maintains agreements with more than 2,000 sales agents, which are authorized to [\*411] sell its service and which independently sell handsets as well. In acquiring the handsets they sell to consumers, Verizon's sales agents "typically have the right to purchase either from Verizon Wireless or from third-party sources, provided that the handsets purchased are approved for operation on Verizon Wireless's CDMA network." Although large retailers, such as Radio Shack, often choose to purchase handsets directly from Verizon Wireless, retailers' contracts with Verizon Wireless specifically empower them to purchase equipment through non-Verizon sources, notably manufacturers or distributors, so long as such equipment has been approved by Verizon and is prepared for use on Verizon's network.<sup>12</sup> These contracts also reflect that most covered retailers establish handset prices without Verizon's involvement and that they have responsibility for the installation and maintenance, as well as warranties for, the handsets they sell.

#### [\*\*21] *The Changing Structure of the Wireless Industry*

Since the late 1990s, the structure of the wireless services industry has fundamentally changed. Just as digital technology offers certain efficiencies, so too does having a nationwide network, which eliminates a provider's need to pay roaming costs to other carriers. Whereas some carriers, such as AT&T Wireless, already had extensive geographic coverage by the late 1990s, other, more regionally-focused carriers began to join forces to achieve nationwide coverage. Verizon Wireless, Cingular, and T-Mobile, all of which now provide national coverage, each

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<sup>9</sup>A substantial share of plaintiffs' evidentiary submissions regarding locking concerns the defendants' coordinated efforts, primarily through various wireless industry organizations, to promulgate handset locks as an industry standard by requiring manufacturers to incorporate such locks in handsets developed for use with their respective networks.

<sup>10</sup>Verizon does not define, however, what it means by "postpay."

<sup>11</sup>Sprint, which also admits to locking handsets, cites similar justifications for locking.

<sup>12</sup>Pursuant to an agreement with the plaintiffs, approximately one dozen contracts were produced and served as a sample. This paragraph also relies on the declaration of Thomas Bryant, an associate director for indirect distribution for Verizon Wireless. The plaintiffs have moved to strike the Bryant declaration, *inter alia*, because he did not sufficiently disclose the bases of his personal knowledge and on other grounds. The motion to strike is denied; the defendants have cured any relevant deficiencies. This Opinion determines that the defendants are entitled to summary judgment even if they control sales and distribution in the U.S. handset market.

emerged from the combination of smaller carriers in 2000.<sup>13</sup> **[\*\*22]** More recently, AT&T Wireless and Cingular merged in 2004, and Sprint merged with Nextel, a non-party to this action, in 2005.<sup>14</sup>

Pursuant to congressional mandate, since 1995, the FCC has reported annually **[\*412]** on competitive conditions in the wireless services industry.<sup>15</sup> Such reports reveal the changing nature of the wireless services industry. According to the FCC, in 1998, none of the five largest service providers possessed more than 11 **[\*\*23]** percent of the nationwide market, and together, they comprised only 47 percent of the market. Since 2000, however, Verizon Wireless has maintained a 24 percent market share, and in 2003, the five largest wireless service providers accounted for 70 percent of the market. The FCC reports that Verizon's market share of 24 percent is the largest in the industry; that Cingular's market share has fluctuated between 15 and 18 percent; that AT&T has held between 10 and 15 percent; that Sprint's share has never exceeded 11 percent; and that T-Mobile has never held more than 8 percent. The FCC has also reported that as of 2004, 97 percent of the American population could choose from at least three providers that own their own network, and 87 percent of the population had a choice of at least five carriers.

In the above-referenced reports, the **[\*\*24]** FCC has not only assessed the carriers' respective market shares but has also observed other indicia of competition, such as "the continued rollout of differentiated pricing plans" by different providers, which it has recognized since 2001. In 2003, for instance, the FCC described the wireless providers as exhibiting "independent pricing behavior, in the form of continued experimentation with varying pricing levels and structures, for varying service packages, with various available handsets and policies on handset pricing." The FCC has also measured how many customers each wireless service provider typically loses per month, a figure known in the industry as "churn." Since 2000, wireless service providers have lost 1.5 to 3 percent of their customers each a month, resulting in a loss, or "churn," of between 18 and 36 percent of customers each year.

On the basis of specific findings such as these, the FCC has repeatedly described the wireless services market as competitive. In 1999, for instance, the FCC observed "steady competitive progress" in the wireless services industry; in 2000, it found the industry continuing to benefit from "the effects of increased competition as evidenced **[\*\*25]** by lower prices to consumers and increased diversity of service offerings;" in 2001 and 2002, it determined the industry featured "increased competition;" in 2003, it concluded that "effective competition" was present in the wireless services market; and in 2004, it wrote that "U.S. consumers continue to benefit greatly from robust competition in the marketplace."

<sup>13</sup> As the FCC related in 2004,

Verizon Wireless's national system was based on a combination of wireless-owned systems (Bell Atlantic, NYNEX, GTE) with those accumulated and consolidated by Vodafone (including AirTouch). Cingular was formed by merging SBC's (including former SNET, PacBell, and Ameritech) and BellSouth's systems. T-Mobile acquired the systems constructed and combined by VoiceStream and Omnipoint.

Mem. Op. & Order, [Applications of AT&T Wireless Servs., Inc. and Cingular Wireless Corp. for Consent to Transfer Control of Licenses and Authorizations, 19 FCC Rcd 21522 \(2004\)](#) ("AT&T/Cingular Order").

<sup>14</sup> Through an August 8, 2005 memorandum opinion and order, the FCC approved the merger of Sprint and Nextel. See Mem. Op. & Order, [Applications of Nextel Comm., Inc. and Sprint Corp. for Consent to Transfer Control of Licenses and Authorizations, 2005 FCC LEXIS 4524, FCC 05-148, WC Docket No. 05-63 \(Aug. 8, 2005\)](#) ("Sprint/Nextel Order"). In an August 16, 2005 letter, the defendants argue that this order, which concludes that the wireless services industry is characterized by vigorous competition and that the national service providers are each substitutes for one another, should be considered in connection with this motion. Because the briefing of this motion was completed before the issuance of the Sprint/Nextel Order, it will not be relied upon in reaching the merits of the defendants' motions.

<sup>15</sup> The plaintiffs do not dispute the accuracy of the FCC's findings, but instead dispute their import, arguing that they do not address the defendants' alleged tying arrangements.

In 2004, Cingular and AT&T Wireless merged, a transaction that required FCC approval and generated substantial analysis of the industry as a whole by the FCC. In approving this merger, the FCC noted that its approval of such mergers is conditioned on a finding that it is in the public interest, which entails honoring the [Communications Act's](#) "deeply rooted preference for preserving and enhancing competition in relevant markets." With this mandate in mind, the FCC concluded that "the nationwide firms are all relatively close substitutes for each other in the eyes of consumers and that the nationwide firms," meaning Verizon Wireless, Sprint, T-Mobile, and Nextel, "have the incentive and ability to reposition in response to any attempted exercise of market power by the merged firm."<sup>16</sup> AT&T Wireless Order at P 147.

## [\*\*26] [\*413] Discussion

**HN1** Summary judgment may be granted only "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." [Rule 56\(c\), Fed. R. Civ. P.](#); see also [Sec. Ins. Co. of Hartford v. Old Dominion Freight Line, Inc., 391 F.3d 77, 82 \(2d Cir. 2004\)](#). **HN2** "The burden of showing that no genuine factual dispute exists rests on the party seeking summary judgment, and in assessing the record to determine whether there is a genuine issue as to a material fact, the court is required to resolve *all ambiguities* and draw *all permissible factual inferences* in favor of the party against whom summary judgment is sought." [Old Dominion Freight Line, 391 F.3d at 83](#) (citation omitted) (emphasis supplied).

**HN3** When the moving party has asserted facts showing that it is entitled to summary judgment, the opposing party must "set forth" specific facts showing that there is a genuine issue for trial, and cannot rest on the "mere allegations or denials" of the movant's pleadings. [Rule 56\(e\), Fed. R. Civ. P.](#); accord [Burt Rigid Box, Inc. v. Travelers Prop. Cas. Corp., 302 F.3d 83, 91 \(2d Cir. 2002\)](#). If there is evidence, however, "from which a reasonable inference could be drawn in favor of the opposing party, summary judgment is improper." [Old Dominion Freight Line, 391 F.3d at 83](#) (citation omitted).

**HN4** In the realm of [antitrust law](#), "summary judgment serves a vital function," [Tops Markets, Inc. v. Quality Markets, Inc., 142 F.3d 90, 95 \(2d Cir. 1998\)](#), by avoiding "wasteful trials and prolonged litigation that may have a chilling effect on procompetitive market forces." [Virgin Atlantic Airways Ltd. v. British Airways PLC, 257 F.3d 256, 263 \(2d Cir. 2001\)](#) (citation omitted). "If the plaintiff's theory is economically senseless, no reasonable jury could find in its favor, and summary judgment should be granted." [Eastman Kodak Co. v. Image Technical Servs., 504 U.S. 451, 468-69, 112 S. Ct. 2072, 119 L. Ed. 2d 265 \(1992\)](#). Nevertheless, [\*28] "no special burden is imposed on a plaintiff opposing summary judgment in an antitrust case." [Virgin Atlantic, 257 F.3d at 262](#) (citation omitted).

### I. Legal Framework

#### A. Elements of Tying

[Section 1 of the Sherman Act](#) provides that **HN5** "every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal." [15 U.S.C. § 1](#). The Sherman Act exists "to protect competition, not individual competitors." [Virgin Atlantic, 257 F.3d at 265](#).

**HN6** Among the activities prohibited by [Section 1](#) are restraints of trade in the form of "an agreement by a party to sell one product but only on the condition that the buyer also purchase a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier." [Eastman Kodak, 504 U.S. at 461](#) (citation omitted); see also Edward M. Iacobucci, *Tying as Quality Control: A Legal and Economic Analysis*, [32 J. Legal Stud. 435, 435 \(2003\)](#). Such agreements are known as tying arrangements. Courts have repeatedly emphasized [\*29] that

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<sup>16</sup> Again, the plaintiffs do not challenge the FCC's findings in the AT&T/Cingular Order but argue that the order "does not address the issue of tying in the context of the merger."

385 F. Supp. 2d 403, \*413L 2005 U.S. Dist. LEXIS 18293, \*\*29

the essential characteristic of an invalid tying arrangement lies in the seller's [\*414] exploitation of its control over the tying product to force the buyer into the purchase of the tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms.

Hack v. President and Fellows of Yale College, 237 F.3d 81, 85 (2d Cir. 2000) (citing Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 12, 80 L. Ed. 2d 2, 104 S. Ct. 1551 (1984)).

**HN7**[] When a consumer is forced to purchase a tied product when the consumer would not do so in a competitive market, a tying arrangement is unlawful. See Jefferson Parish, 466 U.S. at 13-14. In essence, a seller may not use its market power in one market "to impair competition on the merits in another market." Id. at 14. Competition in the tied market can be impaired by injuring existing businesses in the market or creating barriers to entering the market. *Id.* The consumer is injured when her freedom to select the best bargain is impaired by her need to purchase the tying product. Id. at 15. She may also be injured when she is unable to evaluate [\*\*30] the true cost of either product when they are only available as a package. *Id.*

Both before and after the Supreme Court's 1984 decision in *Jefferson Parish*, which is viewed as one of the Court's most significant decisions on Sherman Act tying claims, **HN8**[] the Second Circuit has required proof of five specific elements to state an unlawful tying claim:

first, a tying and a tied product; second, evidence of actual coercion by the seller that forced the buyer to accept the tied product; third, sufficient economic power in the tying product market to coerce purchaser acceptance of the tied product; fourth, anticompetitive effects in the tied market; and fifth, the involvement of a 'not insubstantial' amount of interstate commerce in the tied market.

Hack, 237 F.3d at 86; see also DeJesus v. Sears, Roebuck & Co., 87 F.3d 65, 70 (2d Cir. 1996); Gonzalez v. St. Margaret's House Housing Dev. Fund Corp., 880 F.2d 1514, 1516-17 (2d Cir. 1989); Yentsch v. Texaco, Inc., 630 F.2d 46, 56 (2d Cir. 1980).

#### B. The Per Se Rule of Tying

As the Supreme Court has repeatedly held, **HN9**[] "certain tying arrangements [\*\*31] pose an unacceptable risk of stifling competition and therefore are unreasonable 'per se.'" Jefferson Parish, 466 U.S. at 9. Analysis under the *per se* rule is, by definition, "without inquiry into actual market conditions." Id. at 15. Put another way, where a tying arrangement may be condemned as illegal *per se*, plaintiffs need not allege, let alone prove, facts addressed to the fourth element. Wal-Mart Stores, Inc. v. Visa USA Inc. (In re Visa Check/MasterMoney Antitrust Litig.), 280 F.3d 124, 133 n.5 (2d Cir. 2001); In re Wireless, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, at \*4-5. If a plaintiff succeeds in establishing the existence of sufficient market power to create a *per se* violation, the plaintiff is also relieved of the burden of rebutting any justifications the defendant may offer for the tie.

**HN10**[] A tying arrangement may be condemned as illegal *per se* only "if the existence of forcing is probable" because there is a "substantial potential for impact on competition." Jefferson Parish, 466 U.S. at 15-16. While the Supreme Court has never defined how much market power is necessary to condemn a tying arrangement as illegal *per se*, the [\*\*32] *Jefferson Parish* Court concluded that a thirty percent market share was "far from overwhelming" and did "not establish the kind of dominant market position" that entitles a plaintiff to a finding that the [\*415] tying arrangement is *per se* illegal. Id. at 26-27.

#### C. The Rule of Reason

**HN11**[] Where the plaintiff has alleged a tying violation, and the showing of market power is insufficient to find a *per se* violation of antitrust law, courts apply a rule of reason analysis at the fact-finding stage through a burden-shifting scheme. In re Wireless Tel. Servs., 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, at \*5, 7. Specifically, the plaintiffs "bear an initial burden to demonstrate the defendants' challenged behavior had an *actual* adverse effect on competition as a whole in the [tied product] market." Geneva Pharms. Tech. Corp. v. Barr Labs., Inc., 386 F.3d 485, 506-07 (2d Cir. 2004) (citation omitted) (emphasis in original); see also In re Visa Check, 280 F.3d at 134 n.5.

"Whether an actual adverse effect has occurred is determined by examining factors like reduced output, increased prices and decreased quality." [Virgin Atlantic, 257 F.3d at 264](#). [\*\*33] So too may a demonstration of "significant barriers to entry into [a particular] market" show an actual adverse effect on competition. [CDC Techs., Inc. v. IDEXX Lab., Inc., 186 F.3d 74, 80 \(2d Cir. 1999\)](#). If the plaintiff fulfills this preliminary burden, however, "the burden shifts to the defendants to offer evidence of the pro-competitive effects of their agreement." [Geneva Pharms. Tech. Corp., 386 F.3d at 507](#) (citation omitted). "Assuming defendants can provide such proof, the burden shifts back to the plaintiffs to prove that any legitimate competitive benefits offered by defendants could have been achieved through less restrictive means." *Id.* (citation omitted).

#### D. Market Power in a Rule of Reason Case

**HN12**[<sup>16</sup>] The third element of a tying claim -- market power in the tying product market -- requires that the plaintiff prove that the defendant has "the power to force a purchaser to do something that he would not do in a competitive market," which is often equated with "the ability of a single seller to raise price and restrict output." [Eastman Kodak, 504 U.S. at 464](#) (citation omitted). A seller's market power "ordinarily is inferred [\*\*34] from [its] possession of a predominant share of the market." *Id.* Nevertheless, market power may also exist in other circumstances, such as where "the government has granted the seller a patent or similar monopoly over a product," [Jefferson Parish, 466 U.S. at 16](#), or "when the seller offers a unique product that competitors are not able to offer." [Id. at 17](#).

As noted above, **HN13**[<sup>17</sup>] the Second Circuit requires proof of market power in all tying cases. As the Court observed in *Jefferson Parish*, "without evidence that [defendants] are using market power to force" consumers to purchase the product or service in the tied market, "there is no basis to view the arrangement as unreasonably restraining competition." [Jefferson Parish, 466 U.S. at 24 n.40](#). This is so, because "only if" consumers "are forced to purchase" the tied product "as a result of [the defendants'] market power would the arrangement have anticompetitive consequences." [Id. at 25](#). In her concurrence in *Jefferson Parish*, Justice O'Connor emphasized the centrality of a market power analysis for tying claims even as she argued that it was time to abandon [\*\*35] the *per se* label for a class of tying claims.<sup>17</sup> She recommended [\*416] reducing all analysis of tying claims to a three-part inquiry, the first element of which would be an unqualified requirement that the seller have "power in the tying product market." [Id. at 35, 38](#) (O'Connor, J., concurring).<sup>18</sup> As the Honorable Frank H. Easterbrook has written in connection with his analysis of a tying claim,

**Antitrust law** is based on the premise that when markets are competitive, the process of sellers' rivalry and buyers' choice produces the best results. Unless courts insist on a showing of market power, they run the risk of deleting one of the existing options and so reducing rather than enhancing the vigor of competition and the welfare of consumers.

[Will v. Comprehensive Accounting Corp., 776 F.2d 665, 673-74 \(7th Cir. 1985\)](#).

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Since *Jefferson Parish*, most Circuit Courts of Appeals have explicitly insisted on a showing of market power for a plaintiff to succeed on a tying claim. The Sixth and Seventh Circuits have adopted the three-step analysis proposed by Justice O'Connor, including the threshold requirement of a showing of market power for all tying claims. See

<sup>17</sup> While continuing to list proof of market power as an essential component of a tying claim, the Second Circuit has not yet addressed the ramifications of the *Jefferson Parish* majority and concurring opinions in any detail. In *Gonzalez*, the sole occasion on which our Circuit has even commented on the divergence between the *Jefferson Parish* majority and Justice O'Connor's concurrence, the Honorable Wilfred Feinberg observed that despite "weaknesses in the *per se* tying analysis," the court was obligated to "adhere to the views of a majority of the Supreme Court, which has not abandoned the *per se* test." [Gonzalez, 880 F.2d at 1519](#).

<sup>18</sup> In adopting Justice O'Connor's framework for analysis of all tying claims, the Sixth Circuit noted that in [Eastman Kodak, 504 U.S. at 451](#), issued eight years after [Jefferson Parish, 466 U.S. at 2](#), the majority opinion did not even mention the terms *per se* or rule of reason. [PSI, 104 F.3d at 815 n.2](#).

*PSI Repair Servs., Inc. v. Honeywell, Inc.*, 104 F.3d 811, 815 n.2, 821 (6th Cir. 1997) (affirming summary judgment for defendant for plaintiff's failure to show market power in tying product market); *Hardy v. City Optical Inc.*, 39 F.3d 765, 767 (7th Cir. 1994) (per curiam) (reinstating lawsuit with admonition that district court must find a 30 percent market share [\*\*37] at a minimum); *Hand v. Cent. Transport, Inc.*, 779 F.2d 8, 11 (6th Cir. 1985) (reinstating lawsuit for failure to consider evidence of market power in a submarket); *Will*, 776 F.2d at 673-74 (reversing a jury verdict on a tying claim for a failure to prove defendant had market power). Thus, as the Honorable Richard A. Posner explained in *Hardy*, since "substantial market power is a threshold requirement of all rule of reason" cases in these Circuits, a tying arrangement is not illegal "unless the defendant has substantial market power in the tying product." *Hardy*, 39 F.3d at 767.

Other circuits have disclaimed the requirement of market power for a rule of reason tying claim, but have imported such a requirement through other means. The Third Circuit, for instance, has explained on one hand that *Jefferson Parish* has foreclosed it from requiring a plaintiff to prove the existence of market power in the tying market under a rule of reason analysis, *Town Sound & Custom Tops, Inc. v. Chrysler Motors Corp.*, 959 F.2d 468 at 485, yet it imposes an equivalent burden on a plaintiff by requiring a showing of a "plausible theory of causation of injury of the type the [\*\*38] antitrust laws were designed to prevent," *id. at 486* (citation omitted). The Third Circuit also observes that an antitrust tying claim "falls apart" where a defendant lacks sufficient power in the tying product market to leverage power in the tied product market. *Id.* But see *Grappone, Inc. v. Subaru of New England*, 858 F.2d 792 at 798-99 (proceeding to analyze anti- and pro-competitive effects of the tie after finding that plaintiff had not shown existence of market power in the tying market).<sup>19</sup>

[\*\*39] [\*417] The law regarding what constitutes sufficient market power to create an illegal tie is still developing. Consistent with *Jefferson Parish*, both the Sixth and Seventh Circuits, however, have opined that thirty percent serves as the minimum market share from which the market power in the tying product market can be inferred. *Hardy*, 39 F.3d at 767; *PSI Repair Servs.*, 104 F.3d at 815 n.2, 818. In *Town Sound*, the Third Circuit acknowledged the thirty percent threshold and found that Chrysler's share of 10 to 12 percent of the United States car market did not create "any genuine issue of material fact" as to its "economic power" in that market. *Town Sound*, 959 F.2d at 481.

## II. Defendants' Motion for Summary Judgment: Market Power

Defendants move for summary judgment on the ground that the plaintiffs have not presented evidence raising a question of fact that any one of the defendants had sufficient power in the market for wireless service to "force" consumers, within the meaning of the federal antitrust laws, to purchase unwanted handsets. The defendants are correct.

None of the defendants enjoys a market share that would, [\*\*40] standing alone, permit an inference of market power to be drawn, and the plaintiffs have not shown that questions of fact exist with respect to any other issue which, when combined with a defendant's market share, would allow a finding of market power. Between 1998 and 2003, no defendant has ever possessed more than twenty-four percent of the wireless services market.<sup>20</sup> At the

<sup>19</sup> Despite the repeated emphasis of the *Jefferson Parish* Court on the importance of proof of market power to a tying claim, some courts have fixated on the fact that, after finding that the defendant did not have sufficient market power to warrant application of a *per se* tying analysis, the Court proceeded to analyze the claim without further discussion of the defendant's market power. Having already accepted that the defendant had a 30 percent market share, *466 U.S. at 26*, a number it characterized as "far from overwhelming," *id.*, there was no obvious need for the Court to discuss the defendant's market power further. When the entire *Jefferson Parish* decision is read, and even more so when it is read with the other decisions that comprise the Court's tying jurisprudence, it is obvious that proof of market power remains a critical component of a tying claim.

<sup>20</sup> Defendants acknowledge that Cingular and AT&T Wireless's combined market share in 2003 was 29 percent. Cingular and AT&T Wireless did not even announce, much less complete, their merger until 2004. Given that the defendants assert that the plaintiffs' tying claims target the period 1998 through 2003, and the plaintiffs do not contest that they and their experts have relied entirely on data from this period to support their tying claims and to estimate their purported damages, it is not necessary to contemplate Cingular's post-merger market share.

end of 1998, when plaintiffs allege that each of the defendants (or their predecessors) first tied their service to the purchase of handsets, the largest wireless service provider carried no more than eleven percent of subscribers. The defendants compete against each other in terms of service and price, and the high churn rate is striking evidence of their respective lack of control over the market and the impediments each of them faces to any effort to control price.

[\*\*41] The plaintiffs acknowledge that vigorous competition exists in the wireless services market and that to succeed on a tying claim that they must show that a defendant holds market power, but urge that they need make "only a minimal showing of market power," citing [\*Northern Pac. R. Co. v. United States\*, 356 U.S. 1, 6, 7-8, 11, 2 L. Ed. 2d 545, 78 S. Ct. 514 \(1958\)](#).<sup>21</sup> *Northern Pacific* provides no comfort to the plaintiffs.

[\*418] In *Northern Pacific*, the Court upheld an injunction issued against the Northern Pacific Railway Company that barred it from enforcing or entering into preferential routing clauses. [\*\*42] The railroad had received forty million acres of land in several northwestern states and territories to facilitate its construction of a railroad line, and had sold or leased most of this land. Most of the sales contracts and lease agreements contained a preferential routing clause that required the purchaser or lessee to ship all commodities produced or manufactured on that land over its railroad. For a large portion of these shipments there were two other major competing railroad systems. [\*Id. at 517\*](#). The Court defined the illegality involved in tying as forcing buyers to forego their free choice. [\*Id. at 518\*](#). It observed, "of course where the seller has no control or dominance over the tying product so that it does not represent an effectual weapon to pressure buyers into taking the tied item any restraint of trade attributable to such tying arrangements would obviously be insignificant at most." [\*Id. at 519\*](#). It found that the railroad "possessed substantial economic power by virtue of its extensive land holdings which it used as leverage." *Id.*

*Northern Pacific*, which was written fifty years ago, is entirely consistent with the standards described earlier in this [\*43] Opinion. As more cases have reached the appellate courts, the law regarding what constitutes "sufficient economic power to impose an appreciable restraint," [\*id. at 521\*](#), has become better defined. While the precise amount remains an open question, it has become clear that possession of a 30 percent market share is the minimum sufficient by itself to confer market power. Although *Northern Pacific* did not undertake to define the precise market affected by the railroad's land holdings, or to compute the percentage of its holdings in that market, it nonetheless found the railroad to possess substantial power over a finite but infinitely valuable resource.

The plaintiffs next contend that market shares of less than 30 percent have been found sufficient to create market power in tying cases, citing [\*Rosebrough Monument Co. v. Mem. Park Cemetery Ass'n\*, 666 F.2d 1130, 1143 \(8th Cir. 1981\)](#), as finding that 22 percent was sufficient to invoke the *per se* rule against tying; [\*In re Visa Check/Mastermoney Antitrust Litig.\*, 2003 U.S. Dist. LEXIS 4965, 2003 WL 1712568, at \\*4-5 \(E.D.N.Y. April 1, 2003\)](#), as finding that 26 to 28 percent was sufficient to raise a triable issue on market power for a *per se* tying claim; and [\*United States v. Visa U.S.A., Inc.\*, 163 F. Supp. 2d 322 at 363](#), [\*44] as finding that a 26 percent market share established market power. As *Rosebrough Monument* predates *Jefferson Parish*, its conclusion that the defendants' combined 22 percent market share confers upon them a "unique economic advantage" has negligible force. [\*Rosebrough Monument\*, 666 F.2d at 1143](#).

In addition, neither *Visa Check* nor *Visa* suggests that a 30 percent market share should not be the presumptive line for inferring market power. The *Visa Check* case centered on a claim by several of the nation's largest retailers that Visa and Mastercard "required stores accepting [their] credit cards to also accept their debit cards." [\*In re Visa Check/MasterMoney Antitrust Litig.\*, 192 F.R.D. 68, 71 \(E.D.N.Y. 2000\)](#). The Honorable John Gleeson denied the plaintiffs' motion for summary judgment on their [\*Section 1\*](#) *per se* tying claim. [\*Visa Check\*, 2003 U.S. Dist. LEXIS 4965, 2003 WL 1712568, at \\*6](#). In doing so, Judge Gleeson observed that the tying product market could be defined "at its broadest" as the market for "general purpose credit and charge card services." [\*Visa Check\*, 2003](#)

<sup>21</sup> In denying the motion to dismiss the tying claim, this Court noted that the precise amount of market power necessary to prevail on a tying claim remains an open question, citing a footnote in Justice O'Connor's concurrence in *Jefferson Parish* in which she also described *Northern Pacific* as requiring "only a minimal showing of market power." [\*In re Wireless\*, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, at \\*7](#).

U.S. Dist. LEXIS 4965, 2003 WL 1712568, at \*3. At the same time, however, Judge [\*\*45] Gleeson observed that the relevant evidence suggested "an even narrower product market" consisting of "general purpose credit card services alone." [\*419] *Id.* Therefore, Judge Gleeson assessed MasterCard's share of two alternative markets: the broader market, in which MasterCard's share fluctuated between 26 to 28 percent over the relevant time period, and the more narrowly-defined market, in which it share "varied from between 33 to 36 percent." *Id. 2003 U.S. Dist. LEXIS 4965 , at JWLJ \*4.*<sup>22</sup> Judge Gleeson was asked solely to decide whether those figures were sufficient to impose *per se* liability, and found that he could not, at that stage of the proceeding, conclude as a matter of law that "MasterCard has sufficient economic power to warrant application of the *per se* rule." *Id.* (citation omitted).

The Visa case, which does not involve a tying claim, is no more availing for the plaintiffs. In that case, [\*\*46] the Honorable Barbara S. Jones determined that Visa and MasterCard had market power primarily on the basis of direct evidence demonstrating their "power to control prices or exclude competition" and their "ability to price discriminate." Visa, 163 F. Supp. 2d at 340 (citation omitted). Specifically, Judge Jones noted plaintiffs' evidentiary showing that they could not refuse to accept Visa and MasterCard "even in the face of significant price increases because the cards are such preferred payment methods that customers would choose not to shop at merchants who do not accept them." *Id.* Judge Jones further recognized that both defendants had "raised interchange rates charged to merchants" several times "without losing a single customer" and that they were able to charge "substantially different prices" to different categories of merchants because of customers' insistence on using their cards. *Id.* Moreover, with respect to the defendants' market share, Judge Jones found that together Visa and MasterCard controlled over 73 percent of the relevant market in terms of transactions and 85 percent in terms of cards issued, with Visa responsible for 47 percent and MasterCard [\*\*47] responsible for 26 percent. Id. at 341. Judge Jones found that market power could be presumed in the presence of these numbers because there were "significant enough barriers to entry or expansion that the defendant can charge supracompetitive prices without loss of so many customers that the pricing becomes unprofitable." *Id.* The court did not assert that a 26 percent market share always equals market power but instead provided that market power may be presumed where, as in both Visa and MasterCard's cases, the firm has a "large share in a highly concentrated market with significant barriers to entry." Id. at 342.

The plaintiffs next assert that the wireless market is an oligopoly with six nationwide carriers during most of the class period, and that individual businesses in an oligopoly "may" in some circumstances have market power. The plaintiffs identify the following special circumstances as creating market power here: product differentiation, meaning the creation of products understood by consumers to be "distinct commodities;" the need to obtain FCC spectrum licensing, which presents an "absolute" barrier to new entrants into the wireless [\*\*48] service market; and each defendant's control of its own retail handset network. The plaintiffs have not presented evidence to raise a question of fact as to whether any of these alleged factors has created market power for any one of the defendants.

If by product differentiation, the plaintiffs are referring to the efforts that each defendant has made to brand its product, then the plaintiffs have not shown as either [\*420] a matter of law or fact that the creation of a brand has conferred market power on a defendant. HN14[] "A single branded product may, in rare cases, constitute its own relevant market." U.S. Anchor Mfg., Inc. v. Rule Indus., Inc., 7 F.3d 986, 998 (11th Cir. 1993) (citation omitted). "Entrenched buyer preferences for established brands" can also create significant barriers to entry. Rebel Oil Co., Inc. v. Atlantic Richfield Co., 51 F.3d 1421, 1439 (9th Cir. 1995). Yet the mere existence of a brand and brand identification in the marketplace are not synonymous with market power. See, e.g., Grappone, 858 F.2d at 797 (consumer preference for branded product alone cannot demonstrate market power). In general, where "interbrand [\*\*49] competition exists . . . it provides a significant check on the exploitation of interbrand market power because of the ability of consumers to substitute a different brand of the same product." Cont'l T.V., Inc. v. GTE Sylvania, Inc., 433 U.S. 36, 52 n.19, 53 L. Ed. 2d 568, 97 S. Ct. 2549.

The plaintiffs have failed to offer any evidence that branding has created market power for any of the defendants. Instead, they merely cite the testimony of defendants' expert, Jerry Hausman, who testified that products in the wireless services industry "are differentiated to some extent." The enormous amount of churn in this industry

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<sup>22</sup> Visa's share of the more broadly defined market was 43 to 47 percent, and was nearly 60 percent of the narrower market.

eviscerates the suggestion that consumers do not view these brands and the services underlying them as essentially interchangeable. The FCC found, in approving the Cingular/AT&T Wireless merger in 2004, that the defendants, along with non-parties that offer nationwide coverage "are all relatively close substitutes for each other in the eyes of consumers." AT&T/Cingular Order at P 147.

Holding an FCC license for a portion of the spectrum does not confer market power on any one of the defendants since each of them, as well as others not named here as defendants, have FCC licenses. [\*\*50] Moreover, not only may licensees buy and sell spectrum with the FCC's consent, but to compete with the defendants, a seller of wireless services does not even need an FCC spectrum license, as the growth of the mobile virtual network operator<sup>23</sup> system has shown. As a result, no defendant is specially advantaged *vis a vis* its competitors in this industry because of spectrum licensing. To the extent that the plaintiffs analogize a spectrum license to a patent, that analogy is flawed. A patent confers advantages on one party *vis a vis* its competitors; here, each of the defendants has the same advantage of holding a spectrum license.

The fact that each defendant has or had a network of retail distributors of its service and approved telephones is not evidence of market power within the relevant market of wireless service. Since [\*\*51] each defendant sells its service to the public in this way, no one defendant has any special advantage or power by its use of a retail network. To the extent that the plaintiffs use this factor as evidence of the anti-competitive effects of the tying practice that they assert exist within the tied market of handsets, that will be discussed below. In sum, it is unnecessary to decide if the wireless service market can be properly labeled an oligopoly.<sup>24</sup> The plaintiffs [\*421] have not presented evidence to raise a question of fact that any of the features of this alleged oligopoly on which they place special emphasis has actually conferred market power on any one of the defendants.

[\*\*52] In a related argument, the plaintiffs contend that the structure of the wireless services market, in particular the defendants' parallel actions, serves as evidence of their respective market power in the services market, citing *Broadway Delivery Corp. v. United Parcel Serv. of Am., Inc.*, 651 F.2d 122, 129 (2d Cir. 1981). *Broadway Delivery* addressed the issue of market power in the context of a monopoly claim, not a tying claim. The portion of *Broadway Delivery* on which plaintiffs rely deals with whether a jury should have been charged that a defendant's share of less than fifty percent of a market automatically ruled out a finding of monopoly power under Section 2 of the Sherman Act. *Id. at 127*. Noting that HN15 market share data serves as "strong, perhaps presumptive, evidence of the presence or absence of market power," *id. at 128* (citation omitted), the *Broadway Delivery* court nonetheless cautioned that "careful analysis" of market share, and the structure of the market, including the activities of the defendant and others within the market, was necessary to ascertain whether a defendant had monopoly power. *Id. at 128-29*. [\*\*53] At no point did *Broadway Delivery* identify parallel actions of market participants as evidence that the defendant had market power. As already described, the structure of the wireless services market reflects intense competition with no single, dominant seller.

Turning more directly to the plaintiff's argument about parallel conduct, HN16 although liability may be imposed on the basis of conscious parallelism in certain antitrust contexts, see, e.g., *Todd v. Exxon Corp.*, 275 F.3d 191, 199 (2d Cir. 2001) (horizontal price-fixing agreement), our Circuit's tying case law lends no support for an inference of market power to be drawn from defendants' parallel behavior. Indeed, unless the plaintiff has alleged a conspiracy, it is inappropriate to assess one defendant's market power by measuring "the cumulative power of all defendants practicing tying." 10 Philip E. Areeda & Herbert Hovenkamp, Antitrust Law P 1734e, at 49 (2d ed. 2004) [hereinafter Antitrust Law].

<sup>23</sup> A mobile virtual network operator orders handsets from a large handset manufacturer and resells network capacity leased at wholesale rates from a major wireless service provider.

<sup>24</sup> An oligopoly is defined as "control or domination of a market by a few large sellers, creating high prices and low output similar to those found in a monopoly." *Black's Law Dictionary* 1120 (8th ed. 2004). To the extent that the plaintiffs are using their reference to oligopoly to reposition their tying claim as a conspiracy claim, that effort fails. The plaintiffs abandoned their conspiracy claim long ago and it would prejudice the defendants at this late stage to allow a reformulation in this consolidated lawsuit of plaintiffs' legal theories.

As the Motion to Dismiss Opinion explained, having elected not to proceed on a theory of conspiracy in their Amended Complaint, the plaintiffs must demonstrate that each defendant individually has [\*\*54] market power. [In re Wireless, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, at \\*8](#). While the plaintiffs had originally brought a conspiracy claim in this lawsuit, they dropped that claim from their Amended Complaint. [In re Wireless, 2004 U.S. Dist. LEXIS 19977, 2004 WL 2244502, at \\*6](#). The plaintiffs may not circumvent that history by framing defendants' allegedly parallel actions as evidence of their respective market power.

The plaintiffs next contend that market power exists because the defendants face a "downward sloping demand" curve, that is, that each of the defendants has the power to raise prices somewhat without losing all sales. [HN17](#)[] The test for market power is not whether a defendant can raise its prices somewhat, but whether the defendant has the power to control prices or exclude competition. See [United States v. Visa U.S.A., Inc., 344 F.3d 229 at 239; CDC Techs., 186 F.3d at 81](#) (defining market power as "the ability to raise price significantly above the competitive level without losing all of one's business").

In a related argument, the plaintiffs assert that each of the defendants, even [\*422] those with the smallest market share, has independent market power because each of them sets the price for [\*\*55] its services above marginal cost.<sup>25</sup> While the plaintiffs assume that an estimate of marginal cost, made by an expert for the defendants<sup>26</sup> and based on operational and financial data provided by AIRtouch, applies to all defendants and at the same time overstates defendants' current marginal costs, they have offered no actual data on any one of the defendants' costs nor have they provided any expert analysis of the import of such costs to market power.<sup>27</sup> In fact, the defendants' expert, on whose estimate the plaintiffs rely for this argument, specifically testified that he did not undertake to determine the carriers' marginal costs for the purposes of this case.

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[HN18](#)[] In order to show market power from a defendant's practice of selling its products above marginal cost, a plaintiff must accurately measure price and all appropriate [\*\*57] costs. See [Menasha Corp. v. News Am. Mktg. In-Store, Inc., 354 F.3d 661, 665 \(7th Cir. 2004\)](#) (rejecting plaintiff's claim that defendant consistently sold its product for more than marginal cost without evidence that the defendant obtained an unusually high return on capital). Moreover, the test for the existence of market power is the ability to control price or exclude competition, [Visa, 344 F.3d at 239](#), not simply pricing a product above marginal cost when that price differential can be explained by the existence of economic realities entirely separate from the existence of market power, for instance, the presence of high fixed costs. See [Eastman Kodak, 63 F.3d at 109](#) ("Certain deviations between marginal cost and price, such as those resulting from high fixed costs, are not evidence of market power.") Here, it is undisputed that the defendants' fixed costs include the transmission network, towers, and fiber optic cable. In such circumstances,

<sup>25</sup> Marginal cost is defined as "the additional cost incurred in producing one more unit of output." *Black's Law Dictionary* 372 (8th ed. 2004).

<sup>26</sup> In their opposition brief, the plaintiffs solely rely on testimony of defendants' expert Jerry Hausman in which he agreed that every defendant prices above marginal cost. Through their [Rule 56.1](#) Statement, plaintiffs also note, however, that in a 2000 academic article, Hausman estimated the marginal cost of providing wireless services to be 5 cents per minute. They further note that at his deposition, Hausman acknowledged that "it's quite likely" that the marginal cost of service has declined since then.

<sup>27</sup> The plaintiffs' brief in opposition to this motion creates an argument based on the Lerner Index. Specifically, the plaintiffs note Hausman's expert report states, using data from a 2004 FCC report, that average revenue per minute, often used as a proxy for price, was 29 cents per minute in 1998 and 10 cents per minute in 2003. Using Hausman's academic estimate of marginal cost and these estimates of prices, the plaintiffs have computed a Lerner Index of .85 for 1998 and .5 for 2003. The plaintiffs, however, have presented no expert report regarding the significance of that Index in this case, and in particular its implications for a conclusion that any defendant had market power. See [United States v. Eastman Kodak, 63 F.3d 95, 109 \(2d Cir. 1995\)](#) (rejecting use of Lerner Index as a measure of market power where defendant is not the "seller of a differentiated product that sets prices independently of its rivals").

marginal cost cannot serve as the "competitive benchmark;" rather, all market participants will price above marginal cost to cover fixed costs.

The plaintiffs contend that the existence of **[\*\*58]** market power can be inferred from the fact that each defendant imposes burdensome terms on consumers, specifically, term contracts with early termination and activation fees. A defendant's use of such contracts does not create an inference supporting a finding of market power, since each of the defendants (as well as service **[\*423]** providers who are not defendants) offer service through similar contracts.<sup>28</sup> Therefore, the use of term contracts cannot be said to exclude competition. Nor have plaintiffs alleged, much less demonstrated, that any defendant's use of term contracts, evidences an ability to control prices.

**[\*\*59]** Finally, the plaintiffs contend that it is fair to infer the existence of market power from the fact that competition has been harmed in the handset market. Some courts have stated that market power may be proven through "direct evidence of anticompetitive effects. *"Toys "R" Us, Inc. v. FTC*, 221 F.3d 928, 937 (7th Cir. 2000)

(affirming FTC finding that company's vertical restraints violated the rule of reason under [15 U.S.C. § 5](#)). In *Toys "R" Us*, the company's boycott succeeded in causing ten major toy manufacturers to reduce output of toys to warehouse clubs, which protected the company from having to lower its prices. *Id.* Even assuming that market power can be shown in a tying case through the inference created by providing direct evidence of anticompetitive effect, as will be discussed below, the plaintiffs have failed to provide any such direct evidence. Because the plaintiffs have been unable to show that any one of the defendants has market power in the wireless services industry, each of the defendants is entitled to summary judgment on the plaintiffs' claim that each of the defendants violated the Sherman Act by **[\*\*60]** forcing consumers to purchase handsets to receive service.

## II. Defendants' Motion for Summary Judgment: Anticompetitive Effects

Defendants have also moved for summary judgment on the alternative ground that the plaintiffs have not shown that each defendant's alleged tying arrangements has an anticompetitive effect on the handset market. At the outset, the interrelationship between market power and anticompetitive effects merits some exposition.

Given that market power and anticompetitive effects serve as separate elements of a tying violation, courts are not always explicit about the interaction between these two concepts. Nevertheless, [HN19](#)↑ the Supreme Court has long recognized the interrelationship between market power and anticompetitive effects. Indeed, at the heart of the *per se* rule of tying is the intuition that where a seller has significant market power, one may "presume unreasonableness without the necessity of any analysis of the market context in which the [alleged tying] arrangement may be found." *Jefferson Parish*, 466 U.S. at 9. As a consequence, where a defendant's market power is sufficiently great that its tie qualifies as a *per se* violation, **[\*\*61]** a plaintiff is relieved of the separate burden of showing an anticompetitive effect from the tying in the tied product market. Conversely, the tying case law also reflects the understanding that where market power is not present, an alleged tying violation cannot be a threat to competition in the tied product market. As Justice O'Connor observed in her concurrence in *Jefferson Parish*, a "seller must have power in the tying product market. Absent such power, tying cannot conceivably have any adverse impact in the tied product market and can only be pro-competitive in the tying product market." *Id.* at 37 (O'Connor, J., concurring).

**[\*424]** Even courts that have declined to demand expressly a showing of market power under the rule of reason understand the interplay between market power and anticompetitive effects. As the Third Circuit explained in *Town Sound*, in which the plaintiffs challenged the legality of tying autosound systems to the sale of Chrysler automobiles,

even if we assumed that soon every automobile manufacturer will include an autosound system on every car, the most that we could conclude would be that a certain class of competitors (namely **[\*\*62]** the autosound aftermarket dealers) might be doomed to competitive oblivion. But that would be no concern of the antitrust

<sup>28</sup> The defendants explain that term contracts help carriers recover customer acquisition costs and allow them to charge lower prices and to subsidize handsets in the hope that they will be able to recover the investment. There is no need to address the merits of this argument since the plaintiffs have failed to raise a question of fact that term contracts either create or reflect market power by any one defendant.

laws unless consumers were also hurt because of diminished competition. If the autosound aftermarket were to disappear, vigorous competition in the automobile market would remain. That competition would protect those consumers who care about autosound systems no less than it now protects consumers who care about other standard features, including the comfort of the front seats, the quality of the brakes, and the fuel efficiency of the engine.

Town Sound, 959 F.2d at 494 n.40 (citation omitted). Put another way, the *Town Sound* court understood that in a tying product market characterized by competition, even if all market participants engage in packaged sales, such conduct cannot have actual anticompetitive effects in the tied product market. Thus, having been unable to show that any of the defendants has market power, it is not surprising that plaintiffs are also unable to show that the tying practice in which each defendant is alleged to have engaged has resulted in any anticompetitive effects in the handset market.

**HN20** To demonstrate [\*\*63] anticompetitive effects, a plaintiff must demonstrate that the tie "as it actually operates in the market" harmed competition in the tied product market. Jefferson Parish, 466 U.S. at 29. For a tie to create an anticompetitive effect there must be "a substantial threat that the tying seller will acquire market power in the tied product market. No such threat exists if the tied product market is occupied by many stable sellers who are not likely to be driven out by tying, or if entry barriers in the tied product market are low." *Id. at 38* (O'Connor, J., concurring). "Speculation about anticompetitive effects is not enough." Roy B. Taylor Sales, Inc. v. Hollymatic Corp., 28 F.3d 1379, 1385 (5th Cir. 1994). At no time may "expert testimony rooted in hypothetical assumptions . . . substitute for actual market data." Virgin Airways, 257 F.3d at 264.

In their complaint, the plaintiffs allege that the defendants' alleged tying arrangements have driven numerous handset manufacturers from the market, have deterred entry into the handset market, and have had deleterious effects on the development of handset technology. In re Wireless, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, ¶\*\*641 at \*9. The plaintiffs have not offered sufficient evidence from which a jury could find that any one of those phenomena has occurred.

The plaintiffs first contend in opposition to this motion that each defendant has foreclosed manufacturers from entering the handset market by leveraging "its control of its spectrum licenses and its wireless network to exercise gatekeeping control over a significant portion of the retail market for handsets." Ordinarily, if one were making a foreclosure argument, one would expect the plaintiffs to present a detailed picture of the history of the handset market in the United States, with the number of manufacturers in the market each year, and evidence of failed efforts to enter.<sup>29</sup> The plaintiffs have not done so, [\*425] opting instead to rely entirely on sweeping generalizations and vague opinions rather than facts. For instance, citing the testimony of Kyocera's representative, who estimated that there are "somewhere between 50 and 100 manufacturers in the wireless handset space" worldwide, but that most of the defendants only "do business"<sup>30</sup> with between three to six manufacturers, the

<sup>29</sup> The plaintiffs have devoted some attention to creating a historical picture of the handset market. For instance, to demonstrate how the handset market has changed since the evolution of digital service, the plaintiffs cite the testimony of Peter Skarzynski, a former employee of AT&T Wireless's consumer products division. According to Skarzynski, during his 1994 through 1997 tenure at AT&T, the consumer products division not only sold handsets to retailers such as Sears and Best Buy "without the involvement of the carrier," but such handsets "could be purchased by consumers and then activated with the service of a carrier of the consumer's choice." In a similar vein, the plaintiffs rely on the testimony of their expert, Robert Zicker, who stated that during the analog age, "the technologies were all compatible and an attempt to limit [a consumer's] source of handsets wouldn't be too effective" as the retailers had "a multitude of different places they could buy handsets from." Yet without any showing that manufacturers were precluded from the U.S. handset market as of the time that the defendants' alleged tying practices were imposed or since, such historical reflection has little relevance.

<sup>30</sup> While the plaintiffs repeatedly argue that a manufacturer must have a "business relationship" with a carrier in order to sell handsets in the U.S., they have failed to define precisely what such a business relationship entails. In some instances, the plaintiffs' conception of "doing business" seems to mean a carrier's purchasing a certain manufacturer's handsets. At other times, however, the plaintiffs suggest that a manufacturer's doing business with a carrier involves "working with carriers to put out a product that matches their requirements." At no point have the plaintiffs explicitly argued, much less proven, that any

plaintiffs contend that the number of handset manufacturers operating [\*\*65] in the United States is controlled and limited as a function of defendants' conduct. Yet Kyocera's representative also testified that a number of new manufacturers are entering the U.S. handset market not by selling to the carriers, but instead by selling through a distributor or by developing, manufacturing, and then selling its products "to somebody like Audiovox or Motorola or Nokia or Kyocera Wireless," which then sells the product under its own brand name. Rather than discouraging manufacturers to enter the handset market, Kyocera's representative further testified that where a new entrant has developed an interesting product, a wireless service provider may encourage it to "find one of [its] existing suppliers" to get the product on the market.

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The plaintiffs also cite the expert report of Nicholas Economides, an economics professor at New York University's Stern School of Business, who asserts that the carriers "require that all handset sales flow through the carrier's distribution system if they are to be used in the carrier's network, [\*\*67]" and that "the manufacturers' only customers are the carriers." Economides's support for this argument, however, derives solely from the testimony of LG's representative, who confirmed that "all of LG's sales of GSM handsets in the United States are funneled through GSM carriers;"<sup>31</sup> from the testimony of Kyocera's representative, who credited the carriers with "putting our product out there;" and from that of a Samsung representative, who explained that Samsung had a commercial arrangement with a U.S. carrier [\*426] before making any handset sales in the U.S. market and that he "didn't really know of any manufacturer who doesn't sell through carriers today." Such testimony hardly establishes, as Economides contends, that *all* handset sales flow through carriers' distribution systems.

[\*\*68] Yet even if the plaintiffs could establish that all handset sales flow through the carriers' distribution systems,<sup>32</sup> the fact that the defendants are not handset manufacturers themselves but instead purchase handsets from others has "ameliorating implications." 10 *Antitrust Law* P1727e, at 310. As Professors Areeda and Hovenkamp have explained, using the example of an oil refiner that purchases tires and then resells them to its dealers, "the refiner who buys tires cannot acquire power for itself in the market for manufacturing tires. While the tie forecloses tire makers from selling to defendant's dealers, tire makers can compete as vigorously as ever in seeking the defendant's patronage." *Id.* So too can manufacturers compete vigorously in the U.S. handset market for the patronage of the carriers, even if the plaintiffs were able to show that the carriers' conduct prevents manufacturers from selling directly to retailers or other distributors.

[\*\*69] More significantly, even if the plaintiffs could show that no manufacturer in the U.S. handset market has made direct-to-consumer sales since 1999, such evidence in or itself does not demonstrate that any manufacturer has been precluded from gaining entry to the handset market or that consumers have been adversely affected. See *S. Card & Novelty, Inc. v. Lawson Mardon Label, Inc.*, 138 F.3d 869, 877 (11th Cir. 1998). Most manufacturers of consumer products, such as those sold in grocery, drug, or department stores, choose to sell their products through distribution channels. Handset manufacturers are no different. As LG's representative testified, while LG has *never* sold handsets directly to consumers either before or after 1998, "there's nothing that would stop" it from selling handsets directly to consumers in the United States. Rather, after considering the "resources and infrastructure" a direct sales-based business model would require, LG simply "chose[] not to support any type of [direct] handset sales." To find that such a choice is not a choice at all but instead proves an anticompetitive impact defies logic.

defendant's control over which handsets will be approved for use with its respective network has actually foreclosed manufacturers from the market for handset sales in the U.S.

<sup>31</sup> The same LG representative also testified that LG's entry into the market was "tough but not impossible" and that the packaged sales of handsets and service "helps," rather than hinders, LG's business because "you can't run the product without service. It has to run on a network."

<sup>32</sup> There is evidence that directly contradicts the plaintiffs' contention that all handset sales flow through the carriers' distribution system. For example, some manufacturers, such as Kyocera, do directly sell handsets through their website and are "more than happy to sell the phone without a [service] plan."

The plaintiffs' reliance on the April 16, 2002 edition [\*\*70] of *The Yankee Group Research Notes*, a telecommunications-related publication to which defendants' expert Keith Mallinson contributed, is equally unavailing. According to the plaintiffs, Mallinson's piece, entitled "Mobile Phone Manufacturers Develop Brand and Diversify Distribution," establishes the gatekeeping role played by each defendant with respect to handset distribution. The plaintiffs have selectively quoted from this article. While Mallinson described the U.S. market for handsets as characterized by "carrier dominated distribution," he also argued that the emergence of CDMA and GSM as the dominant technologies increased manufacturers' market power *vis a vis* carriers and that handset vendors should "leverage their brands by reaching out directly to consumers" and "by partnering with third-party distributors." Even if, as Mallinson explained, "alternative channels [of distribution] are unlikely to take the lead in the United States," if manufacturers were truly being "held hostage" [\*427] by the carriers, as the plaintiffs argue, such alternatives would not even be feasible.

The plaintiffs next argue that defendants' tying practices have resulted in increased handset prices. [\*\*71] To support this contention, plaintiffs rely solely on Economides's report, which features a regression analysis that purports to show that the defendants' tying and locking of handsets inflated the average wholesale price of handsets between 1999 through 2003 relative to that of other, comparable consumer electronic goods.<sup>33</sup> The defendants have moved, pursuant to [Rules 401, 402](#), and [702](#), Fed. R. Evid., for an order *in limine* to exclude Economides's report as unreliable. The defendants argue, *inter alia*, that Economides's report must be excluded because in conducting his regression analysis, he failed to consider or test for any alternative explanations for the inflation in handset prices. The defendants further argue that Economides's regression analysis, as well as his report as a whole, fails to address the effects of each defendant's alleged tying arrangements and instead impermissibly measures the aggregate effects of the defendants' practices.

[\*\*72] [HN21](#) [↑] [Rule 702 of the Federal Rules of Evidence](#) provides that expert testimony concerning technical or specialized knowledge is admissible to assist the trier of fact if "(1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case." [Rule 702, Fed. R. Evid.](#) [HN22](#) [↑] A court has an obligation to act as a gatekeeper to ensure the "reliability and relevancy of expert testimony" presented to a jury. [Kumho Tire Co. v. Carmichael](#), 526 U.S. 137, 152, 143 L. Ed. 2d 238, 119 S. Ct. 1167 (1999); see also [Daubert v. Merrell Dow Pharmaceuticals](#), 509 U.S. 579, 594-95, 125 L. Ed. 2d 469, 113 S. Ct. 2786 (1993) (overarching subject of inquiry under [Rule 702](#) is the scientific validity and thus the evidentiary relevance and reliability of the principles that underlie a proposed submission). Specifically, the court must determine that an expert "employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field." [Kumho](#), 526 U.S. at 152. [\*\*73]

[HN23](#) [↑] Where an expert conducts a regression analysis and fails to incorporate major independent variables, such analysis may be excluded as irrelevant. In *Bickerstaff*, the Second Circuit affirmed a district court's exclusion of the Title VII plaintiff's expert's multiple regression analysis, which controlled for experience, rank, productivity, and discipline to conclude that a salary variance was attributable to discrimination, but did not control for such "nondiscriminatory causes" as teaching and service. [Bickerstaff](#), 196 F.3d at 448-49. While noting that in general, an expert's "failure to include variables will affect the analysis' probativeness, not its admissibility," the *Bickerstaff* court determined that the analysis at issue was "so incomplete as to be inadmissible as irrelevant." [Id.](#) at 449 (citation omitted).

The defendants are correct that Economides's regression analysis is methodologically unsound and therefore may not be admitted pursuant to [Rule 702](#). In performing his regression analysis, Economides used United States International [\*428] Trade Commission ("USITC") data on the declared value of imported handsets as a measure of the average wholesale [\*\*74] price of handsets in the U.S. and then performed linear regressions of this data on

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<sup>33</sup> Multiple regression analysis is a commonly accepted statistical tool used to examine "the effect of independent variables on a dependent variable." [Bickerstaff v. Vassar Coll.](#), 196 F.3d 435, 448 (2d Cir. 1999). The parties do not dispute that the retail and wholesale prices for digital handsets have declined annually since the year 2000. The plaintiffs argue, however, that the decline would have been greater but for tying.

each of three Bureau of Labor Statistics (BLS) indices concerning other electronic devices, such as computers and electronic equipment, or component parts of handsets, such as semiconductors. At no point, however, did Economides introduce *any* independent variables into his analysis of the inflation of handset prices *vis a vis* the prices he predicted using the above-referenced BLS indices. In fact, Economides even testified that he "could not think of another explanation" for the inflation of handset prices other than the defendants' alleged tying and locking practices, which in turn allowed the carriers to impose what he characterized as "unwanted features" on consumers, a characterization on which he did not elaborate.

The defendants point to two major developments that could potentially explain why the average wholesale price for wireless handsets exceed those for comparable consumer electronic products and/or their component parts: the shift from analog to digital technology and the related advances in handset features, including caller ID, email, and web browsers; and post-1999 improvements [\*\*75] in handset quality, such as reduced size and weight, longer battery life, and greater spectral efficiency. Economides's failure to test for these obvious and significant alternative explanations renders Economides's analysis "essentially worthless." [Tagatz v. Marquette Univ., 861 F.2d 1040, 1045 \(7th Cir. 1988\)](#) (rejecting study that failed to control for variables for which one can control).

In addition, in his report, Economides explicitly states that his aim in performing his regression analysis was to determine "the effect, if any, of the tying and locking of handsets and services on the price for handsets sold in the United States." His resulting failure to consider "the varying business practices, and business results" of each defendant further strips his regression analysis of reliability, particularly given that the plaintiffs must prove that "each defendant's market power and tying arrangement had an anticompetitive impact on the handset market." [In re Wireless, 2003 U.S. Dist. LEXIS 13886, 2003 WL 21912603, at \\*8](#). As a result, the regression analysis and the related portions of Economides's report must be excluded.

The plaintiffs do not defend the admissibility of Economides' [\*\*76] analysis except to argue that the analysis should be admissible on the issue of *damages*, where they contend there is no legal requirement "to isolate and separately quantify" damages attributable to the various effects of defendants' alleged tying arrangements and contend.<sup>34</sup> Relying on [New York v. Julius Nasso Concrete Corp., 202 F.3d 82 \(2d Cir. 2000\)](#), they argue that in order to prove damages in an antitrust action, a plaintiff need only show "some relevant data from which the district court can make a reasonable estimated calculation of the harm suffered." [Id. at 89](#). The *Nasso* case involved a claim of antitrust conspiracy and recognized that in such circumstances, there may be "a dearth of market information unaffected by the collusive action of the defendants." [Id. at 88](#) (citation omitted). It is unnecessary to decide whether the Economides study would be admissible in proving damages in the con [\*429] text of a conspiracy claim. It is inadmissible to prove the supposed anticompetitive effect from any one defendant's alleged tying practice.

[\*\*77] Besides lack of proof, the plaintiffs' contention that the defendants' distribution practices have worked to inflate handset prices faces another insurmountable hurdle: it makes no economic sense. Since the defendants do not manufacture handsets, and compete with each other through offering handsets with service, it is against each defendant's self-interest to discourage competition among handset manufacturers and thereby to allow handset manufacturers to enrich themselves at a defendant's expense.

Lastly, the plaintiffs claim that defendants' alleged tying arrangements have distorted the development of handset technology by stifling some innovations while needlessly imposing others on consumers. On one hand, plaintiffs argue that as the "gatekeepers" of the handset market, defendants have impeded the development or incorporation of certain handset features, such as multi-carrier functionality, multiple SIM slots,<sup>35</sup> and Bluetooth technology.<sup>36</sup>

<sup>34</sup> Through a letter of May 31, 2005, the plaintiffs requested leave to file a sur-reply to the defendants' motion to exclude Economides's report, *inter alia*, on the ground that the defendants' reply "presented new arguments that plaintiffs have not had a fair opportunity to respond to." Because no arguments raised for the first time in defendants' reply have been relied upon with respect to the admissibility of Economides's regression analysis, the request to file a sur-reply is denied.

<sup>35</sup> A handset with multiple SIM slots would allow a consumer to switch between carriers.

On the other hand, they contend that the defendants have blocked efforts by manufacturers to offer consumers simpler handset models. The plaintiffs have offered no admissible evidence on the first point,<sup>37</sup> and limited, insufficient evidence [\*\*78] on the latter.

The plaintiffs principally rely on two documents from one defendant, AT&T Wireless, regarding the alleged failure to offer basic handsets. In one undated document, AT&T Wireless observed that a more simplistic handset model "drives down costs," "provides higher battery life" and is "less likely to have performance problems resulting in fewer warranty return issues." These observations prove nothing with respect to whether AT&T's [\*\*79] alleged tying arrangement has anticompetitive effects on the handset market. In the second document, dated February 17, 2004, AT&T Wireless comments that approving very basic handset models for use on its network may prevent it from driving technological innovations in handsets and may enable manufacturers to offer "features that enhance their brand yet may be detrimental to the carrier's revenue strategy." These two documents, taken together, do not create a question of fact as to whether AT&T has actually acted to stop manufacturers from offering simpler models or alternatives to consumers, or more to the point, stifled competition in the handset market. Given the competition within the wireless market, and AT&T's lack of market power, AT&T would not, of course, have the ability to do so unilaterally. In any event, the issue is not whether a defendant has impaired the distribution of a particular kind of product with its own service but whether it has impaired competition among handset manufacturers and within the handset market. These documents do not speak to that.

With respect to their argument that the defendants have "forced" certain handset features on "consumers who have [\*\*80] no use for them," the plaintiffs first contend that [\*\*430] there is no consumer demand for handset locks, citing Economides's report for the proposition that "since handset locks have negative value to the customer, there is no consumer demand for such a feature." In coming to this conclusion, Economides relied on three documents, which explain that the purpose of the locks is to control churn.<sup>38</sup>

The allegation that each of the defendants locks handsets sold for use on its respective network is perhaps the heart of the plaintiffs' case. [\*\*81] The plaintiffs' principal concern is that the locks impede consumers from switching readily between carriers.<sup>39</sup> Of course, the defendants have utilized other practices to prevent churn too, such as one-year service contracts. As the statistics compiled by the FCC show, whatever attempts the defendants have made to address churn, those efforts have been to a significant degree futile. Moreover, the defendants' subsidization of handset costs, which they use to lure new customers, undercuts the degree to which a locking mechanism will dissuade a consumer from switching service providers.<sup>40</sup> In any event, and to reiterate, to show

<sup>36</sup> The plaintiffs define Bluetooth technology as "short-range wireless computer connectivity."

<sup>37</sup> The plaintiffs' attempt to demonstrate, through Economides's rebuttal report's citation to a January 2005 *Wall Street Journal* article, that Verizon Wireless has suppressed the introduction of Bluetooth technology, fails as well. Even assuming that the article were admissible, the plaintiffs have not shown that such conduct by Verizon impacted the handset market as a whole.

<sup>38</sup> The first, from June 1995, contains an AirTouch employee's analysis that handset locks "allow[] a carrier to control churn." The second, an undated AT&T Wireless document, similarly explains that AT&T locks handsets to "make[] it costly for the subscriber to switch to another carrier." The third document, a February 19, 2004 AT&T Wireless analysis, determines that if customers could obtain unlocked handsets, they "could replace the carrier without investment in a new device."

<sup>39</sup> The plaintiffs alternately argue that the defendants' tying arrangements allow them to lock handsets and that handset locks serve, by inhibiting the availability of unlocked handsets, to "reinforce the tie." For the reasons discussed above, the plaintiffs have not shown that a triable issue of fact exists as to whether handset locking creates an anticompetitive effect. The plaintiffs' second argument, that the defendants enforce their respective tying arrangements by locking handsets, reveals the fundamental deficiency of their tying claim. A defendant with market power in the tying product market needs no other aid to implement a tying arrangement successfully; rather, by virtue of its control over the tying product market, it is able to diminish competition in the tied product market and force consumers to accept a tying arrangement they would otherwise resist. The plaintiffs' argument, through their expert Robert Zicker, that the defendants were not successful in tying until locking was available underscores this basic point.

<sup>40</sup> As a matter of logic, the need for consumers to buy new handsets when they switch plans should increase competition in the handset market. Defendants contend and plaintiffs do not disagree that the defendants use their offers of handsets at the lowest

anticompetitive effects in the handset market from a defendant's practice of tying the sale of service to the purchase of a locked handset, the plaintiffs must show that an individual defendant's practice has injured a company competing in the handset market, created barriers to entry into that market, or otherwise injured competition in the tied product market. They have not done so.

#### [\*\*82]

Finally, the plaintiffs argue that by virtue of their tying arrangements, the carriers have forced consumers to purchase handsets with data features, such as Internet browsers. For this proposition, the plaintiffs first cite two AT&T Wireless documents, one from February 2004 that states that it "allows only data-capable devices" and another, undated document that includes an XHTML browser among AT&T Wireless's "unique specifications" for handsets. The plaintiffs then contrast this information with a December 2003 report by Forrester Research that asserts that [\*431] only 9 percent of wireless [\*\*83] users report using a "branded data service" and declares that "price remains the most important purchase influencer for mobile subscribers, while new handset features and operator services generally leave users cold."

Even assuming that plaintiffs could show with admissible evidence that consumers as a whole do not want to purchase handsets with data features, the plaintiffs' focus on these features as evidence of "reduced consumer choice adversely affecting the qualities of handsets available in the marketplace" is misguided. The plaintiffs have offered no legal support for the proposition that too much product innovation, as opposed to diminished quality, can show the actual adverse effect on competition needed to prevail under a rule of reason analysis. Just as significantly, the plaintiffs have presented no evidence as to how the inclusion of these features has created barriers to competition among handset manufacturers or in the handset market. For all of these reasons, defendants are also entitled to summary judgment on the plaintiffs' contention that each defendant's alleged tying arrangement has had an anticompetitive effect on the market for handsets in the United States.

#### [\*\*84] Conclusion

For the reasons stated above, the defendants' motion for summary judgment is granted. The Clerk of Court shall close the following cases: 02 Civ. 2637 (DLC), 03 Civ. 1712 (DLC), 03 Civ. 1713 (DLC), 03 Civ. 1714 (DLC), and 03 Civ. 1715 (DLC).<sup>41</sup>

SO ORDERED:

Dated: New York, New York

September 2, 2005

DENISE COTE

United States District Judge

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possible prices to compete with each other. The increased sales of handsets that result from this practice and the incentive to use handset innovations as a draw to bring new customers to a new service provider foster competition in the tied product market.

<sup>41</sup> The parties have been ordered to file in the public record the bulk of their motion papers, which they initially filed under seal. The Court retains jurisdiction over that unsealing process.



## [Ariz. Cartridge Remanufacturers Ass'n v. Lexmark Int'l, Inc.](#)

United States Court of Appeals for the Ninth Circuit

March 17, 2005, Argued and Submitted, San Francisco, California ; August 30, 2005, Filed

No. 03-16987

### **Reporter**

421 F.3d 981 \*; 2005 U.S. App. LEXIS 18753 \*\*; 77 U.S.P.Q.2D (BNA) 1995 \*\*\*

ARIZONA CARTRIDGE REMANUFACTURERS ASSOCIATION INC., an Arizona not-for-profit corporation, individually, and on behalf of its members and the general public, Plaintiff-Appellant, v. LEXMARK INTERNATIONAL INC., a Delaware corporation, Defendant-Appellee.

**Prior History:** [\[\\*\\*1\]](#) Appeal from the United States District Court for the Northern District of California. D.C. No. CV-01-04626-SBA/JL. Saundra B. Armstrong, District Judge, Presiding.

[Ariz. Cartridge Remanufacturers Ass'n v. Lexmark Int'l, Inc., 290 F. Supp. 2d 1034, 2003 U.S. Dist. LEXIS 20668 \(N.D. Cal., 2003\)](#)

## **Core Terms**

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cartridge, consumers, patent, advertising, misleading, district court, remanufacturing, discount, unfair competition, post-sale, lock-out, package, printer, empty, deceptive, wholesalers, regular, unfair, terms, business practice, restrictions, purchasers, opening, percent, notice, reuse

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

### [HN1](#) [Appellate Review, Standards of Review](#)

The appellate court review the district court's grant of summary judgment de novo. The appellate court must determine, by viewing the evidence in the light most favorable to the nonmoving party, whether there are any genuine issues of material fact and whether the district court correctly applied the relevant substantive law.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Torts > ... > Proof > Custom > Business Customs

Antitrust & Trade Law > Consumer Protection > General Overview

421 F.3d 981, \*981LÁ2005 U.S. App. LEXIS 18753, \*\*1LÁ7 U.S.P.Q.2D (BNA) 1995, \*\*\*1995

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Antitrust & Trade Law > Consumer Protection > False Advertising > State Regulation

## [\*\*HN2\*\*](#) Consumer Protection, Deceptive & Unfair Trade Practices

Two California laws provide broad consumer protection for misleading and unfair practices by businesses. [Cal. Bus. & Prof. Code § 17500](#) makes it unlawful for a business to disseminate any statement which is untrue or misleading, and which is known, or which by the exercise of reasonable care should be known, to be untrue or misleading. In turn, [Cal. Bus. & Prof. Code § 17200 et seq.](#), prohibits any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by [Cal. Bus. & Prof. Code § 17500](#).

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Civil Procedure > ... > Injunctions > Grounds for Injunctions > General Overview

Evidence > Burdens of Proof > General Overview

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

## [\*\*HN3\*\*](#) Consumer Protection, False Advertising

To state a cause of action under [Cal. Bus. & Prof. Code § 17500](#) for injunctive relief requires a showing that members of the public are likely to be deceived, but does not call for a showing of actual deception or confusion caused by misleading statements. The law encompasses not just false statements but those statements which may be accurate on some level, but will nonetheless tend to mislead or deceive. A perfectly true statement couched in such a manner that it is likely to mislead or deceive the consumer, such as by failure to disclose other relevant information, is actionable under these sections. The plaintiff has the burden of proving that the challenged advertising is false or misleading to a reasonable consumer.

Antitrust & Trade Law > Consumer Protection > False Advertising > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Advertising > Elements of False Advertising

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

## [\*\*HN4\*\*](#) Consumer Protection, False Advertising

"Unfair competition" under [Cal. Bus. & Prof. Code § 17200](#) means conduct that threatens an incipient violation of an [antitrust law](#), or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition. [Section 17200](#) is not limited to anticompetitive business practices targeted at rivals, but is equally directed toward the right of the public to protection from fraud and deceit, and permits courts to enjoin ongoing wrongful business conduct in whatever context such activity might occur. A violation of the false advertising law automatically gives rise to a violation of the unfair competition provision.

421 F.3d 981, \*981LÁ2005 U.S. App. LEXIS 18753, \*\*1LÁ7 U.S.P.Q.2D (BNA) 1995, \*\*\*1995

Antitrust & Trade Law > ... > Intellectual Property > Ownership & Transfer of Rights > General Overview

Healthcare Law > Business Administration & Organization > Covenants not to Compete > Enforcement

Patent Law > Remedies > Equitable Relief > Injunctions

Healthcare Law > Business Administration & Organization > Covenants not to Compete > General Overview

## **HN5** [down] Intellectual Property, Ownership & Transfer of Rights

A restriction on a patented good is permissible as long as it is found to be reasonably within the patent grant, i.e., that it relates to subject matter within the scope of the patent claims. A condition is impermissible where the patentee has ventured beyond the patent grant and into behavior having an anticompetitive effect not justifiable under the rule of reason.

Commercial Law (UCC) > ... > Subject Matter > Goods > General Overview

Commercial Law (UCC) > Sales (Article 2) > General Overview

Commercial Law (UCC) > Sales (Article 2) > Form, Formation & Readjustment > General Overview

Commercial Law (UCC) > Sales (Article 2) > Subject Matter > General Overview

## **HN6** [down] Subject Matter, Goods

See [Cal. Com. Code § 2204\(1\)](#).

Commercial Law (UCC) > Sales (Article 2) > Form, Formation & Readjustment > General Overview

## **HN7** [down] Sales (Article 2), Form, Formation & Readjustment

See [Cal. Com. Code § 2204\(2\)](#).

Contracts Law > Breach > Breach of Contract Actions > General Overview

## **HN8** [down] Breach, Breach of Contract Actions

Under California law, one may not sue upon a contract unless he is a party to that contract.

**Counsel:** Ronald S. Katz, Eugene L. Hahm, Manatt, Phelps & Phillips, LLP, for the plaintiff-appellant.

J. Thomas Rosch, James L. Day, Richard B. Ulmer Jr., Latham & Watkins, for the defendant-appellee.

**Judges:** Before: Sidney R. Thomas and Raymond C. Fisher, Circuit Judges, and James L. Robart, District Judge. \*

**Opinion by:** Raymond C. Fisher

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\* The Honorable James L. Robart, United States District Judge for the Western District of Washington, sitting by designation.

## Opinion

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[\*\*\*1995] [\*983] FISHER, Circuit Judge:

Appellant Arizona Cartridge Remanufacturers Association ("ACRA"), an association of wholesalers that sell remanufactured printer cartridges, appeals the grant of summary judgment to cartridge-maker Lexmark on claims that Lexmark engaged in deceptive and unfair [\*\*\*1996] business practices in violation of California law. The dispute arises from Lexmark's advertising of its "Prebate" program, under which it gives purchasers an up-front discount in exchange for their agreement to return the empty cartridge to Lexmark for remanufacturing -- a [\*\*2] form of post-sale restriction on reuse. ACRA claims that Lexmark's advertising and promotional materials mislead customers into thinking the post-sale restriction is enforceable and that they actually receive a discounted price for the special cartridges. We agree with the district court that ACRA has not offered evidence that Lexmark's advertisements constitute deceptive or unfair business practices and affirm the grant of summary judgment in favor of Lexmark.

I.

Lexmark, spun off from IBM in 1991, makes and sells laser printers and toner (printer) cartridges. ACRA represents wholesalers that remanufacture emptied Lexmark printer cartridges for reuse. Before 1997, Lexmark did not compete against ACRA's members because it sold only new replacement printer cartridges. In 1997, however, Lexmark began to remanufacture its own cartridges and launched an aggressive new strategy to improve its position in the market for remanufacturing the used cartridges. Most notably, the company introduced its "Prebate" program -- a play on the word "rebate" -- which gives consumers an upfront discount on printer cartridges. The Prebate cartridges cost consumers on average 30 dollars (or 20 percent) [\*\*3] less than a regular cartridge. In return, Lexmark requires the consumer to return the depleted cartridge to Lexmark or its agent.

The Prebate cartridge package sets forth the following license agreement on the outside of the package:

### **RETURN EMPTY CARTRIDGE TO LEXMARK FOR REMANUFACTURING AND RECYCLING**

Please read before opening. Opening of this package or using the patented cartridge inside confirms your acceptance of the following license agreement. The patented cartridge is sold at a special price subject to a restriction that it may be used only once. Following this initial use, you agree to return the empty cartridge [\*984] only to Lexmark for remanufacturing and recycling. If you don't accept these terms, return the unopened package to your point of purchase. A regular price cartridge without these terms is available <sup>1</sup> [\*\*4] Consumers can opt to buy Lexmark cartridges without the Prebate post-sale restriction, but at the higher price. <sup>2</sup>

Lexmark asserts that it devised the Prebate program to boost its competitive position in the remanufacturing market, to preserve the quality of the product offered consumers and to be environmentally conscious by recycling used cartridges. Lexmark advertises the program in packaging, media and on the company's Web site. *Id.* It pays a fee to authorized resellers who collect and return empty cartridges.

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<sup>1</sup> The packaging when the Prebate program was launched in 1997 contained slightly different language:

**IMPORTANT! READ BEFORE OPENING.** Opening this package or using the cartridge inside confirms your acceptance to the following license agreement. **License Agreement:** Patent cartridge inside sold subject to **Single Use Only restriction**. It is a **violation** of this agreement and/or it is **unlawful to resell, reuse, refill or remanufacture**. If you don't agree, return unopened package to point of purchase.

<sup>2</sup> According to Lexmark, its post-sale restriction on reusing the Prebate cartridges does not require consumers to return the cartridge at all; it only precludes giving the cartridge to another remanufacturer. The plain language of the contract does not clearly reflect this position. However, the distinction drawn by Lexmark is unnecessary to our resolution of the present case, which is not a direct challenge to the terms of the contract itself.

The program has been successful. The company estimates that 50 percent of the cartridges sold are returned as empty cartridges to Lexmark, and cartridge returns have increased by 300 percent since the implementation of the Prebate program. Additionally, [\*\*5] from 1997 to 2001, Lexmark's cartridge sales in the United States increased by nearly 100 percent and its sale of printers that use Prebate cartridges increased by 60 percent.

ACRA filed this diversity action against Lexmark in federal district court, alleging that several of the company's statements regarding the terms and benefits associated with purchasing a Prebate cartridge are false and violate California's unfair competition laws. Most important for purposes of this appeal, ACRA argued that Lexmark deceptively suggests that the conditions placed on the outside of the Prebate package create an enforceable [\*\*\*1997] agreement with consumers to return used cartridges. ACRA also contended that Lexmark misleads consumers by falsely promising that they will save money when purchasing Prebate cartridges, when in fact Lexmark cannot control the price charged by retailers. Finally, ACRA's complaint challenged Lexmark's use of a so-called "lock-out" chip as an unfair business practice.<sup>3</sup>

[\*\*6] The district court concluded that Lexmark's Prebate program advertising is not deceptively false. [Arizona Cartridge Remanufacturers Ass'n, Inc. v. Lexmark Int'l, Inc., 290 F. Supp. 2d 1034, 1049 \(N.D. Cal. 2003\)](#). It found that the company could legally enforce the post-sale restriction under a Federal Circuit decision allowing patent holders to limit the use of their products after sale. [Id. at 1042-45](#) (citing [Mallinckrodt, Inc. v. Medipart, Inc., 976 F.2d 700, 708 \(Fed. Cir. 1992\)](#)). The court further found that Lexmark's restriction created a valid agreement with consumers and that Lexmark's claim of discount pricing accurately reflects its sales practice. [Id. at 1045-46](#). It also found that ACRA failed to establish that Lexmark's use of the lock-out chip amounts to unfair competition. [Id. at 1049-50](#).

## II.

**HN1**[<sup>↑</sup>] We review the district court's grant of summary judgment de novo. [Delta Sav. Bank v. United States, 265 F.3d 1017, 1021 \(9th Cir. 2001\)](#). We must determine, by "viewing the evidence in the light most favorable to the nonmoving party, whether there are any genuine issues of material fact and whether [\*\*7] the district court correctly applied the relevant substantive law." *Id.*

## III.

Although this case involves our consideration of important questions of patent and contract law, at its core the dispute between Lexmark and ACRA reduces to state claims of unfair competition and misleading business practices related to Lexmark's advertising. The key issue here is whether Lexmark misleads consumers and engages in unfair competition when it advertises cartridges for sale at a reduced price but with restrictions on their use. ACRA sues under **HN2**[<sup>↑</sup>] two California laws that provide broad consumer protection for misleading and unfair practices by businesses. [California Business and Professions Code § 17500](#) makes it unlawful for a business to disseminate any statement "which is untrue or misleading, and which is known, or which by the exercise of reasonable care should be known, to be untrue or misleading. . . ." In turn, [California Business and Professions Code § 17200, et seq.](#), prohibits "any unlawful, unfair or fraudulent business act or practice and unfair, deceptive, untrue or misleading advertising and any act prohibited by" [§ 17500](#).<sup>4</sup> **HN3**[<sup>↑</sup>] To state a cause of action

<sup>3</sup> The Sixth Circuit described the chip's functioning as a "secret handshake" between the printer and the chip in each cartridge. [Lexmark Int'l v. Static Control, 387 F.3d 522, 530 \(6th Cir. 2004\)](#) (addressing copyright infringement action against rival chip maker). "If the two values do not match each other, the printer returns an error message and will not operate, blocking consumers from using toner cartridges that Lexmark has not authorized." *Id.*

<sup>4</sup> California's Proposition 64, passed in November 2004, amended the statute to prohibit unaffected plaintiffs from bringing suit on behalf of the general public. [Cal. Bus. & Prof. Code § 17204](#). Under this change, ACRA may lack standing to assert that Lexmark is deceiving consumers or engaging in unfair competitive practices that harm consumers. However, California courts are split on whether this requirement applies retroactively to cases that have not been fully adjudicated. Compare [Bivens v. Corel Corp., 126 Cal. App. 4th 1392, 24 Cal.Rptr. 3d 847 \(Cal. Ct. App. 2005\)](#) (finding plaintiff lacked standing because it was not affected), review granted, 28 Cal. Rptr. 3d 3, 110 P.3d 1218 (Cal. 2005), with [Californians for Disability Rights v. Mervyn's](#),

under [§ 17500](#) for injunctive relief requires a showing that members of the public are likely to be deceived, but does not call for a showing of "actual deception or confusion caused by misleading statements." [Day v. AT & T Corp., 63 Cal. App. 4th 325, 74 Cal.Rptr.2d 55, 59 \(Cal. Ct. App. 1998\)](#). The law encompasses not just false statements but those statements "which may be accurate on some level, but will nonetheless tend to mislead or deceive. . . . A perfectly true statement couched in such a manner that it is likely to mislead or deceive the consumer, such as by failure to disclose other relevant information, is actionable under these sections." [Id. at 60](#). The plaintiff has the burden of proving that the challenged advertising is false or misleading to a reasonable consumer. [Nat'l Council Against \[\\*\\*986\] Health Fraud, Inc. v. King Bio \[\\*\\*\\*1998\] Pharm., Inc., 107 Cal. App. 4th 1336, 133 Cal.Rptr.2d 207, 214 \(Cal. Ct. App. 2003\)](#).

[\*\*9] [HN4](#)<sup>↑</sup> "Unfair competition" under [§ 17200](#) "means conduct that threatens an incipient violation of an [antitrust law](#), or violates the policy or spirit of one of those laws because its effects are comparable to or the same as a violation of the law, or otherwise significantly threatens or harms competition." [Cel-Tech Communications, Inc. v. Los Angeles Cellular Tel. Co., 20 Cal. 4th 163, 83 Cal. Rptr. 2d 548, 973 P.2d 527, 544 \(Cal. 1999\)](#). [Section 17200](#) is not limited to anticompetitive business practices targeted at rivals, "but is equally directed toward the right of the public to protection from fraud and deceit," [Comm. On Children's Television, Inc. v. Gen. Foods Corp., 35 Cal. 3d 197, 673 P.2d 660, 667, 197 Cal. Rptr. 783 \(Cal. 1983\)](#) (internal quotation marks and emphasis omitted) (quoting [Barquis v. Merchants Collection Ass'n, 7 Cal. 3d 94, 496 P.2d 817, 828, 101 Cal. Rptr. 745 \(Cal. 1972\)](#)), and permits "courts to enjoin ongoing wrongful business conduct in whatever context such activity might occur," *id.* A violation of the false advertising law automatically gives rise to a violation of the unfair competition provision. [Id. at 668](#).

ACRA argues [\*\*10] that specific statements made by Lexmark in conjunction with its Prebate program -- offering cheaper cartridges that come with restrictions on their reuse -- violate [§§ 17200](#) and [17500](#). We address these allegedly offending statements -- the focus of ACRA's appeal -- in turn.

#### A. Enforceability of Post-Sale Restriction

ACRA contends that Lexmark engages in false advertising and unfair competition by telling consumers they have a legal obligation to honor the post-sale restriction printed on the outside of the cartridge package, when in fact they are not legally compelled to do so. Under ACRA's theory, Lexmark cannot enforce the post-sale conditions and to suggest otherwise violates California's consumer protection laws. To satisfy its burden on summary judgment, ACRA essentially must show that Lexmark has no legal basis for the restriction featured in its advertising. We agree with the district court that ACRA has failed to make such a showing.

##### 1. Patent Law

The district court found that Lexmark could condition the use of its patented Prebate cartridges by consumers under the principle articulated by the Federal Circuit in [Mallinckrodt, Inc. v. Medipart, Inc. \[\\*\\*11\]](#), which held that [HN5](#)<sup>↑</sup> a restriction on a patented good is permissible as long as it is "found to be reasonably within the patent grant, i.e., that it relates to subject matter within the scope of the patent claims." [976 F.2d at 708](#). A condition is impermissible where "the patentee has ventured beyond the patent grant and into behavior having an anticompetitive effect not justifiable under the rule of reason." *Id.* (remanding for a determination of whether the patentee's single-use restriction on its medical device was reasonable and within the scope of its patent); see also [Monsanto Co. v. McFarling, 302 F.3d 1291, 1298-99 \(Fed. Cir. 2002\)](#) (upholding infringement injunction against farmer who purchased patented seeds under an agreement that the seeds be used for "planting a commercial crop only in a single season," and who then replanted the seeds); [B. Braun Med., Inc. v. Abbott Laboratories, 124 F.3d 1419, 1426 \(Fed. Cir. 1997\)](#) (concluding that although typically "an unconditional sale of a patented device exhausts the patentee's right to control the purchaser's [\*987] use of the device thereafter," this does not hold true where the patentee [\*\*12] specifically places restrictions on the sale of the item).

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[LLC, 126 Cal. App. 4th 386, 24 Cal.Rptr. 3d 301 \(Cal. Ct. App. 2005\)](#) (finding the standing requirement to apply only prospectively), review granted, [28 Cal. Rptr. 3d 1, 110 P.3d 1216 \(Cal. 2005\)](#). Because we affirm the district court's grant of summary judgment, we do not address the effect of Proposition 64 on ACRA's claim, if any.

Applying the *Mallinckrodt* principle, the district court determined that Lexmark imposed an enforceable condition on the Prebate printer cartridges because Lexmark's patent rights were not exhausted. [Arizona Cartridge, 290 F. Supp. 2d at 1045](#). On appeal, ACRA does not challenge the district court's reliance on *Mallinckrodt* or the validity of the Federal Circuit's decision, nor does it argue that Lexmark is acting beyond the scope of its patent.<sup>5</sup> In fact, ACRA concedes that the otherwise unfettered use of a patented good can be constrained. [Blue Brief at 21]. But to do so, ACRA contends, the patent holder must have a valid contract with the consumers of its product. [\*\*\*1999]

### [\*\*13] 2. Contract Law

ACRA thus asks us to conclude that Lexmark lacks a valid contract with consumers to limit the post-sale use of the cartridge. California law, adopting the relevant Uniform Commercial Code provisions, establishes that a [HN6](#)<sup>6</sup> "contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract." [Cal. Com. Code § 2204\(1\)](#). Additionally, California law provides that an [HN7](#)<sup>7</sup> "agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined." *Id.* at [§ 2204\(2\)](#).

We agree with the district court that Lexmark has presented sufficient unrebutted evidence to show that it has a facially valid contract with the consumers who buy and open its cartridges. Specifically, the language on the outside of the cartridge package specifies the terms under which a consumer may use the purchased item. The consumer can read the terms and conditions on the box before deciding whether to accept them or whether to opt for the non-Prebate cartridges that are sold without any restrictions.

The district court found that [\\*\\*14](#) the ultimate purchasers of the cartridge -- consumers -- had notice of the restrictions on use and had a chance to reject the condition before opening the clearly marked cartridge container. [Arizona Cartridge, 290 F. Supp. 2d at 1044-45](#). These findings support the conclusion that the consumer accepts the terms placed on usage of the Prebate cartridge by opening the box.<sup>6</sup>

[\\*\\*15](#) In exchange for agreeing to the restricted use of the cartridge, consumers receive consideration in the form of the price discount. [\\*988](#)<sup>7</sup> The district court explicitly found that "the Prebate is offered at a special price that reflects an exchange for a single-use condition." [Arizona Cartridge, 290 F. Supp. 2d at 1045](#). ACRA argues that because Lexmark distributes its cartridges through wholesalers, it has no way to ensure that consumers actually receive the price discount, but offers no factual support for this contention. Lexmark presented evidence that market forces compel wholesalers to pass the discount on to consumers. A regional manager of one supplies retailer said it would be hard, albeit not impossible, for the wholesaler to skim the discount off as profit for itself by passing on only a portion of the discount from Lexmark to the consumer. But he said, "in a very competitive wholesale distribution market, there are too many competitors, really, to be able to do that." Furthermore, the Prebate notice printed on

<sup>5</sup> The Electronic Frontier Foundation, in its amicus brief, argues that *Mallinckrodt* was wrongly decided and urges us to reject explicitly the Federal Circuit's reasoning. However, ACRA has not challenged the district court's reliance on or application of *Mallinckrodt*. Thus, we need not pass on the merits of the Federal Circuit's decision for resolution of the case before us.

<sup>6</sup> This case is different from those instances in which a consumer lacks notice of the condition at the time of purchase. See, e.g., [Step-Saver Data Sys. v. Wyse Tech., Inc., 939 F.2d 91, 105 \(3d Cir. 1991\)](#) (treating box-top license as an additional term not incorporated into the parties' contract where the term's addition to the contract would materially alter the agreement and the consumer did not see license until after paying for product). Another variant involves "shrinkwrap licenses" on software, which impose restrictions that a consumer may discover only after opening and installing the software. See e.g., [ProCD v. Zeidenberg, 86 F.3d 1447, 1452-53 \(7th Cir. 1996\)](#) (holding that contract included license agreement terms that appeared on screen even though they came after user had purchased, opened and installed software).

<sup>7</sup> Lexmark represents that it has not taken legal action against any user for failing to return a cartridge to Lexmark because it "assumes customers will be honest and send cartridges back." To the extent that Lexmark fails to enforce its Prebate policy, a consumer receives the benefit of the bargain through the price reduction without necessarily having to carry through on its obligation to return the cartridges to Lexmark.

the cartridge informs consumers that they can purchase a regular cartridge without the restriction at the regular price; the notice specifically states [\*\*16] that a "regular price cartridge without these terms is available." ACRA has failed to rebut this evidence to create a triable issue of fact.

ACRA's argument that no enforceable agreement exists because there is no privity of contract also fails. ACRA cites a California case stating "the general rule that Hn<sup>o</sup><sup>+</sup> one may not sue upon a contract unless he is a party to that contract." *Watson v. Aced*, 156 Cal. App. 2d 87, 91, 319 P.2d 83 (Cal. Ct. App. 1957). The privity requirement is met here, because the consumer is a party to the contract with Lexmark. As described above, the contract [\*\*17] is formed when the final purchaser opens the cartridge box with notice of the restriction on reuse. ACRA contends, however, that the lack of privity is shown by Lexmark's inability to ensure that consumers will receive the price-reduction benefit of the Prebate program. We have already explained why ACRA has failed to show that consumers do not pay a reduced price. It does not matter that this price discount [\*\*\*2000] results from distributors choosing to pass along their savings -- the consumer still receives consideration for agreeing to the restriction.

We hold that the contract on its face appears to be enforceable based on the district court's findings that consumers (1) have notice of the condition, (2) have a chance to reject the contract on that basis and (3) receive consideration in the form of a reduced price in exchange for the limits placed on reuse of the cartridge.<sup>8</sup> The contract permits Lexmark to restrict the use of its patented item and gives Lexmark a legal basis for asserting its ability to enforce its restriction. Therefore, ACRA has not raised a triable issue of fact that Lexmark's advertising statements as to its Prebate program are false, mislead or tend to deceive consumers [\*\*18] or that they constitute a form of unfair competition. See *Day*, 63 Cal.Rptr.2d at 59-60.

#### B. Lexmark's Statements as to Price Reduction

ACRA contends that Lexmark's advertising is misleading in promising [\*989] consumers a price reduction for buying a Prebate rather than a regular cartridge, because Lexmark cannot guarantee consumers will pay less for a Prebate cartridge. We have already rejected this argument. See *supra* Section III.A.2.

ACRA further alleges that Lexmark engages in deceptive advertising and unfair competition by suggesting that the price difference between Prebate and non-Prebate cartridges approximates the value of an empty cartridge. According to ACRA, Lexmark wants consumers to believe that the Prebate discount reflects the benefit that accrues to Lexmark by getting an empty cartridge back. We agree with the district court [\*\*19] that nothing in the record supports ACRA's claim. *Arizona Cartridge*, 290 F. Supp. 2d at 1047.

#### C. Use of the Lock-Out Chip

ACRA argues that Lexmark's use of the lock-out chip, which prevents consumers from having their Prebate cartridges remanufactured by a different company, is anticompetitive and is intended to preclude competition in the after-market. The district court found ACRA's claim that the lock-out chip is a form of unfair competition to be unsupported by facts or legal authority, as do we. *Id. at 1050*. As discussed above, the district court relied on the Federal Circuit's *Mallinckrodt* decision to find that Lexmark could restrict the post-sale use of its patented cartridge. ACRA has not challenged the court's determination or alleged that Lexmark is acting beyond the scope of its patent in imposing a condition that it uses the lock-out chip to enforce. Additionally, ACRA has not attempted to show that the use of the lock-out chip -- even if designed to keep other companies from remanufacturing Prebate cartridges -- impermissibly exceeds the patent grant to produce anticompetitive effects.

In sum, ACRA has failed to raise a [\*\*20] triable issue of fact as to whether Lexmark's restriction on the use of its patented cartridge is valid and, in turn, whether the lock-out chip is a proper mechanism to ensure compliance with the restriction. We affirm the district court's decision on this issue as well.

#### IV.

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<sup>8</sup> Our holding here does not preclude challenges to the contract that a customer -- which, unlike ACRA, is a party to the contract -- could raise.

We AFFIRM the district court's grant of summary judgment to Lexmark.

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## [\*In re Visa Check/Mastermoney Antitrust Litig.\*](#)

United States District Court for the Eastern District of New York

August 31, 2005, Decided

96 CV 5238 (JG)

**Reporter**

2005 U.S. Dist. LEXIS 18693 \*

IN RE VISA CHECK/MASTERMONEY ANTITRUST LITIGATION

**Notice:** [\*1] FOR ELECTRONIC PUBLICATION ONLY

**Subsequent History:** Magistrate's recommendation at [\*In re Visa Check/Mastermoney Antitrust Litig., 2005 U.S. Dist. LEXIS 49257 \(E.D.N.Y., Nov. 2, 2005\)\*](#)

**Prior History:** [\*In re Visa Check/MasterMoney Antitrust Litig., 2004 U.S. Dist. LEXIS 8729 \(E.D.N.Y., Apr. 27, 2004\)\*](#)

**Disposition:** Merchants' motion to enjoin Ratner v. Wal-Mart Stores, Inc., Case No. CV 05 555060 (Oh Ct. Common Pl. filed Feb. 17, 2005) denied.

## **Core Terms**

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Merchants, settlement, enjoin, purchasers, state court, proceedings, injunction, indirect, Consumers, anti trust law, federal court, parties, antitrust, tying arrangement, allegations, district court, settling, cases, class action, effectuate, damages, Courts, Writs, costs, deter, card

## **LexisNexis® Headnotes**

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Civil Procedure > Remedies > Writs > All Writs Act

Civil Procedure > Remedies > Writs > General Overview

**HN1** [▼] **Writs, All Writs Act**

See [28 U.S.C.S. § 1651\(a\).](#)

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## **HN2** [down arrow] Anti-Injunction Act, Exceptions

See [28 U.S.C.S. § 2283](#).

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## **HN3** [down arrow] Anti-Injunction Act, Exceptions

The Anti-Injunction Act, [28 U.S.C.S. § 2283](#), creates a clear-cut prohibition qualified only by specifically defined exceptions. It is intended to forestall the inevitable friction between the state and federal courts that ensues from the injunction of state judicial proceedings by a federal court, yet the exceptions are designed to ensure the effectiveness and supremacy of federal law.

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## **HN4** [down arrow] Anti-Injunction Act, Exceptions

Both exceptions to the general prohibition of [28 U.S.C.S. § 2283](#) imply that some federal injunctive relief may be necessary to prevent a state court from so interfering with a federal court's consideration or disposition of a case as to seriously impair the federal court's flexibility and authority to decide that case.

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## **HN5** [down arrow] Federal & State Interrelationships, Anti-Injunction Act

The United States Supreme Court has repeatedly recognized the importance of federal courts exercising restraint when deciding whether to enjoin a state action. Since the statutory prohibition rests on the fundamental constitutional independence of the states and their courts, the exceptions should not be enlarged by loose statutory construction. Moreover, doubts as to the propriety of a federal injunction against state court proceedings should be resolved in favor of permitting the state courts to proceed in an orderly fashion to finally determine the controversy.

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > ... > Jurisdiction > In Rem & Personal Jurisdiction > General Overview

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Rem Actions > General Overview

Civil Procedure > ... > In Rem & Personal Jurisdiction > In Rem Actions > Quasi in Rem Actions

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## [\*\*HN6\*\*](#) [down] Anti-Injunction Act, Exceptions

A court may enjoin state court proceedings where necessary in aid of its jurisdiction. [28 U.S.C.S. § 2283](#). It is well-settled that if an action is in rem or quasi-in-rem, the court first obtaining jurisdiction over the res could enjoin suits in other courts involving the same res. In its application, this authority is broader than its terms suggest. Courts have analogized both multidistrict proceedings and large class actions to in rem actions. The analogy is based in part on the limited resources of a defendant in a mass tort or securities case and the court's interest in both equitable treatment of plaintiffs and in the possible viability of corporate defendants.

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## [\*\*HN7\*\*](#) [down] Anti-Injunction Act, Exceptions

Courts have found the [28 U.S.C.S. § 2283](#) basis for enjoining state court proceedings particularly attractive where a federal court is on the verge of settling a complex matter, and state court proceedings may undermine its ability to achieve that objective. Without the power to enjoin in that setting, defendants may be deterred from settling claims. For that reason, the imminence of settlement is an important factor in deciding whether to enjoin state court proceedings; the far-off possibility of settlement, standing alone, is insufficient. Similarly, even in the most complex of cases, a district court may not enjoin state proceedings simply because they interfere with the court's schedule.

Business & Corporate Compliance > ... > Contracts Law > Types of Contracts > Settlement Agreements

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

Civil Procedure > Settlements > General Overview

Civil Procedure > Settlements > Releases From Liability > General Overview

Civil Procedure > Settlements > Settlement Agreements > General Overview

Civil Procedure > ... > Settlement Agreements > Enforcement > General Overview

## [\*\*HN8\*\*](#) [down] Types of Contracts, Settlement Agreements

The power to enjoin does not, however, disappear once the settlement of a case has been reached. Courts must sometimes undertake the herculean task of enforcing the terms of the class settlement agreement against the constant pressure of some settlement class members who, having obtained part of a loaf through the agreement, now pursue alternative avenues to obtain additional slices. In that setting as well, state proceedings may be enjoined, in whole or in part, to effectuate the terms of the settlement.

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

## [\*\*HN9\*\*](#) [down] Federal & State Interrelationships, Anti-Injunction Act

A federal district court may properly enjoin state court proceedings that seriously impair the court's flexibility and authority to decide a case.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Civil Procedure > Remedies > Damages > General Overview

## [\*\*HN10\*\*](#) [blue icon] **Private Actions, Remedies**

A plaintiff who reaps the reward of treble damages may be no less morally reprehensible than the defendant, but the law encourages his suit to further the overriding public policy in favor of competition. A more fastidious regard for the relative moral worth of the parties would only result in seriously undermining the usefulness of the private action as a bulwark of anti-trust enforcement. And permitting the plaintiff to recover a windfall gain does not encourage continued violations by those in his position since they remain fully subject to civil and criminal penalties for their own illegal conduct.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

## [\*\*HN11\*\*](#) [blue icon] **Public Enforcement, State Civil Actions**

There is no federal policy against states imposing liability in addition to the liability imposed by federal **antitrust law**. In other words, indirect purchasers may properly sue the same defendants that have been found liable in federal court.

Civil Procedure > ... > Preclusion of Judgments > Estoppel > Collateral Estoppel

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Anti-Injunction Act > Exceptions

Civil Procedure > Judgments > Preclusion of Judgments > General Overview

Civil Procedure > ... > Preclusion of Judgments > Estoppel > General Overview

Civil Procedure > ... > Preclusion of Judgments > Full Faith & Credit > General Overview

Civil Procedure > Judgments > Preclusion of Judgments > Res Judicata

Civil Procedure > Remedies > Writs > General Overview

Civil Procedure > Remedies > Writs > All Writs Act

## [\*\*HN12\*\*](#) [blue icon] **Estoppel, Collateral Estoppel**

The relitigation exception to the All Writs Act, [\*\*28 U.S.C.S. § 1651\*\*](#), allows a district court to grant an injunction to stay proceedings in state court "to protect or effectuate its judgments." [\*\*28 U.S.C.S. § 2283\*\*](#). The exception precludes relitigation in state courts of issues previously presented to and determined by a federal court. It is

founded in the well-recognized concepts of res judicata and collateral estoppel. An essential prerequisite for applying the relitigation exception is that the claims or issues which the federal injunction insulates from litigation in state proceedings actually have been decided by the federal court. This prerequisite is strict and narrow.

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**Judges:** JOHN GLEESON, U.S.D.J.

**Opinion by:** JOHN GLEESON

## **Opinion**

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### MEMORANDUM AND ORDER

JOHN GLEESON, United States District Judge:

The plaintiff class in this action moves to enjoin *Ratner v. Wal-Mart Stores, Inc.*, Case No. CV 05 555060 (Oh Ct. Common Pl. filed Feb. 17, 2005) ("Ratner"), a proceeding in an Ohio state court. They move pursuant to the All Writs Act, [28 U.S.C. § 1651](#), and their application implicates the Anti-Injunction Act, [28 U.S.C. § 2283](#). *Ratner* is an indirect purchaser antitrust action brought by a putative class of consumers (the "Consumers") against not only Visa U.S.A., Inc. ("Visa") and MasterCard [<sup>2</sup>] International Incorporated ("MasterCard") (the defendants in this case), but also against a putative class of Ohio merchants that is a subset of the nationwide plaintiff class in this case (the "Merchants"). The Merchants contend that the injunction is necessary in aid of my jurisdiction in this case. Alternatively, they argue that the injunction is necessary to protect and effectuate my judgment in this case. The Consumers argue that I cannot properly issue such an injunction under the Anti-Injunction Act. Oral argument was held on June 3, 2005. For the reasons set forth below, the Merchants' motion is denied.

### BACKGROUND

The case before me is an antitrust action in which the Merchants, a class of approximately five million businesses of all sizes, throughout the United States, alleged, *inter alia*, that defendants Visa and MasterCard violated the [Sherman Act](#). Specifically, the Merchants alleged that Visa and MasterCard used their considerable market power in the credit card market to force them, through "Honor All Cards" policies, to accept Visa and MasterCard debit cards as well. This alleged illegal tying arrangement required the Merchants to pay excessive interchange rates [<sup>3</sup>] (*i.e.*, transaction costs) for the debit card purchases they were compelled to accept.

A jury was already empaneled and opening statements were about to commence when the parties settled. The settlements provided for, *inter alia*, a combined settlement fund exceeding \$ 3 billion and injunctive relief valued conservatively at \$ 25 billion. I assume familiarity with my decisions (a) approving the parties' settlement agreements, [In re Visa Check/Mastermoney Antitrust Litigation](#), 297 F. Supp.2d 503 (E.D.N.Y. 2003), aff'd, [Wal-Mart Stores, Inc. v. Visa U.S.A., Inc.](#), 396 F.3d 96 (2d Cir. 2005), cert. denied, [Leonardo's Pizza by the Slice, Inc. v. Wal-Mart Stores, Inc.](#), \_\_ U.S. \_\_, 161 L. Ed. 2d 1080, 125 S.Ct. 2277 (2005); (b) on the parties' motions for summary judgment, [In re Visa Check/Mastermoney Antitrust Litigation](#), 2003 U.S. Dist. LEXIS 4966, No. 96 CV 5238, 2003 WL 1712568 (E.D.N.Y. Apr. 1, 2003); and (c) certifying the class of Merchants, [In re Visa Check/Mastermoney Antitrust Litigation](#), 192 F.R.D. 68 (E.D.N.Y. 2000), aff'd, 280 F.3d 124 (2d Cir. 2001). The following is a brief summary of the facts relevant [<sup>4</sup>] to the indirect purchaser suits that followed the antitrust litigation before me.

In late 2003, after the settlements in this case, approximately 34 indirect purchaser suits were filed in 19 states and the District of Columbia (Constantine Decl. dated March 28, 2005 ("Constantine Decl.") at P16.) Seven of those actions were filed by counsel for the Consumers here. (*Id.*) The cases were filed on behalf of state residents who made purchases from merchants who had tying arrangements with Visa and MasterCard. The defendants were Visa and MasterCard, and the allegations were substantially similar to those made by the Merchants in this case. (*Id.* at PP17-18.)

*Ratner*, which was filed on February 17, 2005 in Ohio, differs from most of the other indirect purchaser actions in that it seeks to pursue Ohio merchants as a defendant class as well as Visa and MasterCard. (See Constantine Decl., Ex. O. ("Ratner Compl.")) Rather than casting those merchants as simply victims of an illegal tying arrangement, the complaint alleges that they knowingly agreed to the tying arrangements for "business reasons" and passed on the costs to consumers. (*Id.* at PP90, 94, 98.)

The Merchants [\*5] moved on March 29, 2005, to enjoin *Ratner* pursuant to the All Writs Act, [28 U.S.C. § 1651\(a\)](#).

<sup>1</sup> The Consumers oppose the motion, arguing that *Ratner* does not fall under any of the applicable exceptions to the statutory bar to enjoining state actions found in the Anti-Injunction Act.

## DISCUSSION

**HN1** The All Writs Act authorizes federal courts to "issue all writs necessary or appropriate [\*6] in aid of their respective jurisdictions and agreeable to the usages and principles of law." [28 U.S.C. § 1651\(a\)](#). **HN2** The Anti-Injunction Act limits this power when it comes to proceedings in state courts. Specifically, it provides as follows: "A court of the United States may not grant an injunction to stay proceedings in a State Court except as expressly authorized by Act of Congress, or where necessary in aid of its jurisdiction, or to protect or effectuate its judgments." [28 U.S.C. § 2283](#). In short, **HN3** the statute creates a "clear-cut prohibition qualified only by specifically defined exceptions." *Amalgamated Clothing Workers of Am. v. Richman Bros.*, [348 U.S. 511, 516, 99 L. Ed. 600, 75 S. Ct. 452, 71 Ohio Law Abs. 177 \(1955\)](#). It is intended to "forestall[] the inevitable friction between the state and federal courts that ensues from the injunction of state judicial proceedings by a federal court," yet the exceptions "are designed to ensure the effectiveness and supremacy of federal law." *Chick Kam Choo v. Exxon Corp.*, [486 U.S. 140, 146, 100 L. Ed. 2d 127, 108 S. Ct. 1684 \(1988\)](#) (quotation marks omitted). As the Supreme Court explained in *Atlantic Coast Line Railroad Company v. Brotherhood of Locomotive Engineers*, [398 U.S. 281, 26 L. Ed. 2d 234, 90 S. Ct. 1739 \(1970\)](#). [\*7]

**HN4** Both exceptions to the general prohibition of [§ 2283](#) imply that some federal injunctive relief may be necessary to prevent a state court from so interfering with a federal court's consideration or disposition of a case as to seriously impair the federal court's flexibility and authority to decide that case.

*Id.* at 295.

**HN5** The Supreme Court has repeatedly recognized the importance of federal courts exercising restraint when deciding whether to enjoin a state action. "Since the statutory prohibition . . . rests on the fundamental constitutional independence of the States and their courts, the exceptions should not be enlarged by loose statutory construction." *Atl. Coast Line R.R. Co.*, [398 U.S. at 287](#); see also *Amalgamated Clothing Workers*, [348 U.S. at 516](#); *Chick Kam Choo*, [486 U.S. at 146](#); *Ret. Sys. of Alabama v. J.P. Morgan Chase & Co.*, [386 F.3d 419, 425-26 \(2d Cir. 2004\)](#). Moreover, "doubts as to the propriety of a federal injunction against state court proceedings should be resolved in favor of permitting the state courts to proceed in an orderly fashion to finally determine the controversy.

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<sup>1</sup> Originally, the Merchants moved on March 24, 2005, to enjoin an action in Tennessee, *Bennett v. Wal-Mart Stores, Inc.*, Case No. 24139 (Tenn. Ch. Ct. filed Feb. 17, 2005) ("Bennett II"). On March 29, 2005, they sought to enjoin *Ratner* as well. As the motions were virtually identical, I scheduled them for a joint oral argument. Oral argument was held on June 3, 2005. By letter dated June 20, 2005, the Merchants sought to withdraw their motion with respect to *Bennett II*. I granted that request on June 29, 2005. Accordingly, this decision addresses only the motion to enjoin *Ratner*.

[\*8] " *Vendo Co. v. Lektro-Vend Corp.*, 433 U.S. 623, 630, 53 L. Ed. 2d 1009, 97 S. Ct. 2881 (1977) (plurality opinion) (quoting *Atl. Coast Line R.R. Co.*, 398 U.S. at 297).

The Merchants do not contend that an act of Congress authorizes the injunction they seek. However, they argue that both of the remaining exceptions to the Anti-Injunction Act apply. Those arguments are addressed below.

#### A. Necessary in Aid of Jurisdiction

**HN6** A court may enjoin state court proceedings "where necessary in aid of its jurisdiction." [28 U.S.C. § 2283](#). It is well-settled that "if an action is in rem or quasi-in-rem[,] the court first obtaining jurisdiction over the res could enjoin suits in other courts involving the same res." Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, Federal Practice and Procedure § 4221 (2d Ed. 2005); [Vendo Co.](#), 433 U.S. at 641; [Mitchum v. Foster](#), 407 U.S. 225, 235-37, 32 L. Ed. 2d 705, 92 S. Ct. 2151 (1972); [Standard Microsystems Corp. v. Texas Instruments Inc.](#), 916 F.2d 58, 60 (2d Cir. 1990). In its application, this authority is broader than its terms suggest. Courts have analogized both multidistrict ("MDL") proceedings [\*9] and large class actions to in rem actions. See [In re Baldwin-United Corp.](#), 770 F.2d 328, 337 (2d Cir. 1985) (securities class action was "so far advanced that it was the virtual equivalent of a res over which the district judge required full control"); [In re Diet Drugs Prods. Liab. Litig.](#), 369 F.3d 293, 306 (3d Cir. 2004); [In re Diet Drugs](#), 282 F.3d 220, 235 n.12 (3d Cir. 2002); [Battle v. Liberty Nat'l Life Ins. Co.](#), 877 F.2d 877, 882 (11th Cir. 1989); [In re Corrugated Container Antitrust Litig.](#), 659 F.2d 1332, 1334-35 (5th Cir. 1981); but see [Alton Box Bd. Co. v. Esprit de Corp.](#), 682 F.2d 1267, 1272 (9th Cir. 1982) (upholding lower court's denial of injunction where indirect purchasers sued the same defendant that the direct purchaser sued in the federal action because "the analogy to the in rem cases is strained"). The analogy is based in part on the limited resources of a defendant in a mass tort or securities case and the court's interest in both equitable treatment of plaintiffs and in the possible viability of corporate defendants. See [In re Diet Drugs](#), 369 F.3d at 296-97; [\*10] [In re Joint Eastern and Southern Dist. Asbestos Litig.](#), 134 F.R.D. 32, 37-38 (E.D.N.Y. & S.D.N.Y. 1990).

**HN7** Courts have found this basis for enjoining state court proceedings particularly attractive "where a federal court is on the verge of settling a complex matter, and state court proceedings may undermine its ability to achieve that objective." [Standard Microsystems Corp.](#), 916 F.2d at 60 (citing [In re Baldwin](#), 770 F.2d at 337); see [United States v. Int'l Bhd. of Teamsters](#), 907 F.2d 277, 281 (2d Cir. 1990). Without the power to enjoin in that setting, defendants may be deterred from settling claims. [In re Prudential Ins. Co. of Am. Sales Practices Litig.](#), 314 F.3d 99, 104-05 (3d Cir. 2002). For that reason, the imminence of settlement is an important factor in deciding whether to enjoin state court proceedings; the far-off possibility of settlement, standing alone, is insufficient. [In re Gen. Motors Corp. Pick-Up Truck Fuel Tank Prod. Liab. Litig.](#), 134 F.3d 133, 145 (3d Cir. 1998). Similarly, even in the most complex of cases, a district court may not enjoin state proceedings simply [\*11] because they interfere with the court's schedule. [Ret. Sys. of Alabama](#), 386 F.3d at 431.

**HN8** The power to enjoin does not, however, disappear once the settlement of such a case has been reached. Courts must sometimes undertake "the herculean task of enforcing the terms of the class settlement agreement against the constant pressure of some settlement class members who, having obtained part of a loaf through the agreement, now pursue alternative avenues to obtain additional slices." [In re Diet Drugs](#), 369 F.3d at 297. In that setting as well, state proceedings may be enjoined, in whole or in part, to effectuate the terms of the settlement. See [id. at 306, 318](#) (district court has power to enjoin settling plaintiffs from seeking punitive damages in state court where release of such claims was a "central pillar" of federal settlement); [In re Prudential Ins. Co.](#), 314 F.3d at 104-05; [Battle](#), 877 F.2d at 881.

The Merchants argue that *Ratner* threatens to interfere with this Court's jurisdiction over the distribution of the settlement fund by demanding a portion of the fund. That fund, they contend, is a [\*12] res, the protection of which authorizes the injunction they seek. For their part, the Consumers contend that this is an in personam action, and that I cannot enjoin the state action simply because it adjudicates similar claims arising out of the same tying arrangements alleged in this case. I find that enjoining *Ratner* is not necessary in aid of my jurisdiction over this case.

First, *Ratner* is not an in rem action, either strictly speaking or in the broader sense contemplated by the cases described above. The Merchants' argument that it is an effort to levy upon the settlement fund itself is factually incorrect. The sole remedy sought is an in personam judgment against a subset of the merchant class in this case. (See Tr. at 11 (Counsel for *Ratner* stating that the Consumers "are seeking an in personam judgment against Wal-Mart, Wal-mart individually licensed and, hopefully, at some point in time, a class.") Indeed, depending on outcome of the *Ratner* plaintiffs' dubious intention to certify a defendant class of conspirators in the alleged tying arrangement, it may be an extremely small subset.

Second, the justifications described above for enjoining state court [\*13] proceedings do not apply here.[HN9↑](#) This Court may properly enjoin state court proceedings that "seriously impair the [] court's flexibility and authority to decide" a case. *Atl. Coast Line R.R. Co., 398 U.S. at 295*. And this is no doubt a large, complex federal class action. But *Ratner* does not raise the specter that the limited resources of a single defendant will be fought over in both state and federal courts, jeopardizing the equitable treatment of plaintiffs in state and federal court. Neither Visa nor MasterCard, the defendants in the case before me, has joined in the instant motion. The moving parties have not paid money to settle this case; they have received it.

Nor is this case "on the verge of settling," *Standard Microsystems Corp., 916 F.2d at 60*, and thus *Ratner* cannot deter the parties in the case before me from settling. *In re Prudential Ins. Co., 314 F.3d at 104-05*. To the contrary, the settlements are now final.

Though I may enjoin *Ratner* if that is necessary to enforce the terms of the settlements, *Ratner* does not impact the enforcement of the settlements. This is not a situation where some class [\*14] members, after committing to an agreement in a federal class action, go to state court in an effort to subvert or improve upon the federal settlement. In the case before me, the Consumers who brought *Ratner* were not even parties.

In an analogous setting, the Ninth Circuit affirmed the district court's refusal to enjoin a state court action. In *Alton Box Board Co.*, indirect purchasers brought suit against the manufacturers of corrugated containers -- the same manufacturers who were being sued in an ongoing MDL action -- approximately six months after certification of a federal class. The Ninth Circuit held that the "necessary in aid of its jurisdiction" exception did not apply, in part because the plaintiff in the state court action was "not a direct purchaser, had never been and [could not] be a member of the federal class, and had never been subject to the jurisdiction of the [MDL]."[Alton Box, 682 F.2d at 1271](#).<sup>2</sup> As in *Alton Box*, the indirect purchasers here are too far removed from the federal antitrust case to warrant an injunction in aid of the federal court's jurisdiction.

[\*15] The Merchants argue that I should enjoin *Ratner* because the Second Circuit has approved of enjoining a state court proceeding even where the plaintiffs in state court were not part of the litigation in federal court. They rely on *In re Baldwin-United Corporation*, which involved a consolidated, multi-district class action brought by approximately 100,000 holders of Baldwin securities against 26 broker-dealers. *In re Baldwin, 770 F.2d at 331*. The district court coordinated settlement talks resulting in 18 of the 26 defendants signing stipulations of settlement. However, numerous state attorneys general objected that the proposed settlement did not adequately compensate the plaintiffs. *Id. at 333*. After the district court preliminarily approved the settlement, the State of New York sent several of the defendants notices of intent to bring suit "seeking restitution for New York citizens" who held Baldwin securities. *In re Baldwin, 770 F.2d at 333*. The district court enjoined any such proceedings in aid of its jurisdiction, finding that they could jeopardize the 18 proposed settlements and the settlement of remaining claims. *Id.*

In affirming, [\*16] the Second Circuit found that the states "desired to use the state proceedings to obtain additional money, over and above the settlement amounts, for distribution to members of the class in the consolidated federal actions." *Id. at 333 n.1*; see also *id. at 337*. The court noted that some states may have wished

<sup>2</sup> Another factor mentioned in the court's decision denying the injunction in *Alton Box* was that the district judge who denied the injunction was in the Northern District of California, but the district judge overseeing the MDL proceeding was in the Southern District of Texas. Thus, the Northern District of California had no "jurisdiction" to preserve. [Alton Box, 682 F.2d at 1271](#).

to pursue other remedies, such as injunctive relief and enforcement of state criminal and regulatory laws. [\*Id.\* at 333.](#) Those remedies, however, were not precluded by the injunction. [\*Id.\* at 339.](#)

As mentioned, the Merchants argue that *In re Baldwin* supports their motion because the court of appeals upheld a district court's decision to enjoin non-parties to a dispute -- the attorneys general -- in aid of its jurisdiction. I disagree. The principal rationale for upholding the injunction in *In re Baldwin* was that the enjoined claims would have sought damages for the benefit of the same plaintiffs who had brought the federal cases. That rationale does not apply in this case. The plaintiffs in *Ratner* are not parties to this case, and they could not have been parties even if they had tried. See [\*Illinois Brick Co. v. Illinois\*, 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 \(1977\)](#) [\*17] (holding that only direct purchasers can recover under federal antitrust laws). Nor are the *Ratner* plaintiffs seeking damages from the same configuration of defendants as in the case before me. In short, the posture of the cases and the parties here is not analogous to those features of *In re Baldwin*.

Moreover, the mere fact that the Merchants obtained favorable settlements in this federal case does not insulate them (or some small subset of them) from antitrust claims arising out of the same events. In holding that antitrust defendants may not shirk liability under the federal antitrust laws by arguing that plaintiffs passed on (to parties below them in the distribution chain) the costs they seek to recover, the Supreme Court stated that

[\*\*HN10\*\*](#)<sup>↑</sup> the plaintiff who reaps the reward of treble damages may be no less morally reprehensible than the defendant, but the law encourages his suit to further the overriding public policy in favor of competition. A more fastidious regard for the relative moral worth of the parties would only result in seriously undermining the usefulness of the private action as a bulwark of anti-trust enforcement. And permitting the plaintiff to recover [\*18] a windfall gain does not encourage continued violations by those in his position since they remain fully subject to civil and criminal penalties for their own illegal conduct.

[\*Perma Life Mufflers v. International Parts Corp.\*, 392 U.S. 134, 139, 20 L. Ed. 2d 982, 88 S. Ct. 1981](#) (citation omitted). Thus, even prior to the Court's holding *Illinois Brick* that only direct purchasers can recover under federal antitrust laws, the Court recognized the possibility that antitrust laws did not limit recovery to innocent victims, and may even serve to reward wrongdoers. "The purposes of the antitrust laws are best served by insuring that the private action will be an ever-present threat to deter anyone contemplating business behavior in violation of the antitrust laws." [\*Perma Life Mufflers, Inc. v. Int'l Parts Corp.\*, 392 U.S. 134, 139, 20 L. Ed. 2d 982, 88 S. Ct. 1981 \(1968\)](#), modified, [\*Copperweld Corp. v. Independence Tube Corp.\*, 467 U.S. 752, 81 L. Ed. 2d 628, 104 S. Ct. 2731 \(1984\)](#) (overruling *Perma Life* to the extent that it acquiesced in intra-enterprise conspiracy doctrine under [Section 1](#) of the Sherman Act).

After *Illinois Brick* foreclosed the ability of indirect purchasers to recover under the federal antitrust laws, the validity of indirect purchaser suits [\*19] under state law was squarely addressed by the Court in [\*California v. ARC America Corp.\*, 490 U.S. 93, 102, 104 L. Ed. 2d 86, 109 S. Ct. 1661 \(1989\)](#). In that case, four states brought price-fixing claims against cement producers under both federal and state antitrust laws as direct purchasers and under state laws as indirect purchasers. In rejecting the defendants' claim that the state indirect purchaser laws were preempted, the Court held that these laws "are consistent with the broad purposes of the federal antitrust laws: deterring anticompetitive conduct and ensuring the compensation of victims of that conduct." [\*ARC Am. Corp., 490 U.S. at 102\*](#) (citing *Illinois Brick Co.*, [431 U.S. at 746](#)). As of 2002, 19 states and the District of Columbia had passed laws known as "Illinois Brick repealers," expressly allowing indirect purchasers to recover under the states' antitrust statutes. See Jonathon T. Tomlin & Dale J. Giali, *Federalism and the Indirect Purchaser Mess*, [11 Geo. Mason L. Rev. 157, 161-62 \(2002\)](#). There is no question that the existence of such statutes complicates antitrust litigation, but that cost is incurred in furtherance of the broader [\*20] goals of deterring anticompetitive conduct and compensating victims of that conduct.

Thus, [\*\*HN11\*\*](#)<sup>↑</sup> there is no federal policy against states imposing liability in addition to the liability imposed by federal [antitrust law](#). [\*Id. at 105.\*](#) In other words, indirect purchasers may properly sue the same defendants that have been found liable in federal court. If the *Ratner* plaintiffs may properly sue Visa and MasterCard in state court -- a proposition the Merchants do not dispute -- it follows that they may sue others who acted in concert with them. The *Ratner* plaintiffs allege that some of the Merchants did precisely that, that is, they knowingly agreed to

contractual relationships with Visa and MasterCard that violated the antitrust laws and passed the resulting costs on to consumers. Whether that allegation has any merit is not for me to decide. If it does, there is no federal impediment to the *Ratner* plaintiffs seeking damages under Ohio law.

Finally, the Merchants argue that the principles discussed above allow indirect purchasers to sue only the principal antitrust violators (here, Visa and MasterCard) in state court, and do not permit claims against direct purchasers as well. [\*21] But the Merchants fail to cite any authority for such a limitation or to articulate any reason why one would be warranted. The Consumers allege that some of the Merchants, as direct purchasers, are responsible for and have benefitted from illegal restraints of trade. If those allegations are true, and I express no opinion on the matter, then the Merchants are precisely the sort of culpable parties whose standing to be plaintiffs under the federal antitrust laws does not insulate them from other civil or criminal penalties if they participated in the illegal restraints of trade. See [\*Perma Life\*, 392 U.S. at 139](#).

#### B. Necessary to Effectuate or Protect A Judgment

[\*\*HN12\*\*](#) [F] The relitigation exception to the All Writs Act allows a district court to grant an injunction to stay proceedings in state court "to protect or effectuate its judgments." [28 U.S.C. § 2283](#). The exception precludes relitigation in state courts of issues previously presented to and determined by a federal court. See [\*Chick Kam Choo\*, 486 U.S. at 147](#); [\*Smith v. Woosley\*, 399 F.3d 428, 433 \(2d Cir. 2005\)](#). "It is founded in the well-recognized concepts [\*22] of res judicata and collateral estoppel." [\*Chick Kam Choo\*, 486 U.S. at 147](#). "An essential prerequisite for applying the relitigation exception is that the claims or issues which the federal injunction insulates from litigation in state proceedings actually have been decided by the federal court. . . This prerequisite is strict and narrow." [\*Id. at 148\*](#).

The Merchants argue that the conspiracy claims in *Ratner* contradict my approval of the settlements. Specifically, they contend that the claims contradict my findings that the Merchants' claims were settled in good faith, at arm's length, and that there was no collusion. According to the Merchants, the *Ratner* plaintiffs are precluded from now alleging that the Ohio merchants had full knowledge of the tying arrangement and conspired to comply with it. I disagree.

First, the Merchants' argument oversimplifies the Consumers' allegations. The complaint in *Ratner* alleges that the tying arrangements were required by Visa and MasterCard. (*Ratner* Compl. at P2.) Some of the Ohio merchants<sup>3</sup> then passed along the cost "even after filing suit against Visa and MasterCard" (*id.* at P10) "in a successful [\*23] effort to recoup" the "tax" on debit cards (*id.* at P12.). This, according to the Consumers, led to unjust enrichment and double recovery. (*Id.* at PP12-13.) The Consumers contend that the Merchants chose to accept the fees and tying arrangements in hopes of getting business that they otherwise would not get. (*Id.* at P98.) In other words, the Merchants acted "for business reasons" and then passed on the costs to consumers. (*Id.* at PP97-99.) My finding that there was no collusion when the case was settled is not inconsistent with those allegations.

Second, even if my findings in connection with settling the class action were inconsistent with the allegations in *Ratner*, [\*24] I would not exercise my equitable power to enjoin parties who -- like the *Ratner* plaintiffs -- had no opportunity to challenge those findings. Neither the indirect purchasers nor anyone in privity or even allied in interest with them was heard in this case. Accordingly, they may not be properly bound by the factual findings it produced.

#### CONCLUSION

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<sup>3</sup>The Consumers conceded at oral argument that they are not alleging knowing complicity by every merchant who accepted debit cards. "I think we would be hard-pressed to say that every, every merchant . . . was part of the conspiracy. But certainly, Wal-Mart was and they knew about it and they participated in it." (Tr. at 20.)

For the reasons stated above, the Merchants' motion to enjoin *Ratner v. Wal-Mart Stores, Inc.*, Case No. CV 05 555060 (Oh Ct. Common Pl. filed Feb. 17, 2005) is denied. The Merchants shall inform the state court of this decision.

So Ordered.

JOHN GLEESON, U.S.D.J.

Dated: August 31, 2005

Brooklyn, New York

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## Alaska Vill. Elec. Coop., Inc. v. Crowley Marine Servs.

United States District Court for the District of Alaska

September 2, 2005, Decided

Case No. A05-0210 CV (RRB)

### **Reporter**

2005 U.S. Dist. LEXIS 39668 \*; 2005-2 Trade Cas. (CCH) P74,994

ALASKA VILLAGE ELECTRIC COOPERATIVE, INC.; INN ELECTRIC COOPERATIVE, INC.; KOTZEBUE ELECTRIC ASSOCIATION, INC.; NAKNEK ELECTRIC ASSOCIATION, INC.; CITY OF NOME D/B/A NOME JOINT UTILITY SYSTEM; NUSHAGAK ELECTRIC & TELEPHONE COOPERATIVE, INC.; and UNALAKLEET VALLEY ELECTRIC COOPERATIVE, INC., Plaintiffs, vs. CROWLEY MARINE SERVICES, INC.; CROWLEY MARITIME CORPORATION; YUKON FUEL COMPANY; NORTHLAND HOLDINGS, INC.; NORTHLAND VESSEL LEASING COMPANY, LLC; and YUTANA BARGE LINES, LLC, Defendants.

### **Core Terms**

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temporary restraining order, consent decree, state court, antitrust, injunction, anti trust law, proceedings, violates, fuel, court's jurisdiction, comment period, no necessity, take effect, documentation, authorities, effectuate, approving, economist, initiated, judgments, modified, supplier, merits, bulk

**Counsel:** [\*1] For Alaska Village Electric Cooperative Incorporated, Inn Electric Cooperative Incorporated, Kotzebue Electric Association Incorporated, Naknek Electric Association Incorporated, City of Nome, Nushagak Electric & Telephone Cooperative Incorporated, Unalakleet Valley Electric Cooperative Incorporated, Plaintiffs: John A. Leman, Kemppel Huffman et al, Anchorage, AK; Paul J. Jones, Kemppel Huff & Ellis P.C., Anchorage, AK.

For Crowley Marine Service Incorporated, Defendant: Mark E. Ashburn, Ashburn & Mason, P.C., Anchorage, AK.

For Yukon Fuel Company, Northland Holdings Incorporated, Northland Vessel Leasing Company L.L.C, Yutana Barge Lines L.L.C., Defendants: Douglas J. Serdahely, Patton Boggs LLP, Anchorage, AK; Jeffrey A. Leon, Winston & Strawn L.L.P., Chicago, IL.

**Judges:** RALPH R. BEISTLINE, UNITED STATES DISTRICT JUDGE.

**Opinion by:** RALPH R. BEISTLINE

### **Opinion**

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#### ***ORDER DENYING MOTION FOR TEMPORARY RESTRAINING ORDER***

This is an action brought by Plaintiffs seeking to prevent the sale of one business to another that allegedly violates federal antitrust law.<sup>1</sup> Crowley Marine Services, Inc. ("Crowley"), a supplier of bulk fuel to Western Alaska, seeks

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<sup>1</sup> Clerk's Docket No. 2 at 3.

to purchase Yukon Fuel Company [\*2] ("Yukon"), a similar company.<sup>2</sup> Plaintiffs argue that the sale violates federal antitrust laws because its effect "may be substantially to lessen competition."<sup>3</sup>

Before the Court reaches the merits of whether a temporary restraining order should be granted, the Court must consider whether it may be involved in this dispute at all.

Plaintiffs' Motion for Temporary Restraining Order is not the first instance where a court has considered the potential antitrust ramifications of this sale. In November of 2003, Plaintiffs filed an antitrust lawsuit in Alaska State Court to stop the sale. In March of 2004, the Alaska Attorney General initiated a formal investigation of the contemplated transaction. The State Court stayed its action until completion of this investigation. The Attorney General's investigation included interviewing people involved in large transportation services, retaining an antitrust economist [\*3] to review relevant documents, meeting with the City of Bethel, the utility groups, and Plaintiffs, and consulting with antitrust attorneys in other states and federal authorities. As a result, the Attorney General determined that modifying the sale was necessary to avoid state anti-trust violations. Thus, at the end of the eight month investigation, a consent decree was reached that allowed the sale of Yukon to go forward as long as Crowley divested certain assets and provided other accommodations to Delta Western, another supplier of bulk fuel in western Alaska. The consent decree was then published and subjected to a public comment period. The State then initiated its own complaint in State Superior Court alleging that the sale would be an antitrust violation, but that its proposed consent decree would remedy the violation.

After the expiration of the comment period, the State Superior Court proceeded to have a hearing<sup>4</sup> where Plaintiffs presented their arguments, the Assistant Attorney General presented his comments, and expert economists were heard.<sup>5</sup> On August 25, 2005, State Superior Court Judge Ben Esch issued his opinion approving consent decree and allowing the sale to [\*4] proceed. Judge Esch concluded that the sale was in the public interest. This Court has reviewed Judge Esch's opinion and found it thoughtful, thorough, and well-reasoned.

[\*5] Plaintiffs now wish this Court to issue a temporary restraining order preventing the sale while it considers whether the sale, as modified by the consent decree, is a violation of federal antitrust law. In so doing, this Court would effectively prevent the judgment of the State Superior Court from taking effect. The Anti-Injunction Act, 28 U.S.C. § 2283, "precludes federal courts from enjoining state court actions unless (1) Congress has expressly authorized such relief by statute, (2) an injunction is necessary in aid of the court's jurisdiction, or (3) an injunction is necessary to protect or effectuate the court's judgments."<sup>6</sup> "In the interest of comity and federalism, these three exceptions must be strictly construed."<sup>7</sup> Therefore, "doubts as to the propriety of a federal injunction against state court proceedings should be resolved in favor of permitting the state courts to proceed in an orderly fashion to finally determine the controversy."<sup>8</sup> The Act applies to any stage of state proceedings, including judgments and

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<sup>2</sup> *Id.*

<sup>3</sup> *Id.* (citing 15 U.S.C. § 18).

<sup>4</sup> While the court limited its review to determine whether the settlement was within the reaches of the public interest, it was not a rubber-stamp and the court considered: "(1) the degree to which the decree achieves the relief sought in the complaint; (2) the nature of the case, including the size of the defendant, the scope and complexity of the proposed settlement, and the importance of the case to the economy as a whole; (3) the quantity and quality of information available to the court on which to base an evaluation of the decree, including the competitive impact statement, public comment and government responses, and any pretrial discovery and trial evidence actually presented; (4) any prior or current history of attempts by the same parties to evade public scrutiny of alleged anti-competitive practices." Clerk's Docket No. 12 at Ex. A at 6.

<sup>5</sup> While Plaintiffs were not a party to the lawsuit, they were participants and were parties to a companion lawsuit that raised identical issues. Furthermore, the Attorney General provided them documentary evidence and they submitted formal objections to the court and participated in the hearing.

<sup>6</sup> Alton Box Board Co. v. Esprit de Corp., 682 F.2d 1267, 1270-71 (9th 1982) (quotations omitted).

<sup>7</sup> Id. at 1271.

appeals.<sup>9</sup> Additionally, "it makes no difference whether the injunction applies to the private litigants or is imposed directly on the [\*6] State Court itself.<sup>10</sup>

Here, Plaintiffs move for a temporary restraining order that would preclude the State Court's decision approving the sale from taking effect. Thus, the Act applies to prohibit this Court from so acting, unless an exception to the Act applies, which does not appear to be the case here. First, there has been no statutory authorization by Congress for the relief sought by Plaintiffs. Second, such an order is not necessary to aid the Court's jurisdiction. Third, such an order is not necessary to protect or effectuate a judgment of the Federal District Court. Thus, it appears that this Court is likely barred from granting the relief requested [\*7] by Plaintiffs.

Moreover, after having reviewed the briefs and documentation supplied by the parties, and noting the extensive nature of the investigation and litigation that led to the consent decree and subsequent State Court decision, and without even considering the issue of collateral estoppel, the Court concludes that Plaintiffs have not shown probable success on the merits or that there is a high degree of irreparable harm, which is critical to the issuance of a temporary restraining order.<sup>11</sup>

Therefore, the Court **DENIES** Plaintiffs' Motion for a Temporary Restraining Order.

This is not to say that Plaintiffs' complaint lacks merit or that Plaintiffs will ultimately fail. Indeed, although Defendants are not precluded from proceeding with the sales transaction, they do so with full knowledge of the pending litigation and its potential consequences.

ENTERED at Anchorage, Alaska, this 2nd [\*8] day of September, 2005.

RALPH R. BEISTLINE

UNITED STATES DISTRICT JUDGE

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<sup>8</sup> *Id.* (citation omitted).

<sup>9</sup> [Hill v. Martin, 296 U.S. 393, 403, 56 S. Ct. 278, 80 L. Ed. 293 \(1935\).](#)

<sup>10</sup> [Alton Box Board Co. V Espirit de Corp., 682 F.2d 1267, 1271 \(9th Cir. 1982\).](#)

<sup>11</sup> [Earth Island Inst. V. United States Forest Service, 351 F.3d 1291, 1298 \(9th Cir. 2003\).](#)



## Creative Copier Servs. v. Xerox Corp.

United States District Court for the District of Connecticut

September 2, 2005, Decided

CIVIL ACTION NO. 3:01cv155 (SRU)

### **Reporter**

2005 U.S. Dist. LEXIS 19402 \*; 2005-2 Trade Cas. (CCH) P74,929

CREATIVE COPIER SERVICES, Plaintiff, v. XEROX CORPORATION, Defendant.

**Prior History:** [Creative Copier Servs. v. Xerox Corp., 344 F. Supp. 2d 858, 2004 U.S. Dist. LEXIS 23048 \(D. Conn., 2004\)](#)

## **Core Terms**

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reasonable juror, limitations period, copiers, customers, summary judgment, machines, mitigate, argues, end-user, damages, entitled to summary judgment, light most favorable, accrued, summary judgment motion, undisputed, policies, independent violations, statute of limitations, affirmative defense, verification

## **LexisNexis® Headnotes**

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Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > Judgments > Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Motions for Summary Judgment > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Genuine Disputes

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Legal Entitlement

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Materiality of Facts

### **HN1 [] Summary Judgment, Evidentiary Considerations**

Summary judgment is appropriate when the evidence demonstrates that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law. [Fed. R. Civ. P. 56\(c\)](#). When ruling on a summary judgment motion, the court must construe the facts in the light most favorable to the non-moving party and must resolve all ambiguities and draw all reasonable inferences against the moving party. When

faced with cross-motions for summary judgment, a court must consider the evidence differently depending on which motion is being addressed.

Civil Procedure > ... > Affirmative Defenses > Statute of Limitations > Revival

Governments > Legislation > Statute of Limitations > Extensions & Revivals

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > US Department of Justice Actions > Criminal Actions > Sherman Act

Governments > Legislation > Statute of Limitations > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

## **HN2** Statute of Limitations, Revival

An action brought under the Sherman Act shall be forever barred unless commenced within four years after the cause of action accrued. [15 U.S.C.S. § 15b](#). Generally, a cause of action accrues and the statute begins to run when a defendant commits an act that injures a plaintiff's business. Although a separate cause of action accrues for each distinct violation that injures the plaintiff, not every act by an antitrust defendant is sufficient to restart the statute of limitations. Specifically, an act must (1) be a new and independent act that is not merely a reaffirmation of a previous act; and (2) it must inflict new and accumulating injury on the plaintiff. The actions cannot be merely the abatable but unabated inertial consequences of some pre-limitations action.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Horizontal Refusals to Deal > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

Antitrust & Trade Law > Sherman Act > General Overview

Governments > Legislation > Statute of Limitations > General Overview

## **HN3** Price Fixing & Restraints of Trade, Horizontal Refusals to Deal

In the "refusal to deal" context, whether a particular refusal is an independent act under the Sherman Act or is simply a reaffirmation of a prior refusal will typically turn on whether the initial refusal to deal is irrevocable, immutable, permanent and final. Consistent with that finality test, courts have found that the statute of limitations, [15 U.S.C.S. § 15b](#), does not run if, despite announcing a policy prior to the limitations period, the policy is not enforced until a period after the start of the limitations period.

Civil Procedure > Judgments > Preclusion of Judgments > Law of the Case

## **HN4** Preclusion of Judgments, Law of the Case

Decisions that were made when a case was consolidated as part of a multi-district litigation, which were not findings of fact but were resolutions of motions for which the facts were assumed to be true for purposes of deciding the motions, the decisions are not binding on the parties or the court to which the case was subsequently transferred.

Antitrust & Trade Law > Sherman Act > General Overview

Governments > Legislation > Statute of Limitations > Time Limitations

## **HN5** Antitrust & Trade Law, Sherman Act

In general a cause of action does not accrue under the Sherman Act until the plaintiff is injured.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN6** Private Actions, Remedies

An antitrust plaintiff has a duty to mitigate damages.

**Counsel:** [\*1] For Creative Copier Svc, Inc, Plaintiff: Elias A. Alexiades, New Haven, CT; James A. Hennefer, San Francisco, CA; Robert J. LaRocca, Kohn, Swift & Graf, Philadelphia, PA.

For Xerox Corp., Defendant: Frederick Brown, Orrick, Herrington & Sutcliffe, San Francisco, CA; Jon J. Nathan, Jonathan Ian Gleklen, Arnold & Porter - DC, Washington, DC; Robert P. Dolian, Cummings & Lockwood, Stamford, CT.

**Judges:** Stefan R. Underhill, United States District Judge.

**Opinion by:** Stefan R. Underhill

## **Opinion**

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### **RULING ON MOTIONS FOR SUMMARY JUDGMENT**

Creative Copier Services ("CCS") sued Xerox Corporation ("Xerox") for attempted monopolization of the market for service of Xerox high-speed copiers in violation of the Sherman Act, [15 U.S.C. § 2](#). Xerox has moved for summary judgment on its affirmative defenses of statute of limitations and failure to mitigate damages, as well as for summary judgment against CCS's monopolization claim on the theory that CCS has failed to establish a relevant market. CCS has moved for summary judgment against Xerox's two affirmative defenses. Both parties' motions are denied.

#### **I. Background**

The following facts are not subject to any genuine dispute.

[\*2] Xerox is in the business of manufacturing, selling, and servicing photocopy machines.

On April 17, 1984, Xerox established a new policy concerning the sale of replacement parts for its "10 Series" copiers. That policy stated in part:

The sale of parts which are unique to the 10 series products . . . will not be permitted to any third party, unless that third party is an end user purchaser . . . , or unless that third party is an authorized service dealer/retailer for those products under the Xerox reseller program.

(Xerox Ex. A)

In 1987, Xerox extended its parts policy to cover replacement parts for additional models of Xerox copiers. (Xerox Ex. E)

On June 1, 1989, Xerox issued a revised parts policy. The revised policy reiterated Xerox's policy of only selling parts to end-users and also established an "end-user verification" procedure, designed to ensure that Xerox did not "knowingly provide ISOs with parts, technical training, technical documentation, or other resources." (Xerox Ex. F)

As part of a 1994 consent decree, Xerox agreed to change its policy to allow ISOs to purchase replacement parts.

CCS is an independent service organization ("ISO") that services [\*3] Xerox copiers.

## II. Discussion

### A. Standard of Review

**HN1**[] Summary judgment is appropriate when the evidence demonstrates that "there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." [Fed. R. Civ. P. 56\(c\)](#); see also [Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 255-56, 91 L. Ed. 2d 202, 106 S. Ct. 2505 \(1986\)](#). When ruling on a summary judgment motion, the court must construe the facts in the light most favorable to the non-moving party and must resolve all ambiguities and draw all reasonable inferences against the moving party. [Anderson, 477 U.S. at 255](#). It follows that, when faced with cross-motions for summary judgment, a court must consider the evidence differently depending on which motion is being addressed.

B. Statute of Limitations **HN2**[] An action brought under the Sherman Act "shall be forever barred unless commenced within four years after the cause of action accrued." [15 U.S.C. § 15b](#). Generally, a cause of action accrues and the statute begins to run when a defendant commits an act that injures a plaintiff's business. [\*4] "[Zenith Radio Corp. v. Hazeltine Research, Inc., 401 U.S. 321, 338, 28 L. Ed. 2d 77, 91 S. Ct. 795 \(1971\)](#)". Although a separate cause of action accrues for each distinct violation that injures the plaintiff, "not every act by an antitrust defendant is sufficient to restart the statute of limitations." [Pace Industries v. Three Phoenix Co., 813 F.2d 234, 237 \(9th Cir. 1987\)](#). Specifically, an act must (1) be a new and independent act that is not merely a reaffirmation of a previous act; and (2) it must inflict new and accumulating injury on the plaintiff. [\*Id. at 238\*](#). The actions cannot be merely the "abatable but unabated inertial consequences of some pre-limitations action." [In re Ciprofloxacin Hydrochloride Antitrust Litigation, 261 F. Supp. 2d 188, 229 \(E.D.N.Y. 2003\)](#) (quoting [AI George v. Envirotech Corp., 939 F.2d 1271 \(5th Cir. 1991\)](#)).

**HN3**[] In the "refusal to deal" context, whether a particular refusal is an independent act or simply a "reaffirmation" of a prior refusal will typically turn on whether the "initial refusal to deal is irrevocable, immutable, permanent and final." 2 Philip Areeda & Herbert Hovenkamp, [\*5] [Antitrust Law](#) P320 (2d ed. 2000). Consistent with that "finality" test, courts have found that the statute does not run if, despite announcing a policy prior to the limitations period, the policy is not enforced until a period after the start of the limitations period. [DXS, Inc. v. Siemens Medical Systems, 100 F.3d 462 \(6th Cir. 1996\)](#).

Both parties agree that the statute of limitations bars CCS from asserting any claims that accrued prior to March 23, 1988.

### 1. Xerox's Motion for Summary Judgment

Xerox argues that it is entitled to summary judgment<sup>1</sup> on its affirmative defense of statute of limitations on the grounds that: (1) it is undisputed that Xerox's parts policy was finalized no later than 1987, and therefore any subsequent actions taken were merely "reaffirmations" of that policy, not independent violations; and (2) even if Xerox's actions in the limitations period did constitute independent acts, there is no evidence that those actions inflicted any new injury on CCS. Construing the evidence in the light most favorable to CCS, I conclude summary judgment is inappropriate on either ground.

[\*6] a. Independent Violation

Xerox argues it is undisputed that since 1984 -- and certainly since 1987 -- it has had a firm policy of not selling parts to ISOs, and its 1989 revision to the policy only changed the mechanism for enforcing that policy, not the policy itself. I agree that since 1984 Xerox has had a policy of not selling parts to ISOs. Nevertheless, I think reasonable jurors could find that from 1984 to 1989 that policy contained a fairly broad exception for ISOs who personally owned Xerox equipment, and it was not until 1989 that Xerox extended its refusal to deal to include those ISOs. In other words, jurors could reasonably find that prior to 1989 Xerox was generally willing to deal with an ISO if that ISO owned Xerox equipment, but after 1989 Xerox substantially limited the circumstances under which it would allow such equipment-owning ISOs to purchase parts. Several pieces of evidence permit such a finding.

First, the plain language of Xerox's two policies admits of this interpretation. The 1984 policy forbade sale of replacement parts subject to the following broad exception: "unless that third party is an end user purchaser." The 1989 policy, by contrast, restricted [\*7] the definition of an end-user to only someone who used the copier "to make internal copies or to sell copies to the public or in a Facilities Management Operation." The policy went on to explain:

we will not sell . . . to an end-user if we have reason to believe that such resources will be used for purposes other than maintenance of the unit of equipment for which these resources are ordered. . . .

As a general rule, ISOs . . . are not considered to be eligible for sale of resources, including parts, on restricted products.

(Xerox Ex. F at 1) Thus, jurors could reasonably read the 1984 policy to mean that Xerox would deal with anyone who owned a Xerox machine *regardless* of whether that person was also an ISO, but read the 1989 policy to mean that Xerox would deal with anyone who owned a Xerox machine *unless* that person was also an ISO (except when the ISO could demonstrate very specific use requirements).

Second, the statements of CCS employees - at least when read in the light most favorable to CCS - also support a finding that Xerox did not, for the most part,<sup>2</sup> refuse to deal with enduser ISOs, such as CCS, prior to 1989, but did refuse to deal with them [\*8] after 1989. William Dixon stated that in 1987 Xerox told him if he showed a serial number for a machine he owned he could order parts. (Dixon Aff. at 42) Similarly, Theodis Bethea, a CCS employee, testified that initially Xerox would allow orders so long as CCS could provide a serial number, and only later imposed stricter requirements. (Bethea Dep. at 15)

[\*9] Alternatively, even if a jury concluded that Xerox's 1989 policy only restated the policy previously announced in 1984, there is sufficient evidence from which reasonable jurors could conclude that the policy was not seriously enforced until after the limitations period. As just noted, there is evidence that Xerox required only minimal

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<sup>1</sup> Xerox's motion is only a motion for partial summary judgment. It does not, for example, address (a) CCS's claim that Xerox engaged in anti-competitive conduct other than "refusal to deal," or (b) CCS's claim that Xerox restarted its refusal to deal after the 1994 consent decree.

<sup>2</sup> Admittedly, there is some evidence that on occasion Xerox either reduced or rejected some CCS parts orders prior to 1989. (Xerox Ex. B; Dixon Dep. at 348-52) Construed in CCS's favor, that evidence only demonstrates that Xerox was not entirely willing to deal with end-user ISOs prior to 1989. It is, however, still consistent with a finding that, for the most part, Xerox was willing to deal with end-user ISOs prior to 1989, and, for the most part, was not willing to deal with them after 1989. (That is, of course, not the only inference that could be drawn from the evidence, but it is a reasonable one, which I must draw when deciding a motion for summary judgment.)

verification of copier ownership in order to allow orders. (Dixon Aff. at 42; Bethea Dep. at 15) Moreover, there is evidence that CCS was, in general, easily able to obtain needed parts prior to 1989 (Dixon Aff. PP35, 41, 44), as well as evidence that Xerox dramatically strengthened its enforcement techniques after 1989. Construed in the light most favorable to CCS, that evidence could reasonably be taken to indicate that, prior to the limitations period, Xerox's policy, at least as applied to CCS, was not strictly enforced and did not result in an actual refusal to deal.

Consequently, because jurors could reasonably conclude that Xerox's 1984 policy was not a complete refusal to deal, Xerox is not entitled to summary judgment on the ground that the 1989 policy was merely a "reaffirmation" of a prior refusal.

#### b. New Injury

Xerox argues that, even [**\*10**] if its 1989 policy was an independent violation, there is no evidence that the policy caused any new injury to CCS. I disagree.

There are several pieces of evidence from which reasonable jurors could find that the 1989 policy caused a new injury to CCS's business. Dixon testified that the 1989 policy caused more harm to CCS than the previous policy. (Dixon Aff. P48) Several of CCS's clients testified that they did not experience any decline in CCS's ability to offer service until after 1989. (Payne Dep. at 17; Lewis Dep. at 21) CCS's expert, Jonathan Cunitz, opined that Xerox did not have ascertainable damages before 1990. (Cunitz Decl. P2)

Xerox's argues, however, that because it never conducted an "end-user verification" of CCS's equipment - a procedure provided for by the 1989 policy - there is no way the 1989 policy could have injured CCS. Although end-user verification was a significant part of the 1989 policy, there is evidence from which reasonable jurors could conclude that other changes introduced by the 1989 policy caused CCS harm. For example, Dixon stated that, starting in 1989, Xerox would delay orders in order to determine whether it needed to conduct verification and [**\*11**] would require CCS to match ordered parts with specific machines. (Dixon Aff. PP44-45)

Accordingly, because there is evidence from which reasonable jurors could conclude that CCS received fresh injury from Xerox's 1989 policy, summary judgment on the ground that the 1989 policy did not cause any harm is inappropriate.

### 2. CCS's Motion for Summary Judgment

CCS argues that it is entitled to summary judgment against Xerox's affirmative defense of statute of limitations on two grounds: (1) that the record evidence compels a finding that Xerox engaged in independent violations within the limitation period; and (2) that the evidence compels a finding that CCS was not injured by any of Xerox's action until after the limitations period began. Viewing the evidence in the light most favorable to Xerox (because now CCS is the moving party), I conclude that neither finding is compelled.<sup>3</sup>

#### [**\*12**] a. Independent Violation

Although I concluded above that reasonable jurors, viewing the evidence in the light most favorable to CCS, could find that the 1989 policy constituted an independent refusal to deal, that is not the same as concluding that the evidence compels such a finding. On the contrary, when the evidence is viewed in the light most favorable to Xerox, a very different finding is possible.

First, reasonable jurors could read the 1989 policy as merely restating the 1984 policy and providing additional mechanisms for enforcing that, unchanged, policy. Both policies forbade sales to ISOs and allowed sales to end

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<sup>3</sup>CCS also argues that the prior decision of the District of Kansas, when this case was consolidated as part of a multi-district litigation, settled the question whether the 1989 actions constituted an independent act. That argument has no merit. [HN4](#)↑ The Kansas decisions were not findings of fact, they were resolutions of motions, and the facts used by the court in deciding those motions were assumed true only for the purposes of those motions. They are, consequently, not binding on Xerox or this court.

users, and it would be quite reasonable to read the additional language contained in the 1989 policy as an elaboration, not an expansion, of the 1984 policy's restrictions.

Second, there is evidence that Xerox informed CCS as early as 1986 that it could only purchase parts for its machines if it actually needed the parts to service those machines. For example, in a letter dated October 10, 1986, Xerox informed CCS that it was reducing CCS's order to "those quantities deemed reasonable to support the machines our records indicate you personally own."<sup>4</sup> (Xerox [\*13] Ex. B)

Third, although the evidence that CCS was able to obtain parts easily prior to 1989 could support a finding that Xerox did not refuse to deal before 1989, that evidence could merely reflect that CCS needed fewer parts before 1989 or that some Xerox employees were not diligent in enforcing Xerox's policies.

Accordingly, because reasonable jurors could find that Xerox's 1989 policy was not an independent refusal to deal but was only the further implementation of its prior refusal, CCS is not entitled to summary judgment on that ground.

#### b. Pre-Limitations Injury

CCS also argues that, even if Xerox's 1989 policy was [\*14] not an independent refusal to deal, there is no evidence that CCS was injured prior to the start of the limitations period and therefore it is undisputed that CCS's cause of action did not accrue before the limitations period.

Although it is true that [HN5](#) in general a cause of action does not accrue until the plaintiff is injured, there is plenty of evidence in this case that CCS was injured by Xerox's 1984 policy well before the start of the limitations period. CCS was forced to buy machines, at significant expense, in order to qualify as an end-user. (Dixon Aff. P37) CCS was forced to ask its customers to order parts on its behalf. (Dixon Aff. P41) One of CCS's employees was kicked out of a Xerox training class. (Dixon Aff. P40) CCS was forced to forgo an opportunity to expand its business into New York. (Dixon Tr. at 349)

In light of that evidence, reasonable jurors could find that CCS's injury accrued well before the start of the limitations period, making summary judgment against the statute of limitations defense inappropriate.

#### C. Mitigation of Damages

[HN6](#) "An antitrust plaintiff has a duty to mitigate damages." *Litton Systems, Inc. v. AT&T*, 700 F.2d 785, 820 n.47 (2d Cir. 1980). [\*15] Xerox argues that is entitled to summary judgment on this affirmative defense because it is undisputed that CCS could have, but did not, ask all its customers to order parts directly from Xerox. CCS argues that, on the contrary, it is entitled to summary judgment against this defense because it is undisputed that it took all reasonable steps to mitigate its damages.

There is some evidence that CCS was able to mitigate the effect of Xerox's policies by asking some of its customers to order parts. (Dixon Aff. PP35, 42) On the basis of that evidence, reasonable jurors could find that, had this been done with all customers, CCS might have significantly mitigated its damages. On the other hand, there is also evidence that it was not feasible for CCS to ask all of its customers to order parts because (a) some of its contracts required CCS to get the parts and (b) CCS's reputation would be harmed if its customers thought it could not obtain parts. (Dixon Aff. PP67-69) On the basis of that evidence, reasonable jurors could find that CCS could not have mitigated its damages more than it actually did.

In short, this a classic example of a disputed issue of material fact. Reasonable jurors [\*16] could find that CCS could have mitigated its damages by asking more customers to order parts. Nevertheless, reasonable jurors could

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<sup>4</sup>The letter does not, however, establish conclusively that this was Xerox's policy as of 1986. There is evidence that Xerox subsequently relented and allowed CCS to order some of the requested parts. (Xerox Ex. D) Moreover, as explained above, *supra* n.2, the fact that on occasion Xerox reduced parts orders does not compel a conclusion that it had by then made a final refusal to deal.

also find that this was not always a practical solution, and, where it was practical, CCS did get its customers to order parts. Consequently, neither party is entitled to summary judgment on the mitigation issue.

#### D. Relevant Market

Xerox argues that in order to establish that the market for servicing Xerox high-speed copiers is the relevant market for antitrust purposes, CCS must establish that Xerox changed one or more of its policies regarding service of copiers *after* some customers had already purchased affected copiers. Xerox contends that CCS has not met that burden because "the undisputed facts show that Xerox has not changed its policies within the limitations period."

Even assuming that Xerox's statement of the law is correct, its assertions about the state of the record are not. As explained above, reasonable jurors could find that Xerox *did* change its policy within the limitations period and, consequently, reasonable jurors could find that customers who purchased copiers between 1984 and 1989 were unaware of the limitations that [\*17] would be imposed on their ability to obtain ISO service. In other words, reasonable jurors could find that customers bought Xerox copiers at a time when it was reasonable for them to expect - either because of the exceptions in Xerox's 1984 policy or Xerox's failure to enforce that policy - that they could obtain low-cost, reliable, third-party service, only to later find - because of Xerox's 1989 change in policy or decision to start enforcing its earlier policy - that reliable service could not be obtained from those third-parties. Summary judgment on this ground is, therefore, unwarranted.

### III. Conclusion

Xerox's motion for summary judgment (doc. # 76) is DENIED. CCS's motion for summary judgment (doc. # 88) is DENIED.

It is so ordered.

Dated at Bridgeport, Connecticut, this 2nd day of September 2005.

/s/ Stefan R. Underhill

United States District Judge

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## **Basic Med. Care Plus, Inc. v. N.C. Mut. Life Ins. Co.**

United States District Court for the Middle District of North Carolina

September 6, 2005, Decided ; September 6, 2005, Filed

1:03CV00269

**Reporter**

2005 U.S. Dist. LEXIS 33033 \*; 2005 WL 2205016

BASIC MEDICAL CARE PLUS, INC., Plaintiff, v. NORTH CAROLINA MUTUAL LIFE INSURANCE COMPANY, Defendant.

### **Core Terms**

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Mutual, terminate, sales, counterclaims, unfair, premium, deceptive trade practices, summary judgment, lost profits, breach of contract, termination notice, matter of law, quarterly, damages, lawsuit, breach of contract claim, medical care, interpolation, competitor, annual, argues, anticipatory repudiation, target, partial summary judgment, summary judgment motion, insurance company, abuse of process, nominal damages, nonmoving party, memorandum

### **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

#### **HN1[] Summary Judgment, Entitlement as Matter of Law**

The summary judgment standard of review under *Fed. R. Civ. P. 56* is well established. A party is entitled to judgment as a matter of law upon a showing that there is no genuine issue as to any material fact. *Fed. R. Civ. P. 56(c)*. The material facts are those identified by controlling law as essential elements of claims asserted by the parties. A genuine issue as to such facts exists if the evidence forecast is sufficient for a reasonable trier of fact to find for the nonmoving party. No genuine issue of material fact exists if the nonmoving party fails to make a sufficient showing on an essential element of its case as to which it would have the burden of proof at trial.

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

#### **HN2[] Appellate Review, Standards of Review**

In evaluating a forecast of evidence on summary judgment review, the court must view the facts and inferences reasonably to be drawn from them in the light most favorable to the nonmoving party. When the moving party has carried its burden, the nonmoving party must come forward with evidence showing more than some "metaphysical doubt" that genuine and material factual issues exist. A mere scintilla of evidence is insufficient to circumvent summary judgment. Instead, the nonmoving party must convince the court that, upon the record taken as a whole, a

rational trier of fact could find for the nonmoving party. Trial is unnecessary if the facts are undisputed, or if disputed, the dispute is of no consequence to the dispositive question.

Business & Corporate Compliance > ... > Contracts Law > Breach > Anticipatory Repudiation

### **HN3** Breach, Anticipatory Repudiation

Repudiation is a positive statement by one party to the other party which indicates that the party will not or cannot substantially perform its contractual duties. A party to a contract repudiates his obligation under a contract when he expresses, by words or conduct, a positive, distinct, unequivocal and absolute refusal to perform. When a party repudiates its obligations under a contract before the time for performance under the contract, the repudiation becomes an anticipatory breach of the contract.

Contracts Law > ... > Sales of Goods > Breach, Excuse & Repudiation > General Overview

### **HN4** Sales of Goods, Breach, Excuse & Repudiation

The law in North Carolina is well-settled that if a party to the contract states that he cannot perform except on some condition which goes outside the terms of his contract then the statement will constitute a repudiation.

Contracts Law > Contract Interpretation > Ambiguities & Contra Proferentem

### **HN5** Contract Interpretation, Ambiguities & Contra Proferentem

When the language of a contract is plain and unambiguous then construction of the agreement is a matter of law for the court.

Contracts Law > ... > Estoppel > Equitable Estoppel > Elements of Equitable Estoppel

### **HN6** Equitable Estoppel, Elements of Equitable Estoppel

Equitable estoppel arises when a party by acts, representations, admissions, or by silence induces another to believe that certain facts exist, and such other person rightfully relies and acts upon that belief to his or her detriment.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices

Business & Corporate Compliance > ... > Breach > Contracts Law > Breach

### **HN7** Consumer Protection, Deceptive & Unfair Trade Practices

Under North Carolina law, "substantial aggravating circumstances" must accompany a breach of contract in order to give rise to an unfair or deceptive trade practice.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices

## [\*\*HN8\*\*](#) Consumer Protection, Deceptive & Unfair Trade Practices

The doctrines governing federal **antitrust law** apply to the North Carolina Unfair or Deceptive Trade Practices Act, N.C. Gen. Stat. § 75.1-1. A plaintiff may not be held liable under federal **antitrust law** for bringing an "objectively reasonable" lawsuit, regardless of the plaintiff's subjective intent in bringing the suit. A lawsuit is objectively reasonable if an objective litigant could conclude that the suit is reasonably calculated to elicit a favorable outcome.

Torts > Intentional Torts > Abuse of Process > Elements

## [\*\*HN9\*\*](#) Abuse of Process, Elements

To establish a claim of abuse of process, a defendant must show that (1) a proceeding was initiated against it by the plaintiff or used by the plaintiff to achieve an ulterior purpose; and (2) once the proceeding was initiated, the plaintiff committed some willful act not proper in the regular prosecution of the proceeding. Where a defendant has made no attempt to show a willful or improper act by the plaintiff subsequent to the filing of the action, the defendant's counterclaim for abuse of process must be dismissed. Summary judgment is appropriate for a defendant where a plaintiff's allegations deal only with defendant's motives in filing the suit, rather than any abuse of the judicial system after the institution of the lawsuit.

Contracts Law > ... > Measurement of Damages > Foreseeable Damages > Lost Profits

## [\*\*HN10\*\*](#) Foreseeable Damages, Lost Profits

The North Carolina Supreme Court has declined to adopt the "new business rule," a per se rule which would preclude lost profit damages for a new business with no established history of profitability. However, the Court has recognized that lost future profits are difficult for a new business to calculate and prove, and adopted the well-established principle of law that proof of damages of lost profits must be made with reasonable certainty.

Contracts Law > ... > Measurement of Damages > Foreseeable Damages > Lost Profits

Evidence > Types of Evidence > Testimony > Expert Witnesses

## [\*\*HN11\*\*](#) Foreseeable Damages, Lost Profits

Under North Carolina caselaw, an expert opinion on lost profits based on his experience 30 years ago is wholly insufficient to support a claim for lost profits.

Contracts Law > ... > Measurement of Damages > Foreseeable Damages > Lost Profits

Evidence > Types of Evidence > Testimony > Expert Witnesses

## [\*\*HN12\*\*](#) Foreseeable Damages, Lost Profits

The North Carolina courts have not allowed claims for lost profits where an expert's opinion is based solely on the claimant's own speculative business plan and not based on any independent research or data or any comparison to similar businesses.

Business & Corporate Compliance > ... > Breach > Contracts Law > Breach

Contracts Law > ... > Damages > Measurement of Damages > Nominal Damages

### **HN13** [Contracts, Breach]

Where a plaintiff proves breach of contract he is entitled at least to nominal damages. When a prima facie case of breach of contract is made out, but there is no evidence upon which a jury could base a damage award, the injured party is still entitled to nominal damages for invasion of his legal rights.

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**Judges:** SHARP, Magistrate Judge.

**Opinion by:** P. Trevor Sharp

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

**SHARP, Magistrate Judge**

This matter comes before the Court on (1) a motion by Defendant North Carolina Mutual Life Insurance Company ("NC Mutual") for summary judgment and for partial summary judgment (Pleading No. 23); and (2) a cross-motion by Plaintiff Basic Medical Care Plus, Inc. ("Basic Medical") for partial summary judgment (Pleading No. 25). The motions have been fully briefed, and the [\*2] parties have been heard in oral argument. The motions are ready for a ruling.

#### **I. Procedural History**

On March 25, 2003, Plaintiff Basic Medical filed a complaint in this Court seeking damages against Defendant NC Mutual for breach of contract and unfair or deceptive trade practices in connection with the development of an insurance product called Basic Medical Care Plus. On May 30, 2003, Defendant NC Mutual filed an answer denying the material allegations in Plaintiff's complaint and asserting counterclaims of breach of contract, unfair or deceptive trade practices, and abuse of process against Plaintiff. Plaintiff filed a reply to the counterclaims on June 17, 2003. After a period of discovery, Defendant NC Mutual filed a motion for summary judgment and partial summary judgment, requesting the Court to grant summary judgment in its favor on its breach of contract and unfair or deceptive trade practices counterclaims and to dismiss all of Plaintiff's claims with prejudice. In turn, Plaintiff Basic

Medical filed a cross-motion for partial summary judgment, urging the Court to grant summary judgment in Plaintiff's favor on its breach of contract claim and to dismiss all of Defendant's [\*3] counterclaims with prejudice.

## II. Statement of Facts

In May 1995, Henry "Hank" J. Miller ("Miller"), a resident of Tennessee and former insurance sales agent for the American Family Life Assurance Company ("AFLAC"), purchased a property and casualty insurance company called Vol-State Agency, Inc. ("Vol-State"). He has owned and operated the business since that time. (Pleading No. 26, Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 1, Henry J. Miller Dep. at 9-11, 68, 79, 83.) In 1997, Miller began researching the creation of a new insurance product (the "Product") which would provide affordable, basic health insurance benefits to employees of small business owners who would not otherwise offer health coverage. *Id.* at 85, 97-98.

In April or May 2000, Miller solicited a consultant to assist him in finding an insurance company to underwrite the Product. *Id.* at 102-07, 110-12. The consultant introduced Miller to James Parrish, who was at that time the Executive Vice President of Defendant NC Mutual, a life insurance company headquartered in Durham, North Carolina. *Id.* at 111; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 2, James N. Parrish Dep. at 67. [\*4] On September 20, 2000, Miller met with Parrish about the Product, and Parrish became Miller's contact person at NC Mutual regarding the Product. (Miller Dep. at 111; Parrish Dep. at 67, 76-77; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 3.)

Although NC Mutual had done very limited business in the field of health insurance, Miller persuaded representatives of NC Mutual that the Product could succeed, forecasting \$ 25 million in sales within five years. (Pleading No. 34, Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. L, Charles D. Watts, Jr. Dep. at 64; Ex. J, Henry J. Miller Dep. (Def.)<sup>1</sup> at 85, 137-38.) On or about November 3, 2000, Parrish called Miller to advise him that NC Mutual was "prepared to go forward" in bringing the Product to market. (Parrish Dep. at 90-95.) Miller sent Parrish a letter that same day to confirm the substance of their telephone conversation. (Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 5.)

[\*5] On approximately November 15, 2000, in anticipation of his retirement from NC Mutual, Parrish entered into an agreement with NC Mutual in which he agreed as follows:

Basic Medical Care Plus Plan: CONSULTANT shall develop a new product in the basic medical care area by July 1, 2001, for which he shall take the steps necessary to launch the product, provide the necessary management and operating services for the product as a self-contained unit including policy filing and follow-up, any licensing follow-up, daily operations, interfacing with the managing general agent and the third party administrator for that product, preparation of accounting entries and any other aspects of this product that the CONSULTANT and the COMPANY agree upon.

(Parrish Dep. at 97, 106, 108; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 6 at 2.) In late 2000 and early 2001, Parrish worked with the Actuarial Resources Corporation to develop and price an appropriate premium structure for the Product. (Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Exs. 9-12.) On February 21, 2001, Miller and Parrish discussed the status of the Product and the terms of the Marketing Agreement to be signed [\*6] by the parties. (Parrish Dep. at 148-51; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 13.) At the end of February 2001, Parrish retired from NC Mutual and continued to work on the Product pursuant to the terms of his Consultant Agreement. (Parrish Dep. at 100, 123-24.) On March 6, 2001, Parrish certified an Actuarial Memorandum for the Product, and on March 12, 2001, NC Mutual filed the necessary paperwork with the North Carolina Department of Insurance to ensure that the Product was approved for sale in North Carolina. (Parrish Dep. at 152; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 14; Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. E.)

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<sup>1</sup> The Court will cite to the portions of depositions attached to Plaintiff's briefs as, e.g., "Miller Dep. at 10." Citations to the portions of depositions attached to Defendant's briefs will appear as, e.g., "Miller Dep. (Def.) at 10."

On March 15, 2001, Miller sent a letter to Parrish asking for the status of the Marketing Agreement. (Parrish Dep. at 153-56; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 15.) Meanwhile, in March or April 2001, Miller incorporated and became president of Basic Medical Care Plus, Inc., a Tennessee corporation formed to market the Product in North Carolina and Tennessee. (Miller Dep. (Def.) at 112-13, 124-25, 148.) On May 16, 2001, Parrish faxed Miller a proposed Marketing Agreement, and Miller responded [\*7] with his own suggestions about the agreement's terms. (Parrish Dep. at 157; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 16.) On July 17, 2001, the North Carolina Department of Insurance approved the Product for sale in North Carolina. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. E at 191.) At approximately the same time, the Product was also approved for sale in Tennessee. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. Q, Goldie Evans Dep. at 27.)

On July 18, 2001, Miller traveled from Tennessee to Durham to meet with representatives of NC Mutual to finalize the terms of the Marketing Agreement. Parrish had prepared a memorandum informing several of NC Mutual's representatives of the meeting with Miller. (Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 19.) When Miller arrived in Durham, however, he was told that the President of NC Mutual, Bert Collins, was not available, and that the Marketing Agreement would have to be signed at a later date. (Pleading No. 1, Compl. P 18.)

Shortly thereafter, Parrish learned that certain representatives of NC Mutual were becoming reluctant to finalize the agreement that had been [\*8] reached orally between Miller and Parrish. In a memorandum dated July 20, 2001, Parrish wrote to Collins as follows:

I was surprised to learn that you are now having reservations about this product. While still serving as Executive Vice President of NCM and at your urging, I worked with Hank Miller to bring this product to fruition as a source of new revenue for NCM. I made verbal commitments on several occasions that NCM wanted to move forward with the project. When Hank wanted to have NCM's commitment in writing, I developed a Marketing Agreement, . . . had it reviewed by Counsel, negotiated it with Hank Miller and committed to it verbally. I hope that you will go ahead and sign the agreement immediately.

...

As you know, I was never a proponent of health insurance but I feel good about the potential success of this venture.

...

. . . Because of the urgency that you felt for new premium sources, I pursued this project and recommend that you continue with it.

(Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 20.) Parrish followed up the July 20, 2001 memorandum with a July 28, 2001 letter to Chuck Watts, Senior Vice President and General [\*9] Counsel for NC Mutual, which provided as follows:

I do not agree with top management's refusal to sign the Marketing Agreement as negotiated in good faith with Miller. I believe that it is a mistake to take the steps that you are planning and do not wish to be associated with these efforts in any way. If the company does incur some liability as a result of the willful and intentional acts associated with [the] failure to continue with the project as agreed to with Hank Miller, please be advised that I would consider Section XII of the Consulting Agreement applicable and any monetary loss that I might suffer as a result of being drawn into the ill-advised course of action that top management has chosen will be borne by the Company.

Please notify Hank Miller that I am no longer associated with this project on Monday.

*Id.*, Ex. 21.

Notwithstanding these areas of conflict, Collins and Miller finally executed the Marketing Agreement in late September 2001.<sup>2</sup> *Id.*, Ex. 23. The Marketing Agreement named Basic Medical as NC Mutual's exclusive marketing

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<sup>2</sup> Although the Marketing Agreement was signed by the parties some time in late September 2001, the agreement contained an effective date of April 1, 2001. The record provides no explanation for this discrepancy. (Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 23.)

agent for the Product in North Carolina and Tennessee, and NC Mutual agreed to pay Basic Medical and its sales [\*10] agents a commission for every policy of the Product sold in those states. *Id.* PP 1.1, 3.1. In return, the Marketing Agreement required Basic Medical to achieve the following yearly minimum premium sales levels:

2002	\$ 1,000,000
2003	\$ 1,500,000
2004	\$ 2,000,000
2005	\$ 2,500,000
Any year after 2005	\$ 3,000,000

*Id.* P 3.2. The Marketing Agreement further provided that it could be terminated, among other reasons, (1) upon ninety days' written notice by either party if the agreement's minimum premium sales levels were not met; or (2) by NC Mutual upon NC Mutual's withdrawal of the Product from the market, provided that NC Mutual did not then market the Product anywhere in the United States during the following year. *Id.* PP 4.2, 5.1.1, 5.1.2.

[\*11] After the execution of the Marketing Agreement, Miller worked towards fulfilling Basic Medical's contractual obligations by securing investors, recruiting agents and investing his own money. (Miller Dep. at 148, 160-68.) However, Miller was not able to devote a significant amount of time to these tasks in January, February, and March 2002, because his other company, Vol-State, was burdened with sharply increasing business demands following a change in Tennessee's insurance laws in January 2002. (Miller Dep. at 167-68; Pleading No. 37, Pl.'s Br. in Opp'n to Def.'s Mot. for Summ. J. and Partial Summ. J., Ex. 27, Henry J. Miller Aff. P 3; Miller Dep. (Def.) at 192; Pleading No. 31, Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J., Ex. M, Miller Dep. Vol. II (Def.) at 60-61.) Also during this time, NC Mutual was undergoing a strategic planning process and examining its business organization and executive structure in anticipation of the retirement of Bert Collins and James Parrish. (Watts Dep. at 6-7.) As part of this process, NC Mutual reevaluated its decision to offer health insurance policies for sale, including the Product. As a result, NC Mutual carefully monitored Basic Medical's [\*12] performance under the Marketing Agreement. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. H, resp. to interrog. no. 5.)

On March 7, 2002, Watts called Miller and informed him that NC Mutual was dissatisfied with the progress that Miller had made towards the 2002 minimum premium sales requirement of \$ 1,000,000.<sup>3</sup> [\*14] (Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J., Ex. A, Charles D. Watts, Jr. Aff. P 14; Miller Dep. (Def.) at 204) On March 11, 2002, Miller received a fax from Watts which provided in relevant part as follows:

Pursuant to our conversation last week, it appears to us, given the performance of the first quarter of this year, that there is very little chance that you would be able to meet the sales targets that are established in our agreement dated April 1, 2001, as amended. Under paragraph 5.1.1 either party may terminate the agreement "upon ninety (90) days prior written notice to the other if or when production requirements . . . are not met." While the production amounts are stated as annual goals, we believe that nothing in the agreement precludes our interpolating them into quarterly goals. Thus, since we believe that you will not [\*13] have made any material progress toward to [sic] meeting [the] one quarter of the million dollar annual target by March 31, 2002, we are giving notice of termination to be effective June 1, 2002.

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<sup>3</sup>The parties dispute the contents of the remainder of their conversation on March 7, 2002. Miller maintains that he advised Watts of the business demands on Vol-State and his temporary inability to devote more time to development of the Product. (Miller Aff. P 3; Miller Dep. at 168; Miller Dep. (Def.) at 192, 196; Miller Dep. Vol. II (Def.) at 63.) Watts denies that Miller mentioned this time commitment to Vol-State in any fashion. (Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J., Ex. O, Charles D. Watts, Jr. Dep. Vol. II at 15.)

. . . We will continue to support you in any way that we can and if your performance begins to approach targeted levels before June 1, 2002 nothing could make us happier than to rescind this letter of termination.

(Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 26.) Miller did not agree with Watts that the Marketing Agreement gave NC Mutual the right to "interpolate" the annual premium goals into quarterly goals.<sup>4</sup> (Miller Aff. P 5; Miller Dep. (Def.) at 196, 198, 204.) Miller felt that it "would have been inappropriate and irresponsible to continue to hire a sales force in light of the notice of termination." (Miller Aff. P 7.) Accordingly, Miller interpreted Watts' March 11th letter as a termination of the Marketing Agreement and held a meeting with his board of directors, which voted to cease all operations immediately. *Id.* P 4; Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 25; Miller Dep. (Def.) at 152.).

Following the board's decision to cease all operations of Basic Medical, Miller took no further actions to market the Product or a similar health insurance policy to any other insurance companies. (Miller Dep. (Def.) at 205-08; Miller Dep. Vol. II (Def.) at 32-33.)

### **III. Summary Judgment Standard of Review**

**HN1**[] The summary judgment standard of review under [Rule 56 of the Federal Rules of Civil Procedure](#) is well established. A party is entitled to judgment as a matter of law upon a showing that "there is no genuine issue as to any material fact." [Fed. R. Civ. P. 56\(c\)](#) [\*15]. The material facts are those identified by controlling law as essential elements of claims asserted by the parties. A genuine issue as to such facts exists if the evidence forecast is sufficient for a reasonable trier of fact to find for the nonmoving party. [Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 \(1986\)](#). No genuine issue of material fact exists if the nonmoving party fails to make a sufficient showing on an essential element of its case as to which it would have the burden of proof at trial. [Celotex Corp. v. Catrett, 477 U.S. 317, 322-23, 106 S. Ct. 2548, 91 L. Ed. 2d 265 \(1986\)](#). **HN2**[] In evaluating a forecast of evidence on summary judgment review, the court must view the facts and inferences reasonably to be drawn from them in the light most favorable to the nonmoving party. [Anderson, 477 U.S. at 255](#).

When the moving party has carried its burden, the nonmoving party must come forward with evidence showing more than some "metaphysical doubt" that genuine and material factual issues exist. [Matsushita Elec. Indus. Co. v. Zenith Radio Corp., 475 U.S. 574, 586, 106 S. Ct. 1348, 89 L. Ed. 2d 538 \(1986\)](#), cert. denied, 481 U.S. 1029, 107 S. Ct. 1955, 95 L. Ed. 2d 527 (1987). A mere scintilla of evidence [\*16] is insufficient to circumvent summary judgment. [Anderson, 477 U.S. at 252](#). Instead, the nonmoving party must convince the court that, upon the record taken as a whole, a rational trier of fact could find for the nonmoving party. [Id. at 248-49](#). Trial is unnecessary if "the facts are undisputed, or if disputed, the dispute is of no consequence to the dispositive question." [Mitchell v. Data General Corp., 12 F.3d 1310, 1315-16 \(4th Cir. 1993\)](#).

### **IV. Discussion**

#### **A. The Breach of Contract Claims**

Basic Medical moves for summary judgment on its breach of contract claim on the ground that NC Mutual's March 11th notice of termination constituted an anticipatory breach of the Marketing Agreement, citing [Pitts v. Broyhill, 88 N.C. App. 651, 364 S.E.2d 738 \(1988\)](#) and [Tillis v. Calvine Cotton Mills, Inc., 251 N.C. 359, 111 S.E.2d 606 \(1959\)](#). Basic Medical argues that NC Mutual's "interpolation" of the annual premium sales requirements into quarterly requirements was not supported by the "plain meaning" of the Marketing Agreement, and thus, that NC Mutual's

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<sup>4</sup>The parties disagree whether Miller attempted to contact Watts about the March 11th letter. Miller maintains that he attempted to call an NC Mutual representative, Art Davis, and Watts at least twice, leaving messages that were not returned. (Miller Aff. P 6; Miller Dep. (Def.) at 152, 188-89, 204; Miller Dep. Vol. II (Def.) at 28.) Watts maintains that he always returns his calls, and that if Miller had called him, he would have been informed of the call and returned it. (Watts Dep. Vol. II at 14.)

attempt to terminate the agreement pursuant [\*17] to these extra-contractual quarterly goals was an anticipatory breach.

In response, NC Mutual argues that (1) the elements of anticipatory breach have not been met;<sup>5</sup> (2) NC Mutual's interpolation of the annual premium goals into quarterly goals was a reasonable contract interpretation; (3) even if not reasonable, the interpolation into quarterly goals was at most an immaterial breach of the Marketing Agreement; (4) Basic Medical's breach of contract claim is barred by equitable estoppel; and (5) any breach of the Marketing Agreement by NC Mutual was excused by the doctrine of mutual mistake. The Court will address each of these arguments in turn.

[\*18] **HN3**[] Repudiation is a positive statement by one party to the other party which indicates that the party will not or cannot substantially perform its contractual duties. *Millis Constr. Co. v. Fairfield Sapphire Valley, Inc., 86 N.C. App. 506, 510, 358 S.E.2d 566, 569 (1987)*. A party to a contract repudiates his obligation under a contract when he expresses, by words or conduct, a "positive, distinct, unequivocal and absolute refusal to perform." *Messer v. Laurel Hill Assoc., 93 N.C. App. 439, 443, 378 S.E.2d 220, 223 (1989)*(quoting *Edwards v. Proctor, 173 N.C. 41, 91 S.E. 584 (1917)*); N.C. Pattern Jury Instr., Civil § 502.05 (2003). When a party repudiates its obligations under a contract before the time for performance under the contract, the repudiation becomes an anticipatory breach of the contract. *Id.*

Defendant NC Mutual argues that its March 11th notice of termination cannot be an anticipatory repudiation because it was not a "positive, distinct, unequivocal and absolute refusal to perform." See *Messer, 93 N.C. App. at 443, 378 S.E.2d at 223*. NC Mutual points out that its March 11th letter expressly conditioned [\*19] termination of the Marketing Agreement upon Basic Medical's ability or inability to make "appreciable progress" towards the 2002 premium sales requirement:

If your performance begins to approach targeted levels before June 1, 2002 nothing could make us happier than to rescind this letter of termination . . . If by the beginning of June we have had no appreciable progress toward the goal, we will stand on this notice at that time as an effective basis to terminate our relationship under the contract.

(Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. C.)

The Court finds that the "conditional" nature of the March 11th notice of termination does not shield it from constituting an anticipatory repudiation. The law in North Carolina is well-settled that "if a party to the contract states that he cannot perform *except on some condition which goes outside the terms of his contract* then the statement will constitute a repudiation." *Millis Constr. Co. v. Fairfield Sapphire Valley, Inc., 86 N.C. App. 506, 511, 358 S.E.2d 566, 569 (1987)*(emphasis added). In *Millis Constr. Co.*, the plaintiff was an independent contractor who was performing [\*20] framing work on residences on the defendant's land pursuant to a series of contracts. *Id. at 506, 358 S.E.2d at 567*. During the course of construction, the plaintiff informed the defendant that he was "belly up" and "busted," and that he did not have enough money to complete the job. *Id. at 507-08, 358 S.E.2d at 567*. The plaintiff then asked the defendant to release the retainage for one of the buildings before it was due under the contract. *Id. at 508, 358 S.E.2d at 567-68*. The Court of Appeals held that because the plaintiff stated that he would not perform except on a condition (release of retainage before it was due) that went outside the terms of the contract, the trial court erred in not instructing the jury on the issue of anticipatory repudiation. *Id. at 511, 358 S.E.2d at 569*.

In this case, the Court finds that NC Mutual's "interpolation" of the annual premium sales requirements into quarterly requirements was an unreasonable contract interpretation and was not supported by the plain language of the Marketing Agreement. The critical language of the Marketing Agreement provides as follows:

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<sup>5</sup> NC Mutual also argues that the March 11th letter was not an anticipatory breach because NC Mutual possessed the right under the Marketing Agreement to withdraw the Product from the market and terminate the Marketing Agreement at any time and in its sole discretion. NC Mutual asserts that it would have withdrawn the Product if Basic Medical had challenged NC Mutual's right to send the March 11th letter. This argument fails. The Court will not adjudicate this matter on the basis of what NC Mutual might have done differently if it had the wisdom of hindsight.

3.2 As consideration [\*21] for the fees being paid by NCM to BMCP hereinabove, BMCP shall provide to NCM at least the following minimum production amounts in the following *calendar years*: 2002, \$ 1,000,000; 2003, \$ 1,500,000; 2004, \$ 2,000,000; and 2005, \$ 2,500,000. After the year 2005, the minimum production target premium amounts shall be \$ 3,000,000 *per year*. However, the amount received in excess of the minimum production premium as hereinabove scheduled shall be credited cumulatively forward to the following years for purposes of crediting minimum annual premium amounts. Notwithstanding the above, the target premium amount in *any year* after 2001 must be \$ 1,000,000 or more.

(Defs.' Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. B § 3.2)(emphasis added). This language is clear and unambiguous - the premium sales requirements are based on "calendar years" - and nothing in this section, nor any other section of the Marketing Agreement, gave NC Mutual the right to "interpolate" these annual requirements into quarterly requirements. The Court finds that NC Mutual's interpretation of section 3.2 was unreasonable as a matter of law. See [Whirlpool Corp. v. Dailey Constr., Inc., 110 N.C. App. 468, 471, 429 S.E.2d 748, 751 \(1993\)](#) [\*22] ("When the language of a contract is plain and unambiguous then construction of the agreement is a matter of law for the court.") Because NC Mutual's interpolation of the annual sales goals into quarterly goals was unreasonable, it follows as a matter of law that NC Mutual did not have the right to demand reasonable assurances of performance from Basic Medical based on these contrived, extra-contractual sales requirements. Under the authority of [Millis Constr. Co.](#), NC Mutual's extra-contractual demands amounted to an anticipatory repudiation of the Marketing Agreement.

NC Mutual argues that *Millis Constr.* Co. does not provide authority for this Court to grant summary judgment to Basic Medical on its breach of contract claim because the Court of Appeals *at most* found that the plaintiff's statements made the issue of anticipatory repudiation a jury question. This is an overly narrow reading of *Millis Constr.* Co. First, the Court notes that the *Millis* court's holding was largely due to the procedural posture of the case - the court was merely asked to rule whether the trial court erred by failing to instruct the jury on the issue of anticipatory breach and was not [\*23] asked to decide whether the defendant had established a claim of anticipatory breach as a matter of law. Second, the plaintiff's statement, "that if [the defendant] would agree to release the retainge on building number 7 which was 99% complete [the plaintiff] would have enough money to pay labor," *at most implied* that the plaintiff would not perform unless he received the undue retainage. The plaintiff's statement was not an express refusal to perform except on an extra-contractual condition, and thus, the Court of Appeals properly left the issue for the jury to decide.

In contrast, in this case, the March 11th notice of termination unequivocally states that NC Mutual will terminate the Marketing Agreement if Basic Medical has not made "appreciable progress" towards the \$ 500,000 in premium sales required by June 1, 2002, see Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. C - a requirement which is clearly outside the terms of the Marketing Agreement. This places the March 11th notice of termination squarely within the doctrine of anticipatory repudiation. See [Pittsburgh-Des Moines Steel Co. v. Brookhaven Manor Water Co., 532 F.2d 572 \(7th Cir. 1976\)](#); [\*24] [Westinghouse Elec. Corp. v. CX Processing Labs., Inc., 523 F.2d 668 \(9th Cir. 1975\)](#); Restatement (2d) of Contracts § 250 cmt. b (1981); [Unif. Commercial Code § 2-610](#) cmt. 2 (2004); 4 A. Corbin, *Contracts* § 973 at 910 (1951).

NC Mutual nevertheless contends that even if the Court should find that NC Mutual breached the Marketing Agreement, as it has, the breach was immaterial, and thus, Basic Medical did not have the right to declare the Marketing Agreement at an end. This contention is without merit. The March 11th letter made it clear that NC Mutual expected Basic Medical's premium sales to "begin to approach targeted levels," i.e., \$ 500,000, by June 1, 2002, or NC Mutual would terminate the Marketing Agreement effective June 1, 2002. (Defs.' Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. C.) The evidence before the Court is that Basic Medical had sold virtually [HN4](#) [↑] no policies at the time of the March 11th letter. (Miller Dep. 167-68.) Thus, upon receiving this letter, Miller realized there was little chance of avoiding termination of the Marketing Agreement. (Miller Dep. (Def.) at [\*25] 192-93, 196-98.) In addition, Miller believed that it would be unethical and futile to continue to attempt to recruit agents while under the cloud of probable termination. See Miller Aff. P 6. Thus, the March 11th letter directly resulted in Basic Medical immediately ceasing all operations. The Court finds as a matter of law that NC Mutual's March 11th letter was a material breach of the Marketing Agreement.

NC Mutual contends that Basic Medical's breach of contract claim is barred by the doctrine of equitable estoppel. More specifically, NC Mutual claims that Basic Medical "refused to contact (and refused to permit its attorneys to contact)" NC Mutual after receipt of the March 11th letter until specific performance of the Marketing Agreement was no longer possible, knowing that NC Mutual would interpret Basic Medical's silence as an acquiescence to the terms and conditions of the March 11th letter, and then brought this lawsuit claiming millions of dollars in lost profits. (Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J. at 15)(emphasis in original).

NC Mutual's argument is meritless. [HN5](#)<sup>6</sup> "Equitable estoppel arises when a 'party by acts, representations, admissions, [\*26] or by silence . . . induces another to believe that certain facts exist, and such other person rightfully relies and acts upon that belief to his or her detriment.'" [State ex rel. Easley v. Rich Food Servs., Inc., 139 N.C. App. 691, 702, 535 S.E.2d 84, 91 \(2000\)](#)(citation omitted). Contrary to NC Mutual's contention, Miller testified on deposition that he attempted to contact both Art Davis and Chuck Watts on at least two occasions following receipt of the March 11th letter, leaving messages each time that were not returned. (Miller Aff. P 6; Miller Dep. (Def.) at 152, 188-89, 204; Miller Dep. Vol. II (Def.) at 28.) When he did not receive a response, Miller and his board of directors determined that any further attempts to resolve the problems between Basic Medical and NC Mutual would be futile. (Pl.'s Br. in Supp. of Mot. for Partial Summ. J., Ex. 25; Miller Dep. (Def.) at 192-93, 196-98.) In contrast, there is simply no evidence in the record of a plan or actions on the part of Basic Medical to deceive NC Mutual regarding its intentions following the March 11th letter. Basic Medical had no duty to respond to NC Mutual's anticipatory repudiation and material breach, [\*27] and NC Mutual cannot manufacture one out of the doctrine of equitable estoppel.

NC Mutual finally argues that if it did breach the Marketing Agreement, its breach was excused by the doctrine of mutual mistake, i.e., that Basic Medical mistakenly interpreted the March 11th letter as an absolute renunciation of the Marketing Agreement. Again, the Court finds no merit to NC Mutual's argument. It is clear from NC Mutual's own argument that the mistake alleged was not "mutual" but unilateral - according to NC Mutual's theory of the case, NC Mutual intended the March 11th letter to be a *conditional* notice of termination, and it was Basic Medical that misinterpreted the March 11th letter as an outright termination of the Marketing Agreement. The defense of mutual mistake fails as a matter of law.<sup>6</sup>

[\*28] Both parties have also moved for summary judgment on NC Mutual's counterclaim for breach of contract. NC Mutual bases its counterclaim on Basic Medical's failure to provide NC Mutual with reasonable assurances of performance and its "unreasonable" decision to cease all operations upon receipt of the March 11th letter. However, as the Court has discussed above, NC Mutual did not have the right to request reasonable assurances of performance on the basis of extra-contractual requirements. See [Millis Constr. Co., 86 N.C. App. at 511, 358 S.E.2d at 569](#). It follows as a matter of law that Basic Medical's response (or lack of response) to the March 11th letter was not a breach of the Marketing Agreement, and NC Mutual's counterclaim for breach of contract must be dismissed.

## B. The Unfair or Deceptive Trade Practices Claims

Basic Medical initially based its unfair or deceptive trade practices ("UDTP") claim on NC Mutual's alleged marketing of an insurance product (the "VMC policy") substantially similar to the Product at the approximate time that NC Mutual attempted to terminate the Marketing Agreement. (Compl. PP 27, 35; Miller Dep. (Def.) at 237.) In its brief [\*29] in support of its motion for summary judgment on Basic Medical's UDTP claim, NC Mutual proffered evidence that the VMC policy was intended for sale to educational institutions in the State of Florida, was never approved for sale by the Florida Department of Insurance, and was abandoned by NC Mutual nine months before

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<sup>6</sup> NC Mutual also argues that "insofar as BMCP contends that the Marketing Agreement limits or prohibits NCM from making a request for reasonable assurances as set forth in the March 11 letter, the Court should deem those parts of the Marketing Agreement . . . to be invalid for failure of the parties to reach a meeting of the minds, as the right to request reasonable assurances was an implied and understood material term of the agreement." (Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J. at 16.) The Court disagrees. The general right to request reasonable assurances is not challenged by Basic Medical. Rather, it is the "right" to request reasonable assurances based on "interpolated" quarterly sales requirements that is challenged, and the Court finds that this supposed "right" was not "an implied and understood material term of the agreement."

the March 11th letter was sent to Basic Medical. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Exs. F, G; Ex. N, James N.Parrish Dep. (Def.) at 163-65, 170-71.)

In its brief in opposition to NC Mutual's motion for summary judgment, Basic Medical shifted its argument on its UDTP claim to the rather bald assertion that NC Mutual concocted an elaborate, four-part plan to terminate the Marketing Agreement by: (1) eliminating Parrish as NC Mutual's representative for the Product; (2) causing Charles Welch<sup>7</sup> to abandon his commitment to be Basic Medical's North Carolina State Manager; (3) ignoring or failing to cooperate with Miller by, among other things, denying knowledge of Miller's commitment to Vol-State from [HN6](#); and (4) seizing the opportunity to terminate the Marketing Agreement while Miller was finishing up his work for Vol-State. [\*30]

At the outset, the Court notes that Basic Medical's argument is based almost entirely upon speculation and appears to be a fanciful attempt to resuscitate its lifeless UDTP claim in the face of compelling evidence that Basic Medical's theories about the VMC policy were unfounded. Second, even if NC Mutual was contemplating terminating the Marketing Agreement, the Court notes that NC Mutual possessed the right to terminate the Agreement on a variety of grounds (as did Basic Medical), and that there is nothing inherently unfair or deceptive about a strategic business decision to terminate an agreement with another party.

The only apparent "wrongful" conduct by NC Mutual on the record before the Court is its "interpolation" of the annual premium sales requirements into quarterly requirements. However, [HN7](#) under [\*31] North Carolina law, "substantial aggravating circumstances" must accompany this breach of contract in order to give rise to an unfair or deceptive trade practice. See [\*Charlotte Commer. Group, Inc. v. Fleet Nat'l Bank \(In re Charlotte Commer. Group, Inc.\), 2003 U.S. Dist. LEXIS 5392, No. 1:02CV00343, 2003 WL 1790882, at \\*3 \(M.D.N.C. Mar. 13, 2003\)\*](#)(unpublished opinion)(Bullock, J.) The Court finds no such circumstances present here. The Court finds that Basic Medical's UDTP claim must be dismissed.

Similarly, the Court finds that NC Mutual's UDTP counterclaim is subject to dismissal. NC Mutual essentially argues that Basic Medical's decision to litigate this matter rather than making any "meaningful effort" to resolve the issues raised by the March 11th notice of termination constitutes an unfair or deceptive trade practice. (Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J. at 18-19.)

NC Mutual's argument is foreclosed by the North Carolina Court of Appeals' decision in [\*Reichhold Chemicals, Inc. v. Goel, 146 N.C. App. 137, 555 S.E.2d 281 \(2001\)\*](#), disc. rev. denied, 356 N.C. 677, 577 S.E.2d 634 (2003). In *Reichhold Chemicals*, the employer filed a variety of claims against a former employee, [\*32] including a claim misappropriation of trade secrets. [\*Id. at 141-42, 555 S.E.2d at 284\*](#). To support its trade secrets claim, the employer obtained confidential documents from a competitor with whom the employee had a consulting agreement and filed a complaint with the Federal Bureau of Investigation ("FBI") regarding the alleged theft of its trade secrets. [\*Id. at 143, 555 S.E.2d at 285\*](#). The documents and FBI investigation revealed that the employer's belief that the employee had misappropriated its trade secrets was unfounded. *Id.* Nevertheless, the employer terminated the employee and filed a lawsuit against the employee and the competitor. [\*Id. at 144, 555 S.E.2d at 286\*](#). In response, the employee alleged numerous counterclaims, including a claim of unfair or deceptive trade practices. [\*Id. at 141, 555 S.E. 2d at 284\*](#). The employee argued that his former employer's actions in filing the lawsuit, obtaining the competitor's documents, and filing a complaint with the FBI constituted unfair or deceptive trade practices. [\*Id. at 156-57, 555 S.E. 2d at 293\*](#).

The *Reichhold Chemicals* court first held that [\*33] [HN8](#) the doctrines governing federal **antitrust law** announced in [\*Eastern R.R. Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127, 81 S. Ct. 523, 5 L. Ed. 2d 464 \(1961\)\*](#) and [\*Professional Real Estate Investors, Inc. v. Columbia Pictures Indus., Inc., 508 U.S. 49, 113 S. Ct. 1920, 123 L. Ed. 2d 611 \(1993\)\*](#) applied to the North Carolina Unfair or Deceptive Trade Practices Act, N. C. Gen. Stat. § 75.1-1. [\*146 N.C. App. at 156, 555 S.E.2d at 293\*](#). Under *Noerr* and *Professional Real Estate Investors*,

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<sup>7</sup> Charles Welch had been the Senior Vice President for Agency Operations at NC Mutual prior to accepting the position of North Carolina State Manager with Basic Medical in September, 2001. (Compl. P 20, Ex. B.)

a plaintiff may not be held liable under federal **antitrust law** for bringing an "objectively reasonable" lawsuit, regardless of the plaintiffs subjective intent in bringing the suit. Professional Real Estate Investors, 508 U.S. at 57, 113 S. Ct. at 1928, 123 L. Ed. 2d at 621. "A lawsuit is objectively reasonable if 'an objective litigant could conclude that the suit is reasonably calculated to elicit a favorable outcome.'" Reichhold Chemicals, 146 N.C. App. at 157, 555 S.E.2d at 293 (quoting Professional Real Estate Investors, 508 U.S. at 60, 113 S. Ct. at 1928, 123 L. Ed. 2d at 624). [\*34] Accordingly, the Court of Appeals held that even though the employer filed its lawsuit for "no legitimate purpose," the suit against the competitor was not "utterly baseless" and was therefore "objectively reasonable." 146 N.C. App. at 157, 555 S.E.2d at 293.

Applying Reichhold Chemicals to the case at bar, the Court finds without hesitation that Basic Medical's lawsuit is objectively reasonable, especially since the Court has found an actual breach of contract by Defendant NC Mutual. To the extent that NC Mutual argues that its UDTP claim is based not just on this lawsuit but on Basic Medical's entire "course of conduct" following receipt of the March 11th notice of termination, see Def.'s Br. in Opp'n to Pl.'s Mot. for Partial Summ. J. at 18-19, the Court notes that *Reichhold Chemicals* once again forecloses this argument:

[The employee] suggests that [the employer's] activities preceding the filing of its suit against [the competitor], including acquiring confidential [competitor] documents and filing a complaint with the FBI, constitute an unfair trade practice independent of the suit against [the competitor]. However, there is no indication [\*35] that [the employer] undertook those acts for any trade related purpose other than preparation for the suit against [the competitor]. We hold that those actions alone are insufficient to qualify as unfair trade practices under N.C.G.S. § 75-1.1

146 N.C. App. at 157, 555 S.E.2d at 293. Similarly, here, there is no indication that Basic Medical's actions following receipt of the March 11th notice of termination were for a "trade related purpose." Rather, it is apparent that Basic Medical was preparing for its lawsuit against NC Mutual. NC Mutual's counterclaim for unfair or deceptive trade practices must be dismissed.

#### C. The Abuse of Process Claim

In its third counterclaim against Basic Medical, NC Mutual once again argues that Basic Medical's decision to litigate this matter rather than to resolve the issues raised by the March 11th notice of termination constitutes an "abuse of process."

The Court finds this counterclaim to be baseless. HN9↑ To establish a claim of abuse of process, NC Mutual must show that (1) a proceeding was initiated against it by Basic Medical or used by Basic Medical to achieve an ulterior purpose; and (2) [\*36] once the proceeding was initiated, Basic Medical committed some willful act not proper in the regular prosecution of the proceeding. Semones v. Southern Bell Tel. & Tel. Co., 106 N.C. App. 334, 341, 416 S.E.2d 909, 913 (1992). Because NC Mutual has made no attempt to show a willful or improper act by Basic Medical subsequent to the filing of this action, NC Mutual's counterclaim for abuse of process must be dismissed. See Edwards v. Advo Sys., Inc., 93 N.C. App. 154, 376 S.E.2d 765 (1989)(summary judgment affirmed for defendant where plaintiff's allegations dealt only with defendant's motives in *filing* the suit, rather than any abuse of the judicial system *after* the institution of the lawsuit).

#### D. Loss of Profit Damages

NC Mutual moves for summary judgment on the issue of Basic Medical's damages on the grounds that Basic Medical's only claimed damages are lost profits, and that Basic Medical's proffered evidence to support these highly speculative damages is insufficient as a matter of law, citing Olivetti Corp. v. Ames Bus. Sys., Inc., 319 N.C. 534, 356 S.E.2d 578 (1987). Accordingly, NC Mutual urges the Court [\*37] to limit Basic Medical's recovery to nominal damages. Basic Medical responds that its three experts have sufficiently described its lost profit damages with "reasonable certainty," as required by North Carolina law.

After consideration of all of the relevant evidence, the Court concludes that Basic Medical's evidence of lost profits is too speculative to support a verdict and fails the "reasonable certainty" test as a matter of law. The starting point

in the Court's analysis is the [Olivetti](#) decision of the North Carolina Supreme Court. In *Olivetti*, [HN10](#)<sup>↑</sup> the Court declined to adopt the "new business rule," a *per se* rule which would preclude lost profit damages for a new business with no established history of profitability. [Id. at 546, 356 S.E.2d at 585](#). However, the Court recognized that "lost future profits are difficult for a new business to calculate and prove," and adopted the "well-established principle of law that proof of damages [of lost profits] must be made with reasonable certainty." [Id.](#) (citing [Weyerhaeuser Co. v. Godwin Bldg. Supply Co., Inc., 292 N.C. 557, 234 S.E.2d 605 \(1977\)](#)).

Basic Medical has produced three expert [\*38] reports in support of its claim for lost profits, none of which, either individually or cumulatively, meets the "reasonable certainty" standard. Plaintiff's first expert, Jay D. Wink, III, has been an insurance broker providing voluntary benefits and enrollment services to employers since 1988. (Pl.'s Br. in Opp'n to Def.'s Mot. for Summ. J. and Partial Summ. J., Ex. 29.) In his expert report, Wink opined that "Basic Medical Care was established to address a significant need in the market place" and that "Mr. Miller's previous experience enabled him to establish a sound sales strategy." [Id.](#) At most, this statement by Wink is a vague prediction that the Product might be profitable. However, Wink's opinion fails to address *how much* profit Basic Medical would have earned but for NC Mutual's breach, which is the critical damage issue in this case. In fact, Wink admitted that he lacked the ability to make any projections about what Basic Medical's actual sales would have been. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. R, Jay D. Wink, III Dep. at 110-15.) ("I have no intention of going out and swagging some numbers.")

Plaintiff's second expert fares [\*39] no better. Donald L. Larson is a Regional Sales Coordinator for AFLAC and has been with the company since December 1973. In his expert report, Larson opined as follows:

The Basic Medical Care Plus is a product that employers and their employees are asking for. I believe that a Basic Medical Care Plus sales person calling on the small business employer market as we did with the cancer insurance product in the middle and late nineteen-seventies could very conservatively establish the equivalent of twenty 15 employee new accounts in his/her first twelve months in the field. I believe that it would be realistic to project that each of those twenty new accounts would generate a minimum of \$ 10,000 in new annualized premium or \$ 200,000 in total new annualized premium.

15 employees X \$ 700.00 Annualized Premium = \$ 10,500 per new account

20 new accounts X \$ 10,500 = \$ 210,000

(Pl.'s Br. in Opp'n to Def.'s Mot. for Summ. J. and Partial Summ. J., Ex. 34)(emphasis added). The fundamental problem with Larson's opinion is that Larson relied on his experience with AFLAC 30 years ago to predict what Basic Medical would be able to achieve in 2002 and beyond. [\*40] [HN11](#)<sup>↑</sup> Under North Carolina caselaw, this is wholly insufficient to support a claim for lost profits. [McNamara v. Wilmington Mall Realty Corp., 121 N.C. App. 400, 409, 466 S.E.2d 324, 330 \(1996\)](#)(expert's testimony "too conjectural to support an award of lost profits" for small custom jewelry store where based on data from independent national jewelers); see also [Olivetti, 319 N.C. at 548-49, 356 S.E.2d at 587](#). Furthermore, even if valid, Larson's opinion presents only one piece of the overall puzzle - Larson has opined about how many policies one Basic Medical sales person could sell. Missing from his opinion is (1) how many agents Basic Medical could hire and retain at any given time; and (2) any attempt to tie the predicted profits to calendar years. Finally, Larson admitted in his deposition that his projections were a "layman's estimate," and not based on any scientific or market data. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. S, Don Larson Dep. at 43-47.)

Plaintiffs third expert, Christopher J. Ruhm, is the Jefferson-Pilot Excellence Professor of Economics at University of North Carolina at Greensboro. (Pl.'s Br. in [\*41] Opp'n to Def.'s Mot. for Summ. J. and Partial Summ. J., Ex. 31.) In his expert report, Ruhm provided damages calculations for Basic Medical based upon two different "scenarios" or sets of assumptions. According to Ruhm, Basic Medical's lost profits were \$ 3,873,673 under the first scenario and \$ 1,178,468 under the second scenario. [Id.](#)

The Court finds that Ruhm's report is insufficient to support Basic Medical's claim for lost profits. In his expert report, Ruhm states, "In forming my opinions, I have reviewed the Plaintiff's responses to the defendant's first set of

interrogatories and the additional information sent via electronic mail from [Defendant's counsel]." *Id.* First, the Court cannot evaluate the validity of Ruhm's opinions when one of the bases of his opinions is unidentified - the Court does not know what "additional information" Ruhm reviewed to form his opinions. Second, the other source on which Ruhm based his opinions was Basic Medical's own sales projections, which Miller admits were optimistic, unscientific estimates made at the time Basic Medical was formed. (Miller Dep. (Def.) at 136-38, 142-51.) [HN12](#)<sup>↑</sup> The North Carolina courts have not allowed claims for lost [\*42] profits where the expert's opinion is based solely on the claimant's own speculative business plan and not based on any independent research or data or any comparison to similar businesses. See [\*Old Well Water v. Collegiate Distrib., Inc., 2002 N.C. App. LEXIS 1939, No. COA01-981, 2002 WL 1315395 \(N.C. App. June 18, 2002\)\*](#) (unpublished opinion); [\*Iron Steamer, Ltd. v. Trinity Rest., Inc., 110 N.C. App. 843, 431 S.E.2d 767 \(1993\)\*](#). Furthermore, Ruhm admitted in his deposition that he could not have created sales projections of his own without first conducting comprehensive market research, which Basic Medical did not ask him to do. (Def.'s Br. in Supp. of Mot. for Summ. J. and for Partial Summ. J., Ex. T, Christopher John Ruhm Dep. at 26-36.)

Because the Court has found that Plaintiff Basic Medical is entitled to summary judgment on its breach of contract claim, but now finds that Plaintiff Basic Medical's proffered evidence in support of its claims for lost profits (the only form of damages it seeks) is insufficient as a matter of law, the Court concludes that Basic Medical's recovery in this case must be limited to nominal damages.<sup>8</sup> [\*Robbins v. C. W. Myers Trading Post, Inc., 251 N.C. 663, 666, 111 S.E.2d 884, 886-87 \(1960\)\*](#) [\*43] [HN13](#)<sup>↑</sup> ("Where plaintiff proves breach of contract he is entitled at least to nominal damages."); [\*Catoe v. Helms Constr. & Concrete Co., 91 N.C. App. 492, 496-97, 372 S.E.2d 331, 335 \(1988\)\*](#) ("When a *prima facie* case of breach of contract is made out, but there is no evidence upon which a jury could base a damage award, the injured party is still entitled to nominal damages for invasion of his legal rights."); [\*Cole v. Sorie, 41 N.C. App. 485, 490, 255 S.E.2d 271, 274 \(1979\)\*](#); [\*Gouger & Veno, Inc. v. Diamondhead Corp., 29 N.C. App. 366, 369, 224 S.E.2d 278, 280 \(1976\)\*](#).

#### [\*44] V. Conclusion

For the reasons stated above, **IT IS HEREBY ORDERED** that Plaintiff Basic Medical's motion for partial summary judgment (Pleading No. 25) be **GRANTED** on its claim of breach of contract, and that NC Mutual be ordered to pay Basic Medical nominal damages of \$ 1.00. **IT IS FURTHER ORDERED** that Basic Medical's motion for summary judgment (Pleading No. 25) on NC Mutual's counterclaims of breach of contract, unfair or deceptive trade practices and abuse of process be **GRANTED**, and that these counterclaims be dismissed with prejudice.

**IT IS FURTHER ORDERED** that Defendant NC Mutual's motion for partial summary judgment (Pleading No. 23) on its counterclaims for breach of contract and unfair or deceptive trade practices be **DENIED**. **IT IS FURTHER ORDERED** that NC Mutual's motion for summary judgment (Pleading No. 23) on Basic Medical's unfair or deceptive trade practices claim be **GRANTED**, and that this claim be dismissed with prejudice; and that NC Mutual's motion for summary judgment (Pleading No. 23) on Basic Medical's breach of contract claim be **DENIED**.

A separate judgment will be entered this day.

/s/ P. Trevor Sharp

United [\*45] States Magistrate Judge

Date: September 6, 2005

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<sup>8</sup> Because of the Court's holding limiting Basic Medical to nominal damages, the Court need not and does not reach NC Mutual's argument that Basic Medical failed to mitigate its damages. It is worth noting, however, that the evidence is uncontested that Basic Medical took no steps to mitigate damages, and its failure to mitigate would be a great obstacle to any substantial recovery by Basic Medical under any theory of lost profits.

**JUDGMENT**

For the reasons set forth in the Memorandum Opinion and Order filed contemporaneously with this Judgment,

**IT IS HEREBY ORDERED AND ADJUDGED** that Plaintiff Basic Medical Care Plus, Inc. be granted summary judgment on its breach of contract claim and recover from Defendant North Carolina Mutual Life Insurance Company nominal damages in the amount of \$ 1.00. **IT IS FURTHER ORDERED AND ADJUDGED** that all remaining claims and counterclaims in this matter be, and the same hereby are dismissed with prejudice. The costs of the action follow the judgment in favor of Basic Medical.

/s/ P. Trevor Sharp

United States Magistrate Judge

Date: September 6, 2005

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## Geneva Pharm. Tech. Corp. v. Barr Labs.

United States District Court for the Southern District of New York

September 6, 2005, Decided ; September 7, 2005, Filed

98 Civ. 861 (DLC), 99 Civ. 3607 (DLC)

**Reporter**

2005 U.S. Dist. LEXIS 19069 \*

GENEVA PHARMACEUTICALS TECHNOLOGY CORP. (as successor in interest to Invamed, Inc.), Plaintiff, -v- BARR LABORATORIES, INC., BRANTFORD CHEMICALS INC., BERNARD C. SHERMAN, APOTEX HOLDINGS INC., APOTEX INC., and SHERMAN DELAWARE, INC., Defendants. APOTHECON INC., Plaintiff, -v- BARR LABORATORIES, INC., BRANTFORD CHEMICALS INC., BERNARD C. SHERMAN, APOTEX HOLDINGS INC., APOTEX INC. and SHERMAN DELAWARE, INC., Defendants.

**Prior History:** [Geneva Pharm. Tech. Corp. v. Barr Labs., Inc., 386 F.3d 485, 2004 U.S. App. LEXIS 21586 \(2d Cir. N.Y., 2004\)](#)

## Core Terms

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warfarin, generic, sodium, relevant market, discovery, Plaintiffs', summary judgment, marketplace, brand, district court, sales, grant of summary judgment, parties, prices, clathrate, consumers, entrants, monopoly, tablets

## LexisNexis® Headnotes

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Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

### [HN1](#) [down arrow] Standards of Review, De Novo Review

An appellate court reviews a grant of summary judgment de novo to ensure the district court applied substantive **antitrust law** correctly. A grant of such relief is proper if there are no genuine issues of material fact and the moving party is entitled to judgment as a matter of law. Upon reviewing the record, the appellate court draws all inferences and resolve all ambiguities in favor of the non-moving party.

Civil Procedure > Appeals > Remands

### [HN2](#) [down arrow] Appeals, Remands

It is an unaccustomed task for the district court to determine the scope of the remand. The guide for the performance of that delicate task is the doctrine known as the mandate rule, which dictates a careful examination of both the remand order itself and the broader spirit of the remand. The United States Court of Appeals for the Second Circuit has described the mandate rule as follows: The mandate rule compels compliance on remand with the dictates of the superior court and forecloses relitigation of issues expressly or impliedly decided by the appellate court. Likewise, where an issue was ripe for review at the time of an initial appeal but was nonetheless foregone, the mandate rule generally prohibits the district court from reopening the issue on remand unless the mandate can reasonably be understood as permitting it to do so. To determine whether an issue remains open for reconsideration on remand, the trial court should look to both the specific dictates of the remand order as well as the broader spirit of the mandate.

Civil Procedure > Discovery & Disclosure > General Overview

### **HN3** Civil Procedure, Discovery & Disclosure

When material events have occurred since the last discovery period, justice requires that the parties have an opportunity to develop those events through discovery.

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > Sherman Act

### **HN4** Antitrust & Trade Law, Sherman Act

Cross-elasticity of demand exists if consumers would respond to a slight increase in the price of one product by switching to another product. Market performance subsequent to alleged attempt to monopolize is relevant to a claim under [§ 2 \(15 U.S.C.S. § 2\)](#) of the Sherman Antitrust Act, [15 U.S.C.S. § 1 et seq.](#)

Antitrust & Trade Law > Sherman Act > General Overview

### **HN5** Antitrust & Trade Law, Sherman Act

In the context of a claim under the Sherman Antitrust Act, [15 U.S.C.S. § 1 et seq.](#), the time period for analyzing the ability of a competitor to enter the marketplace is not tied to the date of a defendant's alleged unlawful conduct. Of course, some time may pass between the commencement of monopoly pricing and a firm's decision to enter. Estimating the time required for entry is itself very rough and should start with initial planning after one decides to enter. Potential entrants in a market must be considered in the relevant market analysis.

**Counsel:** [\*1] For Plaintiff Geneva Pharmaceuticals Technology Corp. (as successor in interest to Invamed, Inc.): Wayne A. Cross, Michael J. Gallagher, White & Case LLP, New York, New York; Frederick R. Dettmer, Law Office of Frederick R. Dettmer, Pelham, New York; David S. Preminger, Rosen, Preminger & Bloom, New York, New York.

For Plaintiff Apothecon, Inc.: Harry Frischer, Colin A. Underwood, Proskauer Rose LLP, New York, New York.

For Defendant Barr Laboratories, Inc.: Kurt L. Schultz, Jay L. Levine, John J. Tully, Jr., Gregory C. Vamos, Winston & Strawn LLP, Chicago, Illinois.

For Defendant Brantford Chemicals, Inc.: Michael J. Gaertner, David G. Greene, John F. Kloecker, Lord, Bissell & Brook LLP, Chicago, Illinois.

**Judges:** DENISE COTE, United States District Judge

**Opinion by:** DENISE COTE

## Opinion

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### OPINION AND ORDER

DENISE COTE, District Judge:

Defendants Barr Laboratories, Inc. ("Barr") and Brantford Chemicals Inc. ("Brantford") have moved to determine the scope of remand or, in the alternative, for relief from a judgment under Rule 60(b)(2), Fed. R. Civ. P., and for supplemental discovery and expert reports and to complete expert depositions. For the reasons stated on the record at a [\*2] conference on August 23, 2005 and for the reasons set forth below, the motion to determine the scope of the remand is granted. In the light of that determination, the discovery motions are also granted.

### BACKGROUND

This action was commenced on February 6, 1998, by the filing of a complaint by Geneva Pharmaceuticals Technology Corp., as successor to Invamed, Inc. ("Geneva") and Apothecon, Inc. ("Apothecon") (collectively, the "Plaintiffs") against Barr, Brantford, Bernard C. Sherman ("Sherman"), Apotex Holdings Inc., Apotex Inc. ("Apotex") and Sherman Delaware Inc. ("Sherman Delaware") (collectively, the "Defendants").

The complaint alleges violations of Sections 1 and 2 of the Sherman Antitrust Act, 15 U.S.C. §§ 1 and 2 (2000), Section 7 of the Clayton Act, 15 U.S.C. § 18 (2000), and state law relating to joint ventures, all arising out of the competition between manufacturers of generic warfarin sodium. After discovery, the Defendants moved for partial summary judgment, which was granted on May 10, 2002 (the "May 10 Opinion"). By its opinion of October 18, 2004, the Court of Appeals reversed the grant of summary judgment dismissing [\*3] the Sherman Act Sections 1 and 2 claims, affirmed the dismissal of the Clayton Act claim and reversed the ruling that Apothecon lacked standing to sue (the "October 18 Opinion"). The May 10 and October 18 Opinions describe the parties and the factual background of the litigation, and familiarity with them is assumed.

The definition of the relevant warfarin sodium tablet market has been at issue throughout these proceedings. Geneva and Apothecon alleged two relevant markets in their complaints: "generic warfarin sodium and/or branded and generic warfarin sodium." In their motion for summary judgment, the Defendants argued in part that the Plaintiffs could not carry their burden of proving a relevant market of "generic warfarin sodium" and that Barr could not possibly possess monopoly power in a relevant market of "branded and generic warfarin sodium." Plaintiffs opposed Defendants' motion for summary judgment, asserting that the definition of the relevant market raised disputed issues of fact.

The May 10 Opinion rejected Plaintiffs' generics-only market definition, holding in relevant part that "the relevant product market is the combined group of generic and the branded warfarin sodium, [\*4]" and concluding that Barr could not possibly hold monopoly power in this market. Accordingly, it dismissed Plaintiffs' Section 2 claims relating to the warfarin sodium market. Geneva Pharms. Tech. Corp. v. Barr Labs., Inc., 201 F. Supp. 2d 236, 271 (S.D.N.Y. 2002). The May 10 Opinion entered summary judgment against Plaintiffs on their other antitrust claims as well.

With respect to the relevant market definition, the Plaintiffs argued on appeal that "the District Court erred in disregarding the evidence and making a factual finding on relevant market that should have been reserved for the jury." In the October 18 Opinion, Geneva Pharms Tech. Corp. v. Barr Labs., Inc., 386 F.3d 485 (2d Cir. 2004), the Court of Appeals discussed the standard of review applied in summary judgment cases:

**HN1** [↑] We review a grant of summary judgment *de novo* to ensure the district court applied substantive antitrust law correctly. A grant of such relief is proper if there are no genuine issues of material fact and the

moving party is entitled to judgment as a matter of law. Upon reviewing the record, we draw all inferences and resolve all ambiguities in favor of the [\*5] non-moving party, here plaintiffs.

[Id. at 495](#) (citation omitted).

Before analyzing the evidence, the Court of Appeals made the following statement:

The district court ruled that the entire warfarin sodium market, including Coumadin, was the appropriate market. It had noted the chemical equivalence between Coumadin and generics, found that customers and vendors viewed the products as competing, and concluded that generics took market share from Coumadin. We have performed our own analysis of the *Brown Shoe* factors and we conclude to the contrary that in this case generics alone constitute the relevant market.

[Id. at 496](#). The Court of Appeals considered the evidence cited by Plaintiffs in support of their generics-only market definition and reviewed the Plaintiffs' evidence of Coumadin and Barr pricing, inelastic demand (i.e., consumer unwillingness to purchase generic warfarin sodium), different distribution chains, industry recognition and supply substitution. [Id. at 496-99](#). After reviewing that evidence, it concluded: "We therefore hold that the relevant market for our purposes is the market for generic [\*6] warfarin sodium tablets." [Id. at 500](#).

The Court of Appeals proceeded to review the other elements of the Section 2 claims regarding warfarin sodium tablets and concluded that there is a question of material fact regarding Barr's monopoly power, [id. at 501](#), and the willful acquisition or maintenance of monopoly power, [id. at 504-05](#). It then remanded the case as follows:

Accordingly, for the foregoing reasons, we (1) reverse the grant of summary judgment dismissing all plaintiffs' claims brought pursuant to the Sherman Act §§ 1 and 2; (2) affirm the dismissal of the Clayton Act claim; and (3) reverse the ruling that plaintiff Apothecon lacks standing to sue. The case is remanded to the district court for further proceedings consistent with this opinion.

[Id. at 514](#).

The Defendants filed a motion for clarification or, in the alternative, petition for partial rehearing to clarify what the Court of Appeals intended with its "holding that the relevant market for our purposes is the market for generic warfarin sodium tablets." [Id. at 500](#). Defendants asked the Court of Appeals to clarify its [\*7] decision because:

While the posture of the case, the evidence before the Court, and the Opinion itself strongly suggest that the definition of the relevant market is reserved for trial, it is unclear whether this Court meant to (1) remand this case for trial on the issue of market definition or (2) rule as a matter of law that the relevant market is limited to generic warfarin sodium tablets and does not include the brand, Coumadin.

The Court of Appeals denied the Defendants' motion without explanation or opinion on December 16, 2004.

On August 9, 2005, these cases were transferred to this Court. At a conference on August 23, the Court advised the parties that the Defendants' motion to determine the scope of the remand was granted, that the issue of the market definition would be submitted to a jury, and set a schedule for the completion of discovery and a trial date of June 12, 2006. This Opinion explains in greater detail the reasons for that ruling on the Defendants' motions.

## DISCUSSION

### *The Scope Of The Remand*

**HN2**  It is an unaccustomed task for the district court to determine the scope of the remand. The guide for the performance of this delicate task [\*8] is the doctrine known as the mandate rule, which dictates a careful examination of both the remand order itself and the "broader spirit" of the remand. The Second Circuit has described the mandate rule as follows:

The mandate rule compels compliance on remand with the dictates of the superior court and forecloses relitigation of issues expressly or *impliedly* decided by the appellate court. Likewise, where an issue was ripe for review at the time of an initial appeal but was nonetheless foregone, the mandate rule generally prohibits the district court from reopening the issue on remand unless the mandate can reasonably be understood as permitting it to do so.

To determine whether an issue remains open for reconsideration on remand, the trial court should look to both the specific dictates of the remand order as well as the broader spirit of the mandate.

[United States v. Ben Zvi, 242 F.3d 89, 95 \(2d Cir. 2001\)](#) (citation omitted) (emphasis in original). See also [Landell v. Sorrell, 382 F.3d 91, 136 n.25 \(2d Cir. 2004\)](#).

The task before the Court of Appeals was the propriety of the grant of summary judgment, construing all facts in [\*9] favor of the Plaintiffs. Given the procedural posture of the appeal, by necessity, the Court of Appeals decided only the question of whether the facts supported summary judgment for the Defendants. According to the Court of Appeals, they did not. The remand therefore must be read to include fact-finding as to the market definition. Any other conclusion would constitute a grant of summary judgment in the Plaintiffs' favor by the Court of Appeals on a hotly contested issue. Since Plaintiffs never sought summary judgment on this or any aspect of their claims, such a result would be at odds with the standards customarily applied on appeal and specifically enunciated in the October 18 Opinion.

When the Court of Appeals has chosen to grant summary judgment, it has been explicit in doing so. See, e.g., [Mut. Export Corp. v. Westpac Banking Corp., 983 F.2d 420, 424 \(2d Cir. 1993\)](#) ("Accordingly, we reverse the judgment of the district court, with directions to grant Westpac's motion for summary judgment."); [Vives v. City of New York, 393 F.3d 129, 133 \(2d Cir. 2004\)](#) ("The cause is remanded to the District Court with instructions to enter summary judgment in [\*10] favor of defendants . . . ."). There is no parallel explicit grant of summary judgment here.<sup>1</sup>

Reinforcing the conclusion that the issue of the market definition was remanded for trial is the repeated reference by the Court of Appeals to the standard of review it applied to the facts: "Upon reviewing the record, we draw all inferences and resolve all ambiguities in favor of the non-moving party, here plaintiffs." [Geneva, 386 F.3d at 495](#). The Court of Appeals acknowledged that it examined the evidence "with these standards in mind." *Id.* "These [\*11] standards," are the standards applied to determine if fact questions exist, not to resolve fact questions.

In the context of the task the Court of Appeals performed, that is, the reversal of a grant of summary judgment, its observations concerning the relevant market must be understood as recognition that the plaintiffs had sufficient evidence in the record to support a verdict, and therefore, to require a trial. This conclusion is reinforced by the acknowledgment of the Court of Appeals that key facts regarding market definition were in dispute. For example, the Court of Appeals cited the Plaintiffs' evidence that Barr allegedly dropped its prices when Geneva entered the market as evidence that supported a generics-only relevant market definition. [Id. at 497](#); see also [id. at 500](#). ("Barr's price was impacted much more by Geneva's entry than by Coumadin."). On the other hand, the Court of Appeals noted that direct evidence that Barr lowered prices in response to Geneva's entry was "at best ambiguous," [id. at 500](#), and "somewhat inconclusive," [id. at 509](#). Similarly, the Court of Appeals considered "supply substitution" [\*12] in analyzing the relevant market, [id. at 499](#), and "readily" dismissed the possibility that other generic manufacturers could enter the market because of "high barriers to entry resulting . . . from limited supply of clathrate." *Id.* Yet, when it actually surveyed the conflicting evidence regarding the availability of clathrate suppliers, the Court of Appeals ruled that there is "a factual dispute over the availability of clathrate." [Id. at 504](#); see also [id. at 502](#) (concluding that there was a factual dispute over whether ACIC/Brantford was the only supplier of available clathrate). Reading the Court of Appeal's analysis of relevant market in conjunction with its finding that key facts are

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<sup>1</sup> The cases cited by Plaintiffs highlight that the October 18 Opinion lacks any limiting instructions of the type included by the Appellate Court when it intends to restrict proceedings following remand. See [Ginett v. Computer Task Group, Inc., 11 F.3d 359, 360-61 \(2d Cir. 1993\)](#); [Ginett v. Computer Task Group, Inc., 962 F.2d 1085, 1101 \(2d Cir. 1992\)](#); [Day v. Morgenthau, 909 F.2d 75, 78 \(2d Cir. 1990\)](#).

"ambiguous," "inconclusive" and "disputed" leads ineluctably to the conclusion that the Court of Appeals sought to search for fact issues, not resolve them.

Based on the factors just discussed, the Defendants' motion to determine the scope of the remand is granted. Relying on both the specific dictates of the remand order and the broader spirit of the remand, it is abundantly clear that the Court of Appeals did not enter judgment in Plaintiffs' [\*13] favor on the issue of the market definition. The trial will include the determination of the relevant market.

#### *Additional Discovery*

In a related application, Defendants seek to reopen discovery to explore marketplace conditions and other relevant events from the intervening months since discovery was closed. Based on the evidence submitted by the Defendants it appears that [HN3](#)[] material events have occurred since the last discovery period, which justice requires that the parties have an opportunity to develop through discovery. Several of the legal issues to which these more recent events are relevant are described here.

The Defendants have submitted new market evidence in support of their motion that is highly relevant to an analysis of the structure of the warfarin sodium market and the willingness of consumers to choose the generic over the brand drug. The data in the record before the Court of Appeals reflected 68% of all warfarin sodium sales going to Coumadin and 32% to the generics. After looking at the data regarding generic market penetration created by the record on appeal, the Court of Appeals "concluded" that Coumadin customers "clearly do not perceive generics to [\*14] be a reasonable substitute for it." [Geneva, 386 F.3d at 497](#). It would appear that the appellate court also concluded that the perceived consumer unwillingness to switch was a "trend" that would continue. See [id. at 498](#).

The new data submitted on this motion shows virtually the opposite; 38% of warfarin sodium sales are of Coumadin while 62% are of generics. This new evidence strongly suggests that Coumadin customers have not remained loyal to Coumadin and are willing to switch to generic warfarin sodium, and that demand for the branded drug is not inelastic. Indeed, the new market data appears to indicate that the actual trend reflects a high willingness of consumers to switch. See [AD/SAT, Div. of Skylight, Inc. v. Associated Press, 181 F.3d 216, 227 \(2d Cir. 1999\)](#) [HN4](#)[] ("Cross-elasticity of demand exists if consumers would respond to a slight increase in the price of one product by switching to another product."). See also [Lektro-Vend Corp. v. Vendo Co., 660 F.2d 255, 270-71 \(7th Cir. 1982\)](#) (market performance subsequent to alleged attempt to monopolize is relevant to Section 2 claim); [Nifty Foods Corp. v. Great Atl. & Pac. Tea Co., 614 F.2d 832, 841 \(2d Cir. 1980\)](#) [\*15] (dismissing Section 2 claim based on market share evidence subsequent to alleged conduct).

The Defendants have also presented new, relevant evidence regarding the barriers to entry. When analyzing the relevant market, the Court of Appeals found that there was no possibility of supply substitution:

We can readily dismiss potential substitution from all entities other than DuPont. We find evidence of particularly high barriers to entry resulting both from limited supply of clathrate and from the regulatory requirements to sell generics. We find no evidence that other generic pharmaceutical manufacturers could quickly and easily have entered the warfarin market if generic warfarin prices were raised substantially above marginal cost.

[Geneva, 386 F.3d at 499](#). Taro had just entered the market at the time discovery was closed and had such a small share (3%) that it did not even rate a mention as an entrant to the marketplace.

The new market data shows that Taro has successfully penetrated the market, gaining 19% of overall warfarin sales and 31% of generic warfarin sales. USL Laboratories and Genpharm also have recently entered the marketplace.

The Plaintiffs [\*16] have urged that the entry of USL Laboratories in 2003 and Genpharm in 2004 "can be easily dismissed as irrelevant" because their entry occurred "five or more years after Plaintiffs' entry and Defendants' unlawful conduct which delayed Plaintiffs' entry." [HN5](#)[] The time period for analyzing the ability of a competitor to

enter the marketplace, however, is not tied to the date of a defendant's alleged unlawful conduct. "Of course, some time may pass between the commencement of monopoly pricing and a firm's decision to enter." Areeda & Hovenkamp, P 422b, at 77. "Estimating the time required for entry is itself very rough" and should start with "initial planning after one decides to enter." *Id.* Potential entrants in a market must be considered in the relevant market analysis. See [United States v. Falstaff Brewing Corp., 410 U.S. 526, 532-34, 35 L. Ed. 2d 475, 93 S. Ct. 1096 \(1973\)](#) (discussing the influence of potential entrants on existing competition in the relevant market). The entrance of USL Laboratories and Genpharm suggests that it may be appropriate to consider them as potential entrants prior to their actual entry date.

Furthermore, the Plaintiffs claim damages of up to \$ 190.8 [\*17] million, which would be trebled under the antitrust laws and, according to Plaintiffs, adjusted further for interest. The Plaintiffs base their damages calculation on lost warfarin sales from 1997 through 2010. Plaintiffs' expert reports previously were based on actual data through 1999 or 2000 and assumptions, projections, and hypotheses for subsequent years, which related to, *inter alia*, an assumed conversion rate of sales of the Coumadin brand to generics; assumed patterns of price increases of the Coumadin brand; assumed price and sales data at which Apothecon would sell its warfarin sodium product; and Apothecon's assumed success in the marketplace.

As discussed above, new companies have entered, the marketplace positions of competitors have changed, and new sales patterns have developed. In addition, Geneva has purchased Invamed and Apothecon's product rights to sell warfarin sodium. Invamed and Apothecon are out of the warfarin sodium business and the alleged Invamed/Apothecon joint venture (which is at the core of the damage calculations) has dissolved. BMS, the parent of Apothecon, has purchased the Coumadin brand. In addition, current IMS data shows that since July [\*18] 2003 Geneva apparently has stopped actively selling warfarin sodium and currently has essentially a 0% market share. Publicly available data does not explain why Geneva exited this market. To evaluate damages, the parties are entitled to discovery regarding each of these events so that any damages award can be based on the firmest possible factual record.

As a final example, the conduct and success of new entrants (as well as Taro) is relevant to causation. For example, Defendants should be entitled to investigate whether Plaintiffs' lack of success in the marketplace was due to their own marketing and pricing decisions, and not due to Defendant's alleged anticompetitive conduct.

As these examples demonstrate, there has been a significant alteration in the marketplace while this case has been proceeding through summary judgment practice, an appeal, and motion practice on remand. Fairness requires that the parties have an opportunity to explore the new environment through discovery so that any verdict that a jury returns reflects as closely as possible the realities of the marketplace.

## **CONCLUSION**

The trial on Plaintiffs' Section 2 claims should proceed on all issues, including [\*19] relevant market definition. Discovery has been reopened to allow the parties to gather evidence for the entire relevant period up to and including the present.

SO ORDERED:

Dated: New York, New York

September 6, 2005

DENISE COTE

United States District Judge



## Schermer v. State Farm Fire & Cas. Co.

Court of Appeals of Minnesota

September 6, 2005, Filed

A04-2054, A04-2088

**Reporter**

702 N.W.2d 898 \*; 2005 Minn. App. LEXIS 742 \*\*

Christopher P. Schermer, et al., on behalf of themselves and all other similarly situated, Appellants, vs. State Farm Fire and Casualty Company, et al., Respondents.

**Subsequent History:** Review granted by, Motion granted by [Schermer v. State Farm Fire & Cas. Co., 2005 Minn. LEXIS 798 \(Minn., Dec. 13, 2005\)](#)

Affirmed by [Schermer v. State Farm Fire & Cas. Co., 2006 Minn. LEXIS 627 \(Minn., Sept. 14, 2006\)](#)

**Prior History:** [\*\*1] Hennepin County; Hon. John Q. McShane, Judge. District Court File No. 02-20839.

**Disposition:** Affirmed.

## Core Terms

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Farm, filed rate doctrine, rates, insurer, electrical system, argues, district court, private cause of action, homeowners, dwelling, summary judgment, differential, discriminatory, regulation, actuarial, premium, Unfair, charging, losses, alleged violation, violations, Practices, surcharge, revised, consent order, noncatastrophic, classification, ranches

## LexisNexis® Headnotes

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Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

Insurance Law > ... > Property Insurance > Homeowners Insurance > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Insurance Law > Claim, Contract & Practice Issues > Premiums > Excess Premiums

Insurance Law > Claim, Contract & Practice Issues > Premiums > Refunds

Insurance Law > Industry Practices > Rate Regulation > General Overview

Insurance Law > Industry Practices > Unfair Business Practices > General Overview

## **[HN1](#)** [down arrow] **Unfair Business Practices, Claims Investigations & Practices**

Minnesota law requires every homeowner insurer doing business in Minnesota to file its rates and rate revisions with the Minnesota Department of Commerce (DOC), and no rate is effective until it has been filed. [Minn. Stat. § 70A.06, subd. 1](#) (2004). The DOC has the power to examine any insurer at any time and for any reason related to the enforcement of the insurance laws. [Minn. Stat. § 60A.031, subd. 1](#) (2004). The DOC may initiate enforcement proceedings to remedy a violation of the applicable statutes. [Minn. Stat. §§ 45.027, 60A.052, subd. 1](#) (2004). If, after a contested proceeding, the DOC determines that a rate violates Minnesota law, it shall order that the rate be discontinued and shall order the excess premium plus interest to be refunded to the policyholder from the date the proceeding was commenced. [Minn. Stat. § 70A.11, subd. 1](#) (2004). Further, if the DOC determines that an insurer has charged illegal or improper rates, engaged in any fraudulent or misleading conduct during the filing process, or engaged in any other unfair trade practice, the commissioner may seek administrative remedies, including the revocation of an insurer's license and penalties. [Minn. Stat. §§ 45.027, 60A.031, 60A.052](#) (2004).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

## **[HN2](#)** [down arrow] **Regulated Practices, Trade Practices & Unfair Competition**

Under the Unfair Claims Practices Act, no person shall engage in any trade practice which is defined in [Minn. Stat. §§ 72A.17 to 72A.32](#) as or determined pursuant to [Minn. Stat. §§ 72A.17 to 72A.32](#) to be an unfair method of competition or an unfair or deceptive act or practice in the business of insurance. [Minn. Stat. § 72A.19, subd. 1](#) (2004).

Governments > Local Governments > Charters

Insurance Law > ... > Property Insurance > Homeowners Insurance > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Governments > Local Governments > Home Rule

Insurance Law > Industry Practices > Rate Regulation > General Overview

Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

Insurance Law > ... > Property Insurance > Coverage > General Overview

## **[HN3](#)** [down arrow] **Local Governments, Charters**

See [Minn. Stat. § 72A.20, subd. 13](#) (2004).

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **HN4** Regulated Practices, Trade Practices & Unfair Competition

A private party does not have a cause of action against an insurer for a violation of *Minn. Stat. § 72A.20* (2004) of the Unfair Claims Practices Act.

Antitrust & Trade Law > Public Enforcement > State Civil Actions

Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

Torts > ... > Prospective Advantage > Intentional Interference > Elements

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

#### **HN5** Public Enforcement, State Civil Actions

The Unfair Claims Practices Act does not create any private cause of action, regardless of how the claims are styled.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Business & Corporate Compliance > ... > Industry Practices > Unfair Business Practices > Claims Investigations & Practices

Antitrust & Trade Law > Public Enforcement > State Civil Actions

#### **HN6** Regulated Practices, Trade Practices & Unfair Competition

A litigant cannot directly sue under *Minn. Stat. § 72A.20, subd. 13* (2004), or use an alleged violation of this statute to prove elements of a common law claim.

Insurance Law > Industry Practices > Rate Regulation > General Overview

#### **HN7** Industry Practices, Rate Regulation

The filed rate doctrine forbids a regulated entity from charging rates for its services other than those properly filed with the appropriate federal regulatory authority. The doctrine holds that any filed rate--a rate that has been approved by the governing regulatory agency--is per se reasonable and unassailable in judicial proceedings brought by ratepayers. The filed rate doctrine applies to regulation by state agencies as well as federal. An appellate court has recognized the filed rate doctrine.

## **Syllabus**

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1. A private party does not have a cause of action for a violation of the Unfair Claims Practices Act, *Minn. Stat.* § 72A.20, *subd.* 13 (2004).

2. The filed rate doctrine bars suit against a regulated insurance company when the suit is based on an allegation that rates filed with the regulatory agency violate state law.

**Counsel:** Lawrence R. King, T. Joseph Snodgrass, Shawn M. Raiter, Larson & King, LLP, St. Paul, Minnesota; and Charles N. Nauen, Robert K. Shelquist, Lockridge Grindal Nauen P.L.L.P., Minneapolis, Minnesota; and Charles S. Zimmerman, J. Gordon Rudd, David M. Cialkowski, Zimmerman Reed, P.L.L.P., Minneapolis, Minnesota; and

Rhett A. McSweeney, McSweeney & Fay, Minneapolis, Minnesota (for appellants).

Todd A. Noteboom, William L. Greene, Daniel Oberdorfer, Douglas R. Boettge, Monica L. Davies, Leonard, Street and Deinard, Professional Association, Minneapolis, Minnesota (for respondents).

Mike Hatch, Attorney General, Brian Dockendorf, Assistant Attorney General, St. Paul, Minnesota (for amicus State of Minnesota).

Sharon L. [\*\*2] Van Dyck, Schwebel, Goetz & Sieben, P.A., Minneapolis, Minnesota; and

Jeffrey D. Bores, Chestnut & Cambronne, P.A., Minneapolis, Minnesota (for amicus Minnesota Trial Lawyers Association).

**Judges:** Considered and decided by Peterson, Presiding Judge; Minge, Judge; and Parker, Judge.

**Opinion by:** Edward J. Parker

## Opinion

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[\*900] PARKER, Judge \*

In this class action suit, appellants challenge the district court's grant of summary judgment in favor of respondent, arguing that the district court erred by (1) rejecting appellants' argument that respondents violated *Minn. Stat.* § 72A.20, *subd.* 13 (2004) as a matter of law; (2) holding that no private right of action exists under *Minn. Stat.* § 72A.20, *subd.* 13 (2004); and (3) holding that the filed rate doctrine bars appellants' claims. Because no private right of action exists under *Minn. Stat.* § 72A.20 , *subd.* 13 [\*\*3] (2004), and because the filed rate doctrine bars appellants' claims, we affirm. Therefore, we need not address appellants' argument that respondents violated *Minn. Stat.* § 72A.20, *subd.* 13 (2004), as a matter of law.

## FACTS

On May 8, 1997, respondent State Farm Fire and Casualty Company and State Farm General Insurance Company (State Farm) filed an initial version of a "Utilities Rating Plan" (URP) with the Department of Commerce (DOC) for homeowners and farm insurance policies. The URP had an effective date of June 15, 1997. It based a rate differential on the age of the oldest of the electrical, plumbing, and heating/cooling system. On May 22, 1997, the DOC notified State Farm that its filing had been reviewed and had to be amended to comply with *Minn. Stat.* § 72A.20, *subd.* 13. Pending that amendment, the filing was held in suspense. On June 5, 1997, State Farm submitted a revised URP. Under this revision, homeowners would be placed in different rate categories based on the age of the electrical system only. On June 10, 1997, the DOC informed State Farm that the URP required

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\* Retired judge of the Minnesota Court of Appeals, serving by appointment pursuant to [\*Minn. Const. art. VI, § 10.\*](#)

further amendment. Pending that amendment, **[\*\*4]** the URP continued to be held in suspense. On June 27, 1997, State Farm submitted a further revision to the URP in response to this **[\*901]** request. On July 18, 1997, the DOC again informed State Farm that further amendments were required to the URP and, pending those amendments, the filing would continue to be held in suspense. On July 23, 1997, the DOC accepted the URP for use effective August 1, 1997.

The accepted URP placed insured homeowners in different rating categories based on the age of the electrical system. A home with a new system would be eligible for a discount from the base premium; a home with an older system would be subject to an additional charge over the base premium. State Farm used the age of the home as a surrogate for the age of the home's electrical system as part of the development of a rating plan that assigned rates based on the age of the homeowner's electrical system. At all times during this process, State Farm relied on its original actuarial exhibit that utilized all noncatastrophic losses (not just those related to electrical systems) as its support for the URP. Approximately one year later, in September 1998, State Farm filed a modified URP with the DOC. **[\*\*5]** Under the revised URP, policyholders could more easily avoid the surcharge by making updates to their electrical system. The September 1998 filing also combined the three rating categories associated with the oldest electrical systems into a single 40-plus year category subject to a six-percent premium.

In January 2001, a private citizen filed a complaint with the DOC about State Farm's URP rating classification. In response to this complaint, the DOC began an investigation. The investigation took approximately 19 months and was led by Martin Fleischhacker. Fleischhacker reviewed the 1997 actuarial data that was supplied in support of the URP and found that the URP was based on the age of the primary structure, not the age of the electrical system. He also found that it did not include information demonstrating the risk of loss due to the age of the electrical system. He believed that when an insurer places homeowners in different rating categories based upon the age of a utility system, such as an electrical system, any differential in rates must be limited to differential in losses caused by or related to the age of that particular system. It was clear that the actuarial exhibits **[\*\*6]** submitted by State Farm in 1997 indicated that the differentials in URP charges and discounts had been calculated using all noncatastrophic losses, not just those caused by aging electrical systems. Fleischhacker concluded that the URP violated *Minn. Stat. § 72A.20, subd. 13*.

State Farm disagreed with Fleischhacker's interpretation of the statute. In October 2002, Fleischhacker sent State Farm a letter attaching a "DRAFT: CEASE AND DESIST ORDER AND NOTICE OF RIGHT TO HEARING." The letter alleged that State Farm did not track and had no loss data to show that the age of the structure's electrical system affects the risk of loss. It alleged that State Farm tracked the age of the insured's dwelling and that its loss data were correlated with the age of the dwelling. Finally, it concluded that the URP was based on the age of the primary structure, which is prohibited by *Minn. Stat. § 72A.20, subd. 13(b)*.

In December 2002, the DOC entered into a settlement with State Farm which was effectuated by a consent order. The order set forth the allegations of wrongdoing. It noted that State Farm denied those allegations. State Farm acknowledged **[\*\*7]** that it had been advised of its right to a hearing and to appeal from any adverse determination after a hearing but expressly waived those rights. The consent order contained the following: "Both the Commissioner and Respondent agree that this Order represents an informal settlement **[\*902]** and that there has been no hearing, findings of fact, or conclusions of law with respect to the allegations of the Commissioner." Under the terms of the consent order, State Farm agreed to discontinue the surcharge portion of the URP for one year while continuing to offer discounts. It retained the right to seek approval of the rates thereafter. It also agreed to reimburse the department \$ 75,000 for its investigative costs.

Appellants Christopher Schermer, John Smith, Marjorie Smith, and Reverend Albert Gallmon, on behalf of themselves and all others similarly situated (the class), filed their first class action on December 6, 2002, within days of the announcement of the consent order. The class states that this lawsuit was "filed to force State Farm to pay the Class back for State Farm's violation of state law." The class sought a refund of all surcharges collected by State Farm from 1997-2002 under **[\*\*8]** the URP. The surcharges totaled nearly \$ 20,000,000. Due to procedural matters and court rulings, the operative complaint is the class's third amended class action complaint. The class alleged the following eight counts in this complaint:

Count 1: Rescission of Unlawful Contract Terms

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Count 2: Breach of Contract and Duty of Good Faith and Fair Dealing

Count 3: Violation of Prevention of Consumer Fraud Act [Minn. Stat. § 325F.69, subd. 1](#) (as to the public)

Count 4: Violation of Prevention of Consumer Fraud Act [Minn. Stat. § 325F.69, subd. 1](#) (as to the DOC and the Commissioner of Commerce)

Count 5: Unreasonable Restraint on Trade or Commerce in Violation of Minnesota [Antitrust Law Minn. Stat. § 325D.53, subd. 2\(1\) to \(4\)](#) and [§ 325D.03, subd. \(1\)\(1\)\(a\)](#) Count 6: Violation of the Act Against Unfair

Discrimination and Competition [Minn. Stat. § 325D.03](#) and [§ 325D.072](#) Count 7: Fraud by Nondisclosure

Count 8: Filed Rate Doctrine

Each count in the complaint was based on State Farm charging an allegedly improper rate, a rate that [\[\\*\\*9\]](#) was approved by the Commissioner of Commerce in 1997 and then subject to a consent order in 2002. In its third amended complaint, the class summarized their claim in a section entitled "Nature of Action":

This is a class action against Defendants State Farm Fire and Casualty Company and State Farm General Insurance Company (referred to collectively as "STATE FARM"), for redlining in Minnesota *by dramatically charging higher premiums for homeowners and farm/ranch insurance for older homes, farms, ranches, buildings and other structures without actuarial support.* STATE FARM is a homeowners and farm/ranch insurer who, under the moniker "Utilities Rating Plan" ("URP"), has systematically charged unfair and discriminatory premiums to Minnesotans living in older homes, farms and ranches to subsidize deep premium discounts for consumers living in new homes, farms and ranches. STATE FARM's URP was a transparent effort to redline and discriminate. STATE FARM's misconduct was and is in violation of state law.

(Emphasis added.)

In 2004, State Farm submitted a rate filing to the DOC in which it sought approval of the same URP filed and approved by the DOC in 1997 and 1998, [\[\\*\\*10\]](#) which is the same URP at issue in this litigation. As it did in 1997, State Farm used age-of-home data as a surrogate for the age of the electrical system. It also provided its actuarial support for the rate [\[\\*903\]](#) differential based on all noncatastrophic losses. In its review, the DOC considered the actuarial data filed in support of the URP in light of the criticisms raised by Fleischhacker in 2002. There were differences of opinion among DOC staff members.

On April 9, 2004, the DOC approved State Farm's filing. In its approval, the DOC accepted the use of the age of the dwelling as a surrogate for the age of the utilities as well as the use of all noncatastrophic losses as actuarial support for the rate differential. According to one staff member of the department, the approval of State Farm's URP in 2004 reflected a return to the position of [Minn. Stat. § 72A.20, subd. 13](#), that the DOC had followed until 2001.

Both parties moved the district court for summary judgment. On September 3, 2004, the district court denied the class's motion for partial summary judgment. The class sought summary judgment on the ground that as a matter of law State Farm's 1997-1998 URP [\[\\*\\*11\]](#) violates [Minn. Stat. § 72A.20, subd. 13](#), because (1) the URP differential is based solely on the age of dwelling; and (2) the statute requires URP rate differentials to be calculated based on losses caused by the age of a home's electrical system, not all noncatastrophic losses. The district court held that there is a genuine issue of material fact with regard to the sole use of age of dwelling. But in response to the class's motion, the district court agreed with State Farm that because the class's claims are predicated on an alleged violation of [Minn. Stat. § 72A.20, subd. 13](#), summary judgment in favor of State Farm is appropriate because there is no private cause of action for a violation of [Minn. Stat. § 72A.20, subd. 13](#), pursuant to [Morris v. Am. Family Mut. Ins. Co., 386 N.W.2d 233 \(Minn. 1986\)](#). On this same date, the district court also granted State Farm's motion for summary judgment under the "filed rate doctrine." This appeal followed.

## ISSUES

I. Does a private right of action exist under the Unfair Claims Practices Act, *Minn. Stat. § 72A.20, subd. 13* [\*\*12] (2004)?

II. Does the filed rate doctrine bar the class's claims?

## ANALYSIS

On appeal from summary judgment, this court determines whether there are any genuine issues of material fact and whether the trial court erred in its application of the law. *State by Cooper v. French*, 460 N.W.2d 2, 4 (Minn. 1990).

### I.

**HN1**[] Minnesota law requires every homeowner insurer doing business in Minnesota to file its rates and rate revisions with the DOC, and no rate is effective until it has been filed. *Minn. Stat. § 70A.06, subd. 1* (2004). The DOC has the power to examine any insurer "at any time and for any reason related to the enforcement of the insurance laws." *Minn. Stat. § 60A.031, subd. 1* (2004). The DOC may initiate enforcement proceedings to remedy a violation of the applicable statutes. *Minn. Stat. §§ 45.027, 60A.052, subd. 1* (2004). If, after a contested proceeding, the DOC determines that a rate violates Minnesota law, it shall order that the rate be discontinued and "shall order the excess premium plus interest . . . to be refunded to the policyholder" from [\*\*13] the date the proceeding was commenced. *Minn. Stat. § 70A.11, subd. 1* (2004). Further, if the DOC determines that an insurer has charged illegal or improper rates, engaged in any fraudulent or misleading conduct during the filing process, or engaged in any other unfair [\*904] trade practice, the commissioner may seek administrative remedies, including the revocation of an insurer's license and penalties. *Minn. Stat. §§ 45.027, 60A.031, 60A.052* (2004).

**HN2**[] Under the Unfair Claims Practices Act (UCPA), no person shall engage in this state in any trade practice which is defined in sections *72A.17 to 72A.32* as or determined pursuant to *sections 72A.17 to 72A.32* to be an unfair method of competition or an unfair or deceptive act or practice in the business of insurance. *Minn. Stat. § 72A.19, subd. 1* (2004). Subdivision 13 of section 72A.20, entitled "Refusal to renew," prohibits the following trade practice:

**HN3**[] Refusing to renew, declining to offer or write, or charging differential rates for an equivalent amount of homeowner's insurance coverage, as defined by section [\*\*14] 65A.27, for property located in a town or statutory or home rule charter city, in which the insurer offers to sell or writes homeowner's insurance, solely because:

....

(b) of the age of the primary structure sought to be insured.

*Minn. Stat. § 72A.20, subd. 13(b)* (2004). Subdivision 13 also contains a "safe harbor provision" stating:

This subdivision shall not prohibit the insurer from applying underwriting or rating standards which the insurer applies generally in all other locations in the state and which are not specifically prohibited by clauses (a) to (d). . . . Clause (b) shall not prohibit the use of rating standards based upon the age of the insured structure's plumbing, electrical, heating or cooling system or other part of the structure, the age of which affects the risk of loss.

The class argues that (1) it did not assert a private cause of action under *Minn. Stat. § 72A.20, subd. 13*, but instead requested that the district court rescind the surcharge terms of its respective contracts because these terms violated this statute; (2) the common law recognizes this distinction and affords the right [\*\*15] to collect for discriminatory rate charges that violate a regulatory scheme; and (3) the legislature expressly intended to allow suits relating to subdivision 13 through the exception-to-immunity provision in *Minn. Stat. § 65A.29, subd. 6* (2004).

State Farm argues that the class's claims fail as a matter of law because the Minnesota Supreme Court in [Morris v. Am. Family Mut. Ins. Co., 386 N.W.2d 233 \(Minn. 1986\)](#), held that there is no private cause of action for claims premised on an alleged violation of *Minn. Stat. § 72A.20, subd. 13*.

The court in *Morris* held that [HN4](#) a private party does not have a cause of action against an insurer for a violation of the UCPA, *Minn. Stat. § 72A.20*. [Morris, 386 N.W.2d at 238](#). In *Morris*, the first-party insured plaintiff sued her insurer for basic economic loss no-fault benefits arising out of an auto accident. [Id. at 233, 237 n.7](#). The plaintiff sought to amend her complaint to add a count alleging that the insurer violated the UCPA. [Id. at 233](#). The supreme court reasoned in *Morris* that the "comprehensive [\[\\*\\*16\]](#) scheme of administrative enforcement" under the UCPA is "more appropriate to investigating and regulating an insurer's general business practices." [Id. at 237](#); see also [LaBarre v. Credit Acceptance Corp., 175 F.3d 640, 643 \(8th Cir. 1999\)](#) ("Minnesota law permits only administrative recourse for violations of § 72A.20 and . . . does not provide a private cause of action for violations of this provision.").

[\[\\*905\]](#) The class's claims were predicated on an alleged violation of *Minn. Stat. § 72A.20, subd. 13*. The class claimed that State Farm's alleged breaches of contract violated this statute. Thus, the class sought to bring a private cause of action under the UCPA, which is barred by [Morris](#).

Moreover, this court has rejected a plaintiff's attempt to use an alleged violation of the UCPA as an element of the plaintiff's common law claim for tortious interference with prospective relations. See [Glass Serv. Co. v. State Farm Mut. Auto. Ins. Co., 530 N.W.2d 867 \(Minn. App. 1995\)](#), review denied (Minn. May 2, 1995). Relying on *Morris*, this court in *Glass Serv.* reiterated that [HN5](#) the UCPA does not create [\[\\*\\*17\]](#) any "private cause of action," regardless of how the claims are styled. [Id. at 872](#); cf. [Olson v. Moorhead Country Club, 568 N.W.2d 871, 873 \(Minn. App. 1997\)](#) (relying on *Morris* and *Glass Serv.* to hold that an employee did not have a private cause of action for conversion where his only alleged right arose under a statute that did not provide for a private cause of action), review denied (Minn. Oct. 31, 1997); see also [Elder v. Allstate Ins. Co., 341 F. Supp. 2d 1095, 1100-02 \(D. Minn. 2004\)](#) (citing *Morris* and the absence of a private cause of action under the UCPA to hold that a common law claim for negligence per se cannot be based on an insurer's alleged violation of the UCPA). Thus, the law is settled that [HN6](#) a litigant cannot directly sue under *Minn. Stat. § 72A.20, subd. 13*, or use an alleged violation of this statute to prove elements of a common law claim.

Finally, the class argues that this court must recognize that the legislature expressly intended to allow litigation concerning violations of subdivision 13. The class cites [Minn. Stat. § 65A.29, subd. 6](#), entitled [\[\\*\\*18\]](#) "Immunity of Insurer or commissioner," which provides:

There shall be no liability on the part of and no cause of action of any nature shall arise against the commissioner or against any insurer, its authorized representative, its agents, its employees or any firm, person or corporation furnishing to the insured information as to reasons for declination, nonrenewal, or cancellation, for any statement made by them in any written notice of declination, nonrenewal or cancellation, for the providing of information relating thereto, or for statements made or evidence submitted at any hearings or investigations conducted in connection therewith. *This subdivision shall not apply to any action or proceeding arising under section 72A.20.*

(Emphasis added.) According to the class, "by declaring an exception, [\[section 65A.29\]](#) permits litigation concerning violations of § 72A.20, subd. 13."

We reject the class's argument that this statute authorizes it to bring a suit against State Farm. While State Farm is not "immune" from liability under *Minn. Stat. § 72A.20, subd. 13*, because the DOC may bring an action against State Farm, the class may not [\[\\*\\*19\]](#) bring a private cause of action against State Farm.

Next, the class argues that the district court erred in granting summary judgment because the "filed rate" doctrine does not apply to bar its claims.

In *Keogh v. Chicago & Nw. Ry. Co.*, 260 U.S. 156, 43 S. Ct. 47, 67 L. Ed. 183 (1922), Justice Brandeis set forth what has come to be known as "the filed rate doctrine." In *Keogh*, the plaintiff alleged that the defendant carrier conspired to fix rates for transporting freight, and that this conspiracy violated the Sherman Act. *Id. at 160, 43 S. Ct. at 48*. The plaintiff alleged that [\*906] because he was forced to pay higher rates than he would have absent the conspiracy, he suffered damages to the extent of that difference in rates. *Id.* The Supreme Court dismissed the plaintiff's claim, holding that where the defendant charged a rate that had been filed with the Interstate Commerce Commission, "the rates were reasonable and non-discriminatory." *Id. at 161, 43 S. Ct. at 49*.

Thus, **HNT** [↑] the filed rate doctrine forbids "a regulated entity [from charging] rates for its services other than those properly filed with the appropriate [\*\*20] federal regulatory authority." *Ark. La. Gas Co. v. Hall*, 453 U.S. 571, 577, 101 S. Ct. 2925, 2930, 69 L. Ed. 2d 856 (1981). The doctrine holds that any filed rate--a rate that has been approved by the governing regulatory agency--"is per se reasonable and unassailable in judicial proceedings brought by ratepayers." *Wegoland Ltd. v. NYNEX Corp.*, 27 F.3d 17, 18 (2d Cir. 1994). The filed rate doctrine applies to regulation by state agencies as well as federal. *H.J. Inc. v. Nw. Bell Tel. Co.*, 954 F.2d 485, 494 (8th Cir. 1992) (applying filed rate doctrine to Minnesota phone rates). This court has recognized the filed rate doctrine. See, e.g., *G & T Trucking Co. v. GFI Am., Inc.*, 535 N.W.2d 658, 660-61 (Minn. App. 1995) (noting that the filed rate doctrine requires a regulated entity to prove its filed rate).

The district court held that the filed rate doctrine bars the class's claims and relied on the *Wegoland* decision. In *Wegoland*, the plaintiff class alleged that two telephone companies gave regulatory agencies and consumers misleading financial information to support the inflated rates they requested. [\*21] *Wegoland, Ltd. v. NYNEX Corp.*, 806 F. Supp. 1112, 1113 (S.D.N.Y. 1992), aff'd, 27 F.3d 17 (2d Cir. 1994). The plaintiffs alleged that companies purchased products at inflated prices, then used those prices to justify inflated rates which resulted in high profits. *Id.* The Second Circuit affirmed the district court's holding that the filed rate doctrine barred the plaintiff's claims and that no fraud exception to the doctrine exists. *Wegoland*, 27 F.3d at 21-22. The district court found that the facts in *Wegoland* are "exceedingly similar" to this case, in which the class alleges that State Farm gave the DOC misleading actuarial information in support of its surcharge. We affirm the district court's holding that the filed rate doctrine bars the class's claims.

The class argues that (1) the facts of this case do not warrant adoption of the filed rate doctrine; (2) the filed rate doctrine does not apply to insurance; (3) the filed rate doctrine does not apply to discriminatory insurance practices; (4) the filed rate doctrine does not apply because it conflicts with Minnesota common law; and (5) the filed rate doctrine cannot apply [\*\*22] to the class's rental dwelling policy claims. State Farm argues that the filed rate doctrine applies in this case and that the exceptions the class cites are inapplicable. We address each of the claims.

The class first argues that the facts of this case do not warrant adoption of the filed rate doctrine because "while initially created to protect consumers, the filed rate doctrine has been used in recent times to victimize consumers." But here, applying the filed rate doctrine comports with the policies underlying the doctrine. Application of the filed rate doctrine (1) prevents the judiciary from "reconstituting the whole rate structure" of an industry; (2) avoids retroactive relief that would lead to discrimination in rates such that a victorious plaintiff would end up paying less than similarly situated nonsuing customers; and (3) avoids "undermining the congressional scheme of uniform rate regulation." *Wegoland*, 27 F.3d [\*907] at 19 (quoting *Keogh*, 260 U.S. at 163-64, 43 S. Ct. at 49-50; *Ark. La. Gas.*, 453 U.S. at 579, 101 S. Ct. at 2931). Additionally, the filed rate doctrine preserves the regulatory agency's authority to determine [\*\*23] the reasonableness of an entity's filed rates. *Id. at 21*. We agree with the *Wegoland* court that "as compared with the expertise of regulating agencies, courts do not approach the same level of institutional competence to ascertain reasonable rates. . . . Courts are simply ill-suited to systematically second guess the regulators' decisions and overlay their own resolution." *Id.*

Here, State Farm complied with Minnesota law by filing its rates with the DOC and thus should not now be subject to retroactive rate revisions when it satisfied the regulatory agency--the DOC. Furthermore, it was only after the DOC completed its review and required changes to comply with the statute at issue that the DOC accepted the URP for use in Minnesota. Allowing the class to challenge retroactively the reasonableness of the DOC-approved URP would undermine Minnesota's statutory process.

Next, the class argues that the competitive and deregulated nature of the private insurance market and the absence of exclusive jurisdiction of the DOC do not support applying the filed rate doctrine in Minnesota. But the class lacks authority for its position that the filed rate doctrine is premised upon the [\*\*24] exclusive jurisdiction of regulators. Our decision is consistent with other courts that have applied the filed rate doctrine to the insurance industry. See *Kirksey v. Am. Bankers Ins. Co., 114 F. Supp. 2d 526, 529-30 (S.D. Miss. 2000)*; *Allen v. State Farm Fire & Cas. Co., 59 F. Supp. 2d 1217, 1228-29 (S.D. Ala. 1999)*; *Korte v. Allstate Ins. Co., 48 F. Supp. 2d 647, 650-52 (E.D. Tex. 1999)*; *Morales v. Attorneys' Title Ins. Fund, Inc., 983 F. Supp. 1418, 1426-29 (S.D. Fla. 1997)*; *Uniforce Temp. Pers., Inc. v. Nat'l Council on Comp. Ins., Inc., 892 F. Supp. 1503, 1511-12, 1512 n.11 (S.D. Fla. 1995)*, aff'd, 87 F.3d 1296 (11th Cir. 1996); *Richardson v. Standard Guar. Ins. Co., 371 N.J. Super. 449, 853 A.2d 955, 962-64 (N.J. Super. Ct. App. Div. 2004)*; *Horwitz v. Bankers Life & Cas. Co., 319 Ill. App. 3d 390, 745 N.E.2d 591, 604-05, 253 Ill. Dec. 468 (Ill. App. Ct. 2001)*; *Am. Bankers' Ins. Co. v. Wells, 819 So. 2d 1196, 1204 (Miss. 2001)*; *N.C. Steel, Inc. v. Nat'l Council on Comp. Ins., 347 N.C. 627, 496 S.E.2d 369, 372 (N.C. 1998)*; [\*\*25] *Byan v. Prudential Ins. Co., 242 A.D.2d 456, 662 N.Y.S.2d 44, 45 (N.Y. App. Div. 1997)*; *Prentice v. Title Ins. Co., 176 Wis. 2d 714, 500 N.W.2d 658, 661-63 (Wis. 1993)*.

Next, the class argues that the filed rate doctrine does not apply to discriminatory insurance practices. The class argues that State Farm "cloaked its discriminatory intent behind a fictitiously named 'utilities' classification, when the classification was really an age of dwelling classification." The class cites *Dehoyos v. Allstate Corp., 345 F.3d 290 (5th Cir. 2003)*, for the proposition that courts have allowed class action lawsuits seeking to restore premiums charged under discriminatory classifications to proceed. But the court in *Dehoyos* did not address the filed rate doctrine. Instead, the court addressed whether the McCarran-Ferguson Act preempted federal discrimination law. *Id. at 293*. Thus, we do not find persuasive the class's argument that there is a "discriminatory practice" exception to the filed rate doctrine.

Next, the class argues that the filed rate doctrine does not apply because it conflicts with Minnesota common law. The [\*\*26] class cites *Bell Lumber Co. v. Great N. Ry. Co., 135 Minn. 271, 160 N.W. 688 (1916)*, for the proposition that Minnesota law has long permitted a ratepayer to recover for illegal rate charges regardless of the existence of [\*\*908] a regulatory scheme, in contradiction to the filed rate doctrine. Similarly, the class cites *Sullivan v. Minneapolis & R. R. Ry. Co., 121 Minn. 488, 142 N.W. 3 (1913)*, arguing that a Minnesota rate regulation scheme did not impair the right of a ratepayer to recover under the common law for illegal, discriminatory rates.

The class's reliance on these two Minnesota cases is not persuasive because they predate the U.S. Supreme Court's decision in *Keogh* and because they do not involve challenges to the reasonableness or legality of rates properly filed with and approved by a regulatory agency. Furthermore, the Minnesota Supreme Court's decision in *Morris* confirms the policies embodied in the filed rate doctrine.

Finally, the class argues that if this court adopts the filed rate doctrine, remand is required for holders of rental dwelling policies (RDP). The class argues that the filed rate doctrine cannot apply to the class's [\*\*27] RDP claims because an RDP is a policy form covering one- or two-family dwellings owned, but not occupied, by the policyholder. We disagree. The district court properly dismissed the class's RDP claims because *Minn. Stat. § 72A.20, subd. 13*, applies to "homeowners' insurance," and not rental dwellings. Thus, *Minn. Stat. § 72A.20, subd. 13*, does not cover RDP claims.

## DECISION

702 N.W.2d 898, \*908L<sup>2005</sup> Minn. App. LEXIS 742, \*\*27

Because the class has no private cause of action under the Unfair Claims Practices Act, *Minn. Stat. 72A.20, subd. 13* (2004), and because the filed rate doctrine bars the class's claims, the district court did not err by granting summary judgment in favor of State Farm.

**Affirmed.**

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## **Tritent Int'l Corp. v. Commonwealth**

United States District Court for the Eastern District of Kentucky

September 8, 2005, Decided ; September 8, 2005, Filed

Civil Action No. 3:04-67-JMH

### **Reporter**

2005 U.S. Dist. LEXIS 20233 \*; 2005-2 Trade Cas. (CCH) P75,066

TRITENT INTERNATIONAL CORP.; DWI, LLC; and CIBAHIA TABACOS ESPECIAS LTDA, Plaintiffs, v.  
COMMONWEALTH OF KENTUCKY, Defendant.

**Subsequent History:** Reconsideration denied by [\*Tritent Int'l Corp. v. Kentucky, 395 F. Supp. 2d 521, 2005 U.S. Dist. LEXIS 24819 \(E.D. Ky., 2005\)\*](#)

Affirmed by [\*Tritent Int'l Corp. v. Ky., 2006 U.S. App. LEXIS 26911 \(6th Cir. Ky., Oct. 30, 2006\)\*](#)

## **Core Terms**

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Manufacturers, escrow, cigarette, preempted, Participating, preemption, hybrid, implementation of a statute, market share, anticompetitive, settlement, authorize, allegations, annual payment, anti trust law, Plaintiffs', cases, motion to dismiss, state statute, tobacco, prices, empowered, immunity, boycott, sellers, cartel, join

## **LexisNexis® Headnotes**

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Governments > Police Powers

Tax Law > State & Local Taxes > Alcohol & Tobacco Products > General Overview

### **HN1 [down arrow] Governments, Police Powers**

The Escrow Statute, Ky. Rev. Stat. Ann. § 131.600-602, forces nonparticipating manufacturers (NPM) to either become subsequent participating manufacturers (SPMs), which would require paying to the state all money that would have been owed if the NPM had been an SPM from the beginning, or else to place a specified amount of money into escrow. The amount required to satisfy the second option is intended to approximate the amount being paid to the state by participating manufacturers, and is based on a flat fee per cigarette that will increase over time. The NPMs are entitled to receive interest from the escrow account, and the escrow accounts are set up as 25 year revolvers, with each year's escrow payment repaid to the NPM after being held for that period. [\*Ky. Rev. Stat. Ann. § 131.602\(2\).\*](#)

Governments > Police Powers

Tax Law > State & Local Taxes > Alcohol & Tobacco Products > General Overview

## **HN2** Governments, Police Powers

See [Ky. Rev. Stat. Ann. § 131.602\(2\)\(b\)](#).

Governments > Police Powers

Tax Law > ... > Alcohol & Tobacco Products > Tobacco Products Taxes > General Overview

Tax Law > Federal Excise Taxes > Alcohol, Firearm & Tobacco Taxes > General Overview

Tax Law > Federal Excise Taxes > Alcohol, Firearm & Tobacco Taxes > Tobacco & Tobacco Products

Tax Law > State & Local Taxes > Alcohol & Tobacco Products > General Overview

## **HN3** Governments, Police Powers

The Contraband Statute makes it illegal for distributors to place Kentucky tax stamps on cigarettes purchased from nonparticipating manufacturers who are not in compliance with the Escrow Statute. [Ky. Rev. Stat. Ann. § 131.612](#). The Attorney General of Kentucky is required to maintain a list of compliant companies, and is empowered to de-list noncompliant companies. [Ky. Rev. Stat. Ann. § 131.610](#).

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

## **HN4** Motions to Dismiss, Failure to State Claim

A district court considering a motion to dismiss must assume that all allegations are true and dismiss the claim only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations. A [Rule 12\(b\)\(6\)](#) motion tests the sufficiency of the pleadings and is not a challenge to plaintiff's factual allegations. To survive a motion to dismiss under [Rule 12\(b\)\(6\)](#), a complaint must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory. Conclusory allegations or legal conclusions masquerading as factual conclusions will not suffice to prevent a motion to dismiss.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Constitutional Law > Supremacy Clause > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN5** Exemptions & Immunities, Parker State Action Doctrine

Two findings are required before state legislation can be preempted by the Sherman Act, [15 U.S.C.S. § 1](#). First, a court must determine, as it would with all preemption claims, whether there is an irreconcilable conflict between state and federal law. Second, if such a conflict is found, a court must determine whether the legislation is protected under the doctrine of state action immunity, which will only be the case if the state "clearly articulates" its intention to displace competition and "actively supervises" the anticompetitive behavior. The preemption analysis is logically prior to the state action immunity analysis.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Constitutional Law > Supremacy Clause > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN6** [down] Exemptions & Immunities, Parker State Action Doctrine

Preemption of state statutes is not to be found lightly. The Sherman Act, [15 U.S.C.S. § 1](#), makes no mention of the state as such, and gives no hint that it was intended to restrain state action or official action directed by a state. A mere showing that a statute has anticompetitive effects will not lead to a finding of preemption. If an adverse effect on competition were, in and of itself, enough to render a state statute invalid, the States' power to engage in economic regulation would be effectively destroyed.

Antitrust & Trade Law > Sherman Act > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Constitutional Law > Supremacy Clause > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

## **HN7** [down] Antitrust & Trade Law, Sherman Act

The standard for antitrust preemption is high: a state statute, when considered in the abstract, may be condemned under the antitrust laws only if it mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Civil Procedure > ... > Federal & State Interrelationships > Federal Common Law > General Overview

Constitutional Law > Supremacy Clause > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

## **HN8** [down] Exemptions & Immunities, Parker State Action Doctrine

A statute will not be preempted by the Sherman Act, [15 U.S.C.S. § 1](#), if it "does not explicitly authorize" the illegal conduct.

Antitrust & Trade Law > Regulated Practices > Price Fixing & Restraints of Trade > General Overview

Antitrust & Trade Law > Exemptions & Immunities > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

## **HN9[ Regulated Practices, Price Fixing & Restraints of Trade**

Hybrid restraints are to be found when state acts grant "private regulatory power" to private parties. When a hybrid restraint is found to conflict with federal **antitrust law**, the statute will only be immune from challenge if it meets the same two-part test as any other statute that is *prima facie* preempted. First, the challenged restraint must be one clearly articulated and affirmatively expressed as state policy; second, the policy must be actively supervised by the State itself.

**Counsel:** [\*1] For Trident International Corp. An Illinois Corporation, DWI, LLC A Kentucky Corporation, Cibahla Tabacos Especias Ltda A Brazilian Corporation, Plaintiffs: David Foster Dobbins, Patterson, Belknap, Webb & Tyler LLP, New York, NY; Melinda G. Wilson, M.G. Wilson, PLLC, Lexington, KY; Walter Michael Luers, Patterson, Belknap, Webb & Tyler LLP - New York, New York, NY.

For Commonwealth of Kentucky Ex Rel Gregory D. Stumbo, Attorney General, in his official capacity - Gregory D. Stumbo, Defendant: James Michael Herrick, Assistant Attorney General, Frankfort, KY; Michael Plumley, Office of Attorney General - KY, Frankfort, KY.

**Judges:** Joseph M. Hood, United States District Judge.

**Opinion by:** Joseph M. Hood

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

\*\*\* \* \* \* \*

This matter is before the Court on Defendant's motion to dismiss [Record No. 36]. Plaintiffs filed a response [Record No. 74] to which Defendant replied [Record No. 75]. This matter is now ripe for review.

### **FACTUAL BACKGROUND**

In 1998, 46 states including Kentucky, collectively known as the "Settling States," entered into the Master Settlement Agreement ("MSA") with the four major cigarette companies, Philip Morris, Lorillard, [\*2] Brown & Williamson, and R.J. Reynolds, collectively known as "Original Participating Manufacturers" ("OPMs"). The MSA allowed for other manufacturers to join the agreement, and more than forty cigarette companies have joined as "Subsequent Participating Manufacturers" ("SPMs"). Together, the OPMs and SPMs are known as "Participating Manufacturers."

Participating Manufacturers are required to make large annual payments to the Settling States in perpetuity to offset a portion of healthcare and other costs imposed on states by smoking-related diseases. For OPMs, the annual payment is determined by their relative market share compared to the other Participating Manufacturers. For SPMs, the annual payments are based on a flat rate per cigarette for each cigarette sold above a certain "grandfathered" amount, which is set at the higher of either the individual SPM's 1998 market share or 125% of the SPM's 1997 market share. In addition, Participating Manufacturers must adhere to certain other conditions, such as restrictions on advertising. In exchange for these commitments, the Settling States agreed to dismiss pending lawsuits and refrain from filing additional lawsuits against the Participating [\*3] Manufacturers.

Although the four major cigarette companies are OPMs, and many other smaller cigarette companies have chosen to become SPMs, there are also many cigarette companies that have declined to join in the MSA. These companies are collectively known as "Nonparticipating Manufacturers" ("NPMs"). The Participating Manufacturers feared that

they would lose market share to the NPMs, who would not be burdened by the large annual payments to be made by OPMs and SPMs, and therefore would be able to charge lower prices. Therefore, they included in the MSA the NPM Downward Adjustment, which decreases the OPMs' annual payments if they lose market share to NPMs. The MSA also included a provision that required the Settling States to pass escrow statutes, as described below, or face substantial reductions in the annual payment. These provisions made it in the Settling States' best interest to prevent a loss of market share to NPMs as well.

In 2000, Kentucky passed an Escrow Statute, as provided for in the MSA, designed to address the concern that NPMs would escape liability for smoking-related costs associated with their cigarettes. See [KRS 131.600-602](#) [\*4] (2004). [HN1](#)[] The statute forces NPMs to either become SPMs (which would require paying to the state all money that would have been owed if the NPM had been an SPM from the beginning), or else to place a specified amount of money into escrow. The amount required to satisfy the second option is intended to approximate the amount being paid to the state by Participating Manufacturers, and is based on a flat fee per cigarette that will increase over time. Currently the escrow amount is about 1.67 cents per cigarette, about \$ 4 per carton. See [KRS 131.602\(1\)\(b\)](#). The NPMs are entitled to receive the interest from the escrow account, and the escrow accounts are set up as twenty-five year revolvers, with each year's escrow payment repaid to the NPM after being held for that period. See [KRS 131.602\(2\)](#).

In addition, the money can be removed from the escrow account in two other circumstances. First, the money can be taken out of escrow to pay any judgment or settlement to the state related to smoking-related costs. See [KRS 131.602\(2\)\(a\)](#). Second, under the Allocable Share Release ("ASR") provision, [KRS 131.602\(2\)\(b\)](#) [\*5], the NPM can request that any amount the NPM paid into escrow that was in excess of what it would have been forced to pay to Kentucky if it had been an SPM be returned to them. The statute as originally enacted provided as follows:

To the extent that a tobacco product manufacturer establishes that the amount it was required to place into escrow in a particular year was greater than the state's allocable share of the total payments that such manufacturer would have been required to make in that year under the Master Settlement Agreement . . . had it been a participating manufacturer, the excess shall be released from escrow and revert back to such tobacco product manufacturer.

This statute was intended to equalize the amounts paid into escrow by NPMs and the amounts paid to the states by SPMs. If NPMs sold their products nationally, this indeed would be the case. However, for regional NPMs that only sold in a few states, the ASR allowed the NPMs to recover almost all of the money placed into escrow. For example, an NPM selling cigarettes only in Kentucky would pay the flat rate intended to be equivalent to that paid by an SPM selling the same number of cigarettes nationwide, [\*6] but would be able to recover over 98% of that money since Kentucky's allocable share under the MSA is less than two percent. To correct this imbalance, in 2004 Kentucky enacted what Plaintiffs call the ASR Repeater, HB 97, amending [KRS 131.602\(2\)\(b\)](#) to read as follows:

[HN2](#)[] To the extent that a tobacco product manufacturer establishes that the amount it was required to place into escrow on account of units sold in the state in a particular year was greater than the master settlement agreement payments, as determined pursuant to section IX (I) of that agreement, including after final determination of all adjustments, that such manufacturer would have been required to make on account of such units sold had it been a participating manufacturer, the excess shall be released from escrow and revert back to such tobacco product manufacturer.

The ASR as amended returns funds from escrow back to the NPM based on the excess over not Kentucky's allocable share under the MSA, but rather the number of units actually sold in Kentucky.

To ensure that NPMs were forced to make the required escrow payments, Kentucky enacted a third statute, [HN3](#)[] the Contraband Statute, [\*7] which makes it illegal for distributors to place Kentucky tax stamps on cigarettes purchased from NPMs who are not in compliance with the Escrow Statute. See [KRS 131.612](#). The Attorney General of Kentucky is required to maintain a list of compliant companies, and is empowered to de-list noncompliant companies. See [KRS 131.610](#).

Plaintiffs in their Amended Complaint describe five mechanisms by which the MSA and its implementing statutes create and sustain the cartel:<sup>1</sup>

- a. Keying the annual settlement payment of each Major to its relative Market Share for that year;
- b. Restricting the output of firms joining the MSA after it was executed [i.e. SPMs] . . . ;
- c. The mandate in the MSA requiring enactment by the Settling States of escrow statutes which force NPMs to make escrow payments to eliminate any "cost advantages" those NPMs would have by not joining the MSA;
- d. The "diligent" enforcement of these escrow statutes required of each Settling State by the MSA, e.g. enactment and enforcement of contraband statutes in 43 of the 46 Settling States preventing sales by NPMs not making escrow fund payments; [\*8] and
- e. Enactment of the ASR Repealers in now at least 39 of the Settling States.

As a direct result of these conditions, the OPMs have been able to raise prices dramatically without losing any substantial share of the market. The wholesale price of a carton of premium cigarettes has increased from \$ 19 to over \$ 30 since the MSA, while the OPMs' market share has dropped only from 98% to approximately 90%. The total number of cigarettes sold domestically by the OPMs dropped twenty-five percent from 1999 to 2003, yet the OPMs' profits have increased.

OPMs have an incentive to not compete on price, since a gain in market share would lead to higher annual settlement payments. SPMs have an incentive to not compete in price, since any market share they gained would lead to their exceeding their grandfathered number of sales, which are exempt from annual payments. NPMs face the equivalent of a tax on their sales in the form of the flat fee [\*9] per cigarette that must be placed in escrow; this fee prevents them from competing by lowering prices below what the Participating Manufacturers are able to charge.<sup>2</sup>

#### **[\*10] PROCEDURAL BACKGROUND**

Plaintiffs Trident International Corp. ("Trident"), DWI, LLC ("DWI"), and Cibahia Tabacos Especias Ltda. ("Cibahia") filed this action against the Commonwealth of Kentucky on September 23, 2004, alleging claims arising out of the MSA and ensuing legislation passed to implementing the agreement. Plaintiffs are, respectively, a cigarette importer, a cigarette wholesaler, and a cigarette manufacturer. None of the Plaintiffs are parties to the MSA, and none have become SPMs. Cibahia and the company through which Trident buys cigarettes have been de-listed from the Attorney General's list of manufacturers eligible to have their cigarettes sold in Kentucky.

Specifically, Plaintiffs allege that Kentucky's Escrow, Contraband, and ASR and ASR Repeater Statutes (collectively referred to as the "implementing statutes") are preempted by Section 1 of the Sherman Act, and that those statutes also violate Plaintiffs' right to due process, equal protection, and freedom of speech, as well as being prohibited by the Kentucky Constitution's prohibition of special legislation. Plaintiffs seek declaratory and injunctive relief.

<sup>1</sup> Citations to the various provisions of the MSA have been omitted

<sup>2</sup> Plaintiffs also allege many facts that are immaterial to the current motion. Plaintiffs assert that the MSA and its implementing statutes have been ineffective in reducing smoking and that a flat tax on cigarettes would be more effective, but the effectiveness of a state policy is irrelevant to the question of whether the state statute will be preempted. See Hoover v. Ronwin, 466 U.S. 558, 574, 80 L. Ed. 2d 590, 104 S. Ct. 1989 (1984) (noting that the Supreme Court has never "suggested . . . that a state action is exempt from antitrust liability only if the sovereign acted wisely"). Plaintiffs also devote substantial space to showing that the Settling States' motivations were purely directed toward raising revenue, and that in effect the Settling States entered into a conspiracy with the OPMs to violate the Sherman Act. However, a state's subjective motivations in enacting legislation are irrelevant to whether that legislation can be challenged under the antitrust laws, see Consol. Television Cable Serv., Inc. v. City of Frankfort, 857 F.2d 354, 362 (6th Cir. 1988), and there is no conspiracy exception to state action immunity. See Mich. Paytel Joint Venture v. City of Detroit, 287 F.3d 527, 535 (6th Cir. 2001).

Plaintiffs also seek to have a class comprising [\*11] "all firms throughout the United States that purchase cigarettes made by manufacturers that do not make MSA settlement payments" certified pursuant to [Federal Rules of Civil Procedure \("Rules"\) 23\(b\)\(2\)](#) and [23\(b\)\(3\)](#) of the Federal Rules of Civil Procedure.

On February 25, 2005, Defendant filed a motion to dismiss the complaint pursuant to [Rule 12\(b\)\(6\)](#). In their response, Plaintiffs withdrew all of their claims except their [Sherman Act](#) claim.<sup>3</sup> Therefore, the Court need only address that claim.

## [\*12] STANDARD OF REVIEW

**HN4** [↑] A district court considering a motion to dismiss must "assume that all allegations are true and dismiss the claim only if it is clear that no relief could be granted under any set of facts that could be proved consistent with the allegations." [Golden v. City of Columbus, 404 F.3d 950, 959 \(6th Cir. 2005\)](#) (internal quotation marks omitted). A [Rule 12\(b\)\(6\)](#) motion tests the sufficiency of the pleadings and is "not a challenge to the plaintiff's factual allegations." [Id. at 958-59](#). However, "to survive a motion to dismiss under [Rule 12\(b\)\(6\)](#), a complaint must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory. Conclusory allegations or legal conclusions masquerading as factual conclusions will not suffice to prevent a motion to dismiss." [Mezibov v. Allen, 411 F.3d 712, 716 \(6th Cir. 2005\)](#) (internal citations omitted).

## DISCUSSION

### A. Plaintiffs' Antitrust Claim

Plaintiffs seek a declaratory judgment that Kentucky's implementing statutes are preempted by Section 1 of the Sherman Act, [15 U.S.C. § 1](#), [\*13] and an order enjoining the enforcement of the same. In support, Plaintiffs claim that the statutes enacted pursuant to the MSA create an output cartel that is *per se* illegal under the [Sherman Act](#), and for the purposes of this motion the illegal output cartel is presumed to exist. However, the interpretation of the implementing statutes is the type of "legal conclusion" on which the Court is not bound by Plaintiffs' assertions. See *id.*

### B. Preemption Under *Rice*

**HN5** [↑] Two findings are required before state legislation can be preempted by the [Sherman Act](#). First, the Court must determine, as it would with all preemption claims, whether there is an irreconcilable conflict between state and federal law. See, e.g., [Rice v. Norman Williams Co., 458 U.S. 654, 659, 73 L. Ed. 2d 1042, 102 S. Ct. 3294 \(1982\)](#); [McNeilus Truck and Mfg., Inc. v. Ohio ex rel Montgomery, 226 F.3d 429, 440 \(6th Cir. 2000\)](#). Second, if such a conflict is found, the Court must determine whether the legislation is protected under the doctrine of state action immunity, which will only be the case if the state "clearly articulates" its intention to displace competition and "actively supervises" the anticompetitive [\*14] behavior. See [Freedom Holdings, Inc. v. Spitzer, 357 F.3d 205, 222 \(2004\)](#), *reh'g denied* [363 F.3d 149 \(2d Cir. 2004\)](#); see also [Rice, 458 U.S. at 661 n.9](#) (finding it unnecessary to

<sup>3</sup> It is not entirely clear whether Plaintiffs have withdrawn their claim that the challenged statutes constitute special legislation under [Section 59 of the Kentucky Constitution](#). In listing the claims being withdrawn, Plaintiffs only explicitly mentioned their federal constitutional claims, but they also cited the Fourth Count of their Amended Complaint, which was composed solely of the state constitutional claim, and Plaintiffs did not devote any space to defending that claim in their response to this motion. In any case, the challenged statutes are not prohibited special legislation since they are based on "a reasonable and natural distinction which relates to the purpose of the act," namely, the distinction between NPMs and Participating Manufacturers, and the legislation "applies equally to all in a class." [St. Luke Hosp., Inc. v. Health Policy Bd., 913 S.W.2d 1, 3, 43 1 Ky. L. Summary 13 \(Ky. App. 1996\)](#).

engage in the immunity analysis after holding that the state statute at issue was not preempted). Thus, the preemption analysis is logically prior to the state action immunity analysis.

**HN6** [↑] Preemption of state statutes is not to be found lightly. "The *Sherman Act* makes no mention of the state as such, and gives no hint that it was intended to restrain state action or official action directed by a state." *Parker v. Brown*, 317 U.S. 341, 351, 87 L. Ed. 315, 63 S. Ct. 307 (1943). A mere showing that the statute has anticompetitive effects will not lead to a finding of preemption. See *Rice*, 458 U.S. at 659. "If an adverse effect on competition were, in and of itself, enough to render a state statute invalid, the States' power to engage in economic regulation would be effectively destroyed." *Exxon Corp. v. Governor of Maryland*, 437 U.S. 117, 133, 57 L. Ed. 2d 91, 98 S. Ct. 2207 (1978).

**HN7** [↑] The standard for antitrust preemption is high:

[A] state statute, when considered [\*15] in the abstract, may be condemned under the antitrust laws only if it mandates or authorizes conduct that necessarily constitutes a violation of the antitrust laws in all cases, or if it places irresistible pressure on a private party to violate the antitrust laws in order to comply with the statute.

*Rice*, 458 U.S. at 661; see also *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345 n.8, 93 L. Ed. 2d 667, 107 S. Ct. 720 (1987) ("Our decisions reflect the principle that the federal antitrust laws preempt state laws authorizing or compelling private parties to engage in anticompetitive behavior."); *McNeilus*, 226 F.3d at 440-41 (applying *Rice*).

The Sixth Circuit recently had the opportunity to apply this standard to an Ohio statute in *McNeilus Truck and Manufacturing, Inc. v. Ohio ex rel Montgomery*, 226 F.3d 429, a case closely analogous to the instant case. In *McNeilus*, a seller of remanufactured trucks sought to enjoin an Ohio licensing statute that prevented sellers of new or manufactured vehicles from selling in Ohio unless they either operated their own repair department, or had binding contracts with a sufficient number of repair shops [\*16] so that the sellers' customers would be able to have their vehicles serviced by someone authorized by the vehicle manufacturer to work on the vehicle without voiding the warranty. *Id.* at 434-35. The Plaintiff in *McNeilus* argued that the licensing statute facilitated a group boycott of independent sellers such as himself, and therefore that it should be preempted under *Section 1 of the Sherman Act*. *Id.* at 440-441. The district court granted summary judgment to the defendant on the *Sherman Act* preemption claim, and the Sixth Circuit affirmed that decision. *Id.*

Like the output cartel alleged in this case, the conduct alleged in *McNeilus*, a group boycott, was illegal *per se*. See *id.* at 441; see also *Fashion Originators' Guild, Inc. v. FTC*, 312 U.S. 457, 467-68, 85 L. Ed. 949, 61 S. Ct. 703, 32 F.T.C. 1856 (1941) (holding that group boycotts are illegal *per se*). Moreover, the Sixth Circuit accepted that the Ohio statute actually had created the anticompetitive effects complained of, finding that the statute "no doubt facilitates either coordinated action, if such there be, or else uncoordinated (though perhaps unconscious) parallel action by dealers [\*17] in refusing to enter binding contracts." See *McNeilus*, 226 F.3d at 441. Despite finding that the statute facilitated a *per se* violation of the *Sherman Act*, the Sixth Circuit refused to enjoin the statute on antitrust grounds. "The statute does not explicitly authorize a boycott." *Id.* Since "the statute neither authorized nor required the dealers to engage in behavior proscribed by the federal antitrust laws," the Sixth Circuit found that there was no preemption, and suggested that it would have been more proper for the plaintiff to sue the dealers actually engaged in the boycott. *Id.*

Likewise, the challenged Kentucky statutes in this case neither mandate that anyone violate the federal antitrust laws in order to comply with the statutes, nor authorize anyone to do so.<sup>4</sup> Also like the statute at issue in *McNeilus*,

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<sup>4</sup> Plaintiffs do not address the third prong of the *Rice* standard, "irresistible pressure," in either their Amended Complaint or their Response to the Motion to Dismiss. Reading Plaintiffs' allegations in the most favorable light, this Court cannot find that the Plaintiffs have alleged the existence of irresistible pressures. Plaintiffs' allegations demonstrate that the output cartel allows the participating manufacturers to extract suprareactive profits. This Court is unaware of any precedent suggesting that legislation facilitating anticompetitive conduct creates irresistible pressure to engage in such conduct, nor indeed is this Court aware of any case from the Supreme Court, the Sixth Circuit, or any other federal court actually finding preemption under the "irresistible pressure" standard in the absence of an explicit statutory mandate.

the Kentucky statutes can be presumed to facilitate conduct that is illegal *per se*, but this is not enough to support a finding of preemption. The statutes merely require cigarette manufacturers to pay certain amounts either to the state, for Participating Manufacturers, or into an interest-bearing escrow account, for NPMs; this is not [\*18] equivalent to an explicit statutory mandate or authorization of a "contract, combination . . . or conspiracy, in restraint of trade" that would be prohibited by the Sherman Act. [15 U.S.C. § 1 \(2004\)](#).

[\*19] Other courts that have addressed substantially identical challenges to state tobacco legislation have found that the state statutes were not preempted by the [Sherman Act](#). The District Court for the Northern District of California rejected one similar preemption claim:

The key allegation of plaintiff's [Sherman Act](#) claim is that the MSA creates an incentive for the manufacturer defendants to raise prices in parallel fashion, since a price increase by one OPM alone would increase market share for the others as well as for the SPMs, resulting in their having to make higher payments under the settlement. This scenario presents a "hypothetical" or "potential" conflict with the [Sherman Act](#), but not the "irreconcilable" conflict required for preemption.

[Sanders v. Lockyer, 365 F. Supp. 2d 1093, 1101 \(N.D. Cal. 2005\)](#) (dismissing a challenge to California's statutes relating to NPMs); see also [Xcaliber Int'l Ltd., LLC v. Edmondson, 2005 U.S. Dist. LEXIS 26705, No. 04-CV-0922-CVE-PJC \(N.D. Ok. May 20, 2005\)](#) (granting summary judgment in favor of the Attorney General of Oklahoma and holding that the Oklahoma version of the ASR Repealer "cannot be said to enforce any market-sharing or price-fixing agreement [\*20] among manufacturers, or any other private decision to restrain competition").<sup>5</sup>

Plaintiffs support their arguments by pointing to a series of decisions arising out of the litigation challenging a substantially identical set of statutes in New York.<sup>6</sup> See [Freedom Holdings, Inc. v. Spitzer, 357 F.3d 205 \(2d Cir.\), reh'g denied 363 F.3d 149 \(2d Cir. 2004\), remanded to 2004 U.S. Dist. LEXIS 18296, 2004 WL 2035334 \(S.D.N.Y. Sept. 14, 2004\)](#). The Second Circuit found that the plaintiffs in that case alleged sufficient facts suggesting that the statutes would be preempted to survive a motion to dismiss, see [id. at 222-26](#), and on remand the district court granted a preliminary injunction against the enforcement of New York's version of the ASR Repealer, although it denied the injunction against the other implementing statutes. See [id., 2004 U.S. Dist. LEXIS 18296, 2004 WL 2035334 at \\*1. \[\\*21\]](#) As support for the decision, the Second Circuit relied on the plaintiffs' allegations that the OPMs "have discretion to increase prices . . . assured that competitors will follow," that "the MSA empowers the tobacco companies to make anticompetitive decisions," and that the combination of the MSA and the implementing statutes "allows OPMs to set up supracompetitive prices." [Id. at 225-26](#) (internal citations omitted).

[\*22] This Court cannot find that the fact that the statutes at issue "empower," "allow," and give "discretion" to the OPMs is sufficient for preemption under *Rice*, which requires that the challenged statutes either mandate or authorize conduct that is in all cases illegal. Even read in the light most favorable to Plaintiffs, these allegations do not constitute the equivalent of a statutory mandate, and while the Second Circuit's reasoning might support a finding of authorization in the abstract, the Sixth Circuit's decision in *McNeilus* forecloses that possibility in this case. In *McNeilus*, there was no dispute that the challenged statute allowed (or empowered, or, if one prefers, gave discretion to) the dealers to engage in conduct that is *per se* illegal by boycotting independent sellers of

<sup>5</sup> The Court notes that although *Xcaliber* is unreported, both parties devoted substantial space to it in their briefs.

<sup>6</sup> Plaintiffs also cite two decisions by the Third Circuit in passing, but do not rely heavily on them in their argument, which is probably just as well. In the first case, the Third Circuit affirmed the dismissal under the *Noerr-Pennington* doctrine (which was not raised in this case) of a suit brought by NPMs against Participating Manufacturers, and then went on to opine that if the case had not been dismissed under *Noerr-Pennington*, it would also not have been dismissed under the doctrine of state action immunity. [A.D. Bedell Wholesale Co. v. Philip Morris, Inc., 263 F.3d 239 \(3d Cir. 2001\)](#). In a subsequent case brought against the State of Pennsylvania seeking to enjoin the enforcement of its implementing statutes, the Third Circuit also dismissed the suit under *Noerr-Pennington*, and then added a discussion that cast considerable doubt on the logic of *Bedell*, suggesting that the court in *Bedell* had "unintentionally" found the absence of state action immunity for the state, although the court declined to actually overrule the prior opinion. [Mariana v. Fisher, 338 F.3d 189, 203 \(3d Cir. 2003\)](#).

remanufactured cars, but this was held insufficient to invalidate the statute. [HN8](#) A statute will not be preempted if it "does not explicitly authorize" the illegal conduct. [McNeilus](#), 226 F.3d at 441 (emphasis added).

The Second Circuit felt that it could "not dismiss a challenge to the [statutory] scheme on the grounds that it is not, as a matter of law, anticompetitive. [\*23] . . . The complaint alleges such an effect and plaintiffs are entitled to attempt to prove it." [Freedom Holdings](#), 363 F.3d at 154 (denying rehearing). Nor would this Court hold, as a matter of law, that the statutory scheme is not anticompetitive. However, an anticompetitive effect is not all that Plaintiffs must allege. See [Rice](#), 458 U.S. at 659. To survive a motion to dismiss for failure to state a claim, Plaintiffs must allege facts supporting "all the material elements to sustain a recovery." [Mezibov](#), 411 F.3d at 716. Plaintiffs must therefore allege the existence of an irreconcilable conflict between the implementing statutes and the [Sherman Act](#), and to do so, those statutes must mandate or authorize conduct that would in all cases violate the [Sherman Act](#). See [Rice](#), 458 U.S. at 659. The implementing statutes clearly do not.

### C. Plaintiffs' Hybrid Restraint Claim

Plaintiffs also argue that the statutes should be preempted as [HNG](#) hybrid restraints, which are to be found when state acts grant "private regulatory power" to private parties. [324 Liquor Corp.](#), 479 U.S. at 345 n.8. The "private regulatory power" [\*24] alleged by Plaintiffs is the power of the Participating Manufacturers to force their competitors to follow their price increases so as to avoid an increase in settlement or escrow payments. When a hybrid restraint is found to conflict with federal [antitrust law](#), the statute will only be immune from challenge if it meets the same two-part *Midcal* test as any other statute that is *prima facie* preempted. See [id. at 343-44](#) (applying the test developed in [California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.](#), 445 U.S. 97, 63 L. Ed. 2d 233, 100 S. Ct. 937 (1980)). "First, the challenged restraint must be one clearly articulated and affirmatively expressed as state policy; second, the policy must be actively supervised by the State itself." [Midcal](#), 445 U.S. at 105 (internal quotation marks omitted). The Second Circuit in *Freedom Holdings* found that the MSA and its implementing statutes constituted a hybrid restraint, and also that they could not meet the *Midcal* standard since there was no active supervision of the private parties' price-setting. See [Freedom Holdings](#), 357 F.3d at 226-32. This Court need not address the *Midcal* test, however, [\*25] since the Court finds that the implementing statutes are not preempted under the *Rice* standard.

The concept of hybrid restraints is narrower than Plaintiffs would suggest. Plaintiffs seem to regard a finding of a hybrid restraint as a substitute for the preliminary preemption analysis required by *Rice* and *McNeilus*. It is not. Instead, it is simply a name for a type of regulatory scheme in which the state itself does not directly effectuate the anticompetitive restraint, but instead delegates some authority to others. A finding of a hybrid restraint answers a defendant's claim that there is no "contract, combination . . . or conspiracy in restraint of trade" of the type that would be prohibited by the [Sherman Act](#), nothing more. See [324 Liquor Corp.](#), 479 U.S. at 345 n.8.

In every case in which the Supreme Court has found a hybrid restraint preempted, the statute being challenged *explicitly mandated or authorized* illegal conduct, just as a non-hybrid restraint must in order to be preempted. Therefore, it is natural that there was no need in those cases to dwell on the initial preemption analysis required under *Rice*. In *324 Liquor Corp.* and *Midcal*, the [\*26] challenged statutes *explicitly mandated* resale price maintenance, which is illegal *per se*. [Id. at 337-40](#); [Midcal](#), 445 U.S. at 99-100. In *Schwegmann Brothers*, the challenged Louisiana statute *mandated* vertical price-fixing, which is illegal *per se*. [Schwegmann Bros. v. Calvert Distillers Corp.](#), 341 U.S. 384, 386-87, 95 L. Ed. 1035, 71 S. Ct. 745, 60 Ohio Law Abs. 81 (1951). In *FTC v. Ticor Title Insurance Company*, 504 U.S. 621, 119 L. Ed. 2d 410, 112 S. Ct. 2169 (1992), the challenged statutes *explicitly authorized* horizontal price-fixing by title insurance companies, which is illegal *per se*. See [id. at 630](#).<sup>7</sup> The

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<sup>7</sup> *324 Liquor Corp.* is the only Supreme Court case to strike down a law using the term "hybrid restraint," and none of the other cases cited above actually use the term, but Plaintiffs and others have characterized the statutory schemes in those cases as "hybrid restraints," and the usage is consistent with the definition in *324 Liquor Corp.* See, e.g. [Rice](#), 458 U.S. at 665-66 (Stevens, J., concurring). The Sixth Circuit has never adopted the concept of a "hybrid restraint" for use in its analysis.

absence of a discussion of the *Rice* standard in these cases does not mean that the standard is not applicable to hybrid restraint cases; it simply means that it was not at issue.

[\*27] Characterizing the implementing statutes as a hybrid restraint does nothing to lessen the burden on Plaintiffs to allege facts that, if true, would be sufficient to show an irreconcilable conflict between the *Sherman Act* and the state statutes. The Second Circuit in *Freedom Holdings* held that the statute was preempted because it allowed and empowered private parties to form a cartel, and therefore moved on to the *Midcal* analysis. See *Freedom Holdings*, [357 F.3d at 223-26](#). However, as discussed in Part B, *supra*, this Court cannot find that the Kentucky statutes at issue either mandate or explicitly authorize conduct that would be in all cases illegal, which is the standard for any challenged restraint in the Sixth Circuit, hybrid or not. Therefore, there is no need to reach whether the statutes are hybrid restraints, or if the statutes would satisfy the *Midcal* test for state action immunity.

## CONCLUSION

Accordingly, and for the foregoing reasons, **IT IS ORDERED:**

- (1) That Defendant's motion to dismiss Plaintiffs' Amended Complaint [Record No. 36] be, and the same hereby is, **GRANTED**;
- (2) That all of Plaintiffs' claims be, and the [\*28] same hereby are, **DISMISSED WITH PREJUDICE**.

This the 8th day of September, 2005.

**Signed By:**

**Joseph M. Hood**

**United States District Judge**

## JUDGMENT

\*\* \* \* \* \*

In accordance with the Order of even date and entered contemporaneously herewith,

**IT IS HEREBY ORDERED:**

- (1) That this action be, and the same hereby is, **DISMISSED AND STRICKEN FROM THE ACTIVE DOCKET**.
- (2) That all pending motions be, and the same hereby are, **DENIED AS MOOT**.
- (3) That all scheduled proceedings be, and the same hereby are, **CONTINUED GENERALLY**.
- (4) That this Order is **FINAL AND APPEALABLE** and **THERE IS NO JUST CAUSE FOR DELAY**.

This the 8th day of September, 2005.

**Signed By:**

**Joseph M. Hood**

**United States District Judge**

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## Slattery v. Apple Comput., Inc.

United States District Court for the Northern District of California, San Jose Division

September 9, 2005, Decided; September 9, 2005, Filed

NO. C 05-00037 JW

### **Reporter**

2005 U.S. Dist. LEXIS 50531 \*; 2005 WL 2204981

Thomas William Slattery, individually, and on behalf of all others similarly situated, Plaintiff(s), v. Apple Computer, Inc., Defendant.

**Subsequent History:** Later proceeding at [Slattery v. Apple Computer, Inc., 2005 U.S. Dist. LEXIS 32423 \(N.D. Cal., Nov. 15, 2005\)](#)

### **Core Terms**

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music, digital, alleges, iTunes, files, iPod, online, players, hard drive, portable, antitrust, monopolization, monopoly, format, relevant market, consumer, music store, played, unjust enrichment, vendors, motion to dismiss, tying product, market power, tied product, legal sale, Cartwright Act, alteration, leveraging, possesses, unfair

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**Judges:** JAMES WARE, United States District Judge.

**Opinion by:** JAMES WARE

## **Opinion**

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### **ORDER GRANTING IN PART, DENYING IN PART DEFENDANT'S MOTION TO DISMISS**

#### **I. INTRODUCTION**

Plaintiff Thomas William Slattery ("Plaintiff") brings this action on behalf of himself and all other similarly situated to challenge alleged anticompetitive conduct by Defendant Apple Computer, Inc. ("Defendant"), relating to portable hard drive digital music players and legal online sales of digital music. On June 6, 2005, the Court heard arguments on Defendant's Motion to Dismiss the Complaint pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#). Having carefully considered

the arguments of the parties and the papers submitted, this Court GRANTS in part and DENIES in part Defendant's Motion.

## **II. BACKGROUND**

Plaintiff, alleges that at some undisclosed time, he purchased digital music from Defendant's iTunes online music store. (Compl. ¶¶ 9, 14.) The music was downloaded to the hard drive of his computer. He admits that he could play the purchased music on his computer and compact disc ("CD") player. (Compl. ¶¶ 39, 42.) However, the crux of Plaintiff's complaint is that if he wishes to directly play the downloaded music from iTunes [\*6] on a portable hard drive digital music player, an iPod is the only product that can play the purchased songs. In this sense, Plaintiff claims he has been forced to buy an iPod. (Compl. ¶ 9.)

The Plaintiff alleges that there are two separate relevant markets pertinent to these claims. The first is the market for the legal online sale of digital music. (Compl. ¶ 11.) Plaintiff asserts that through its iTunes online music store, Defendant possesses monopoly market power in the legal online sale of digital music. (Compl. ¶¶ 20-21.) The second market is portable hard drive digital music players. (Compl. ¶ 11.) Plaintiff asserts that through its iPod product, Defendant possesses monopoly market power in the portable hard drive digital music players market.

The Plaintiff has pled a number of Claims that all relate to Defendant's alleged anticompetitive conduct. Primarily, the Plaintiff alleges that Defendant foreclosed iTunes digital music files from being played on any portable hard drive digital music player other than an iPod. Likewise, Defendant foreclosed digital music files downloaded from other online music vendors from being played on the iPod. The Complaint alleges that when it first [\*7] launched iTunes, Defendant adopted an encoding format, called Advanced Audio Coding ("AAC"), for its digital music files. According to the Plaintiff, this format was an "open-source" format used by many competing vendors and players that would allow iTunes' music files to play on many different competing portable hard drive digital players. (Compl. ¶¶ 37-45.) Plaintiff alleges that to stifle competition, Defendant altered the AAC format by embedding within it a separate propriety code that prevents portable hard drive digital music players other than the iPod from playing iTunes music files, and that also prevents music files bought from online music vendors other than iTunes from being played on the iPod. (Compl. ¶¶ 26-27, 37-45.)

According to the Plaintiff, the net effect of Defendant's alteration of the AAC format into the "AAC Protected" format is that the user must purchase both the online digital music file and the portable hard drive digital music player from Defendant. (Compl. ¶ 41-43.) Likewise, due to the alteration of formats, an owner of Defendant's iPod who wishes to legally purchase online digital music files must purchase such files only from Defendant's iTunes to the [\*8] exclusion of any other competing online music vendor. (Compl. ¶ 46.) Thus, but for the alteration, iTunes files would be readily playable on any number of competing portable hard drive digital music players other than the iPod, and owners of an iPod could play online digital music files purchased from any number of competing online music vendors other than Defendant's iTunes store. (Compl. ¶¶ 43, 46.)

In addition to Defendant's initial alteration of the AAC format into its proprietary protected format, Plaintiff alleges that on one occasion, Defendant took action to prevent a competitor from selling online digital music to customers. According to Plaintiff, when RealNetwork, a competing online vendor of digital music files, independently defeated Defendant's "AAC Protected" format and began selling music files that played on the iPod for 45 cents a song verses iTunes' price at 99 cents per song, Defendant immediately changed its software code so as to prevent RealNetwork's music files from being played on Defendant's iPod devices. RealNetwork's digital music files were being sold for less than the price of Defendant's iTunes music files. Thus, Plaintiff alleges that Defendant's actions [\*9] prevented consumers of the iPod from accessing these competing, less expensive music files. (Compl. ¶¶ 46-50.)

## **III. STANDARDS**

A complaint may be dismissed for failure to state a claim upon which relief can be granted. [Fed. R. Civ. P. 12\(b\)\(6\)](#). A claim may be dismissed as a matter of law for: "(1) lack of a cognizable legal theory or (2) insufficient facts under a cognizable legal theory." [Robertson v. Dean Witter Reynolds, Co., 749 F.2d 530, 534 \(9th Cir. 1984\)](#). "A complaint should not be dismissed for failure to state a claim unless it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief." [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#). The court "must presume all factual allegations of the complaint to be true and draw all reasonable inferences in favor of the nonmoving party." [Usher v. City of Los Angeles, 828 F.2d 556, 561 \(9th Cir. 1987\)](#). In determining the propriety of a [Fed. R. Civ. P. 12\(b\)\(6\)](#) dismissal, a court may not look beyond the complaint. [Schneider v. California Dept. of Corrections, 151 F.3d 1194, 1197 \(9th Cir. 1998\)](#) ("The focus of any [Rule 12\(b\)\(6\)](#) dismissal . . . is the complaint"). A court may dismiss a case without leave to amend if the Plaintiff is unable to cure the defect by amendment. [Lopez v. Smith, 203 F.3d 1122, 1129 \(9th Cir. 2000\)](#). To survive a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion, an antitrust complaint "need only allege sufficient facts from which the court can discern the elements of an injury resulting from an act forbidden by the antitrust laws." [Newman v. Universal Pictures, 813 F.2d 1519, 1522 \(9th Cir. 1987\)](#), cert. denied, 486 U.S. 1059, 108 S. Ct. 2831, 100 L. Ed. 2d 931 (1988); [United States v. LSL Biotechnologies, 379 F.3d 672, 698 \(9th Cir. 2004\)](#) (stating [\*10] that notice pleading is the only requirement for an antitrust claim).

#### **IV. DISCUSSION**

Based on alleged anticompetitive behavior, Plaintiff charges Defendant with violating the [Sherman Act](#), [California's Cartwright Act](#), [California's unfair competition law](#), common law monopolization, and common law unjust enrichment. Defendant now moves the Court to dismiss Plaintiff's Complaint under [Fed. R. Civ. P. 12\(b\)\(6\)](#), for failure to state a claim upon which relief can be granted.

##### **A. Illegal Tying Claims**

In order to establish an illegal tying arrangement under [15 U.S.C. § 1](#), plaintiffs must show "three elements: (1) a tie between two separate products or services sold in relevant markets; (2) sufficient economic power in the tying product market to affect the tied market; and (3) an effect on a non-insubstantial volume of commerce in the tied product market." [County of Tuolumne v. Sonora Cnty. Hosp., 236 F.3d 1148, 1157-58 \(9th Cir. 2001\)](#). Implicit in these elements is the need of the seller of the tying product "to force the buyer into the purchase of the tied product that the buyer did not want at all, or might have preferred to purchase elsewhere on different terms." [Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 12, 104 S. Ct. 1551, 80 L. Ed. 2d 2 \(1984\)](#); [Paladin Assocs., Inc. v. Montana Power Co., 328 F.3d 1145, 1159 \(2003\)](#).

Plaintiff, in Claims I and II, alleges two federal antitrust tying claims against the Defendant. (Compl. 19:8-21:17.) Claim I alleges that the [\*11] tying product is the legal sale of online digital music files, sold through its iTunes music store. (Compl. ¶ 63.) The tied product is the iPod. (Compl. ¶ 63.) Plaintiff alleges, if a consumer purchases digital music from Defendant's iTunes music store and chooses to purchase a portable hard drive digital music player in order to listen to the purchased digital music remotely, Defendant coerces the consumer to purchase its iPod. (Compl. ¶ 63.) Claim II alleges that the tying product is the iPod and the tied product is iTunes. (Compl. ¶ 70.) If a consumer purchases Defendant's iPod and chooses to purchase an online digital music file, Defendant coerces the consumer to purchase online digital music from its iTunes music store. (Compl. ¶ 70.)

In both Claims I and II, Plaintiff alleges that Defendant has market power in the tying product which is used to coerce the consumer to purchase the tied product. Both Claims include the same two allegedly separate products, the difference being the two products are switched as to which is the "tying" product and which is the "tied" product. It seems inconsistent to allege that a product is both a "tying" product and a "tied" product. However, for [\*12] pleading purposes, the Court will allow the inconsistency to persist. At some appropriate point in the litigation, an election might be necessary.

Accepting Plaintiff's allegations as true, all elements of a tying claim are met. The Plaintiff alleges two relevant markets: the legal sale of online digital music files and portable hard drive digital music players in the geographic market of the United States. (Compl. ¶ 11.) The Plaintiff also alleges that Defendant possesses an 80 percent market share in the legal sale of online digital music files, and over a 90 percent market share in portable hard drive digital music players. (Compl. ¶¶ 20, 24.) This Court also finds that the tying would have an effect on a substantial volume of commerce. (Compl. ¶¶ 20.) The element of coercion is also adequately plead in Plaintiff's Complaint. (Compl. 19:8-21:17.) This Court finds that, at the pleading stage, Plaintiff has satisfied the burden of alleging Defendant has sufficient economic power in the tying markets to affect the tied markets.

The Defendant argues that a tying claim cannot be made because consumers can purchase either iTunes or the iPod separately. (Motion to Dismiss at 4:26-5:8.) However, [\*13] the fact that Plaintiff can purchase the items separately does not dismiss a tying claim. *Eastman Kodak Co. v. Image Technical Servs., Inc.*, 504 U.S. 451, 463, 112 S. Ct. 2072, 119 L. Ed. 2d 265 (1992). The Defendant further contends that both products are capable of functioning independently without a consumer purchasing both. (Motion to Dismiss at 5:9-19.) However, this argument ignores Plaintiff's allegations of the relevant markets. The alleged relevant markets, as this Court must limit itself to, are the legal sale of online digital music files and portable hard drive digital music players. (Compl. ¶ 11.) Plaintiff alleges that, within these relevant markets, the only legal digital music files capable of playing directly on an iPod are music files sold by Defendant's iTunes music store. (Compl. 19:8-21:17.) Further, the only portable hard drive digital music player capable of directly playing music from Defendant's iTunes music store is the iPod. (Compl. 19:8-21:17.) Although the alleged markets are narrowly defined by Plaintiff, this Court accepts these allegations as true for the purposes of this motion. Thus, as plead, Plaintiff alleges all of the elements of a tying claim to survive a motion to dismiss under [Rule 12\(b\)\(6\)](#).

## **B. Monopolization Claims**

Plaintiff, in Claims III and IV, alleges that Defendant [\*14] violated [15 U.S.C. § 2](#) by acquiring or maintaining monopoly market power. (Compl. at 21:18-23:10.) In order to state a claim for monopolization under [15 U.S.C. § 2](#), a plaintiff must show that: "(1) the defendant possesses monopoly power in the relevant market; (2) the defendant has willfully acquired or maintained that power; and (3) the defendant's conduct has caused antitrust injury." *Cost Mgmt. Servs. v. Washington Natural Gas*, 99 F.3d 937, 949 (9th Cir. 1996). Both Claims III and IV of Plaintiff's Complaint allege Defendant possesses monopoly market power in the legal sale of online digital music and portable hard drive digital music players, respectively. (Compl. ¶¶ 79, 84.) Further, the Plaintiff alleges facts which if proven could be found to suggest the conclusion that Defendant has willfully acquired or maintained that power. (Compl. ¶¶ 78, 83.) Finally, the Plaintiff alleges that an antitrust injury has resulted from Defendant's conduct. (Compl. ¶¶ 80, 85.) This Court finds that Plaintiff has sufficiently plead the elements for a claim of monopolization to survive a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion. Further, by satisfying the elements of a Sherman Act monopolization claim, the Plaintiff has adequately plead, in Claim X, a common law claim of monopolization.

## **C. Attempted Monopolization and Leveraging [\*15] Claims**

Plaintiff, in Claims V and VI, alleges that Defendant has violated [15 U.S.C. § 2](#) by leveraging its power in one market to attempt to establish a monopoly in another. (Compl. at 23:11-24:17.) The Ninth Circuit does not view leveraging of a monopoly as an independent claim under [section 2](#) of the Sherman Act. *Alaska Airlines, Inc. v. United Airlines, Inc.*, 948 F.2d 536, 546 (9th Cir. 1991). However, attempted monopolization may include allegations of monopoly leveraging. *Id. at 549* ("If there is a dangerous probability that a monopoly will be created by leveraging conduct, then the conduct will be reached under the doctrine of attempted monopoly."). Therefore, in order to state a claim, Plaintiff must allege the elements of attempted monopolization. The elements include, "(1) a specific intent to monopolize a relevant market--i.e., an intent to control prices or destroy competition in a relevant market; (2) predatory or anticompetitive conduct designed to control prices or destroy competition; (3) a dangerous probability of success--i.e., a probability of achieving monopoly power in the relevant market; and (4) causal antitrust injury."

Paladin Assocs., 328 F.3d at n.22. This Court finds that Plaintiff has not adequately plead the elements of attempted monopolization. Therefore this Court [\*16] dismisses Claims V and VI with leave to amend.

#### **D. Cartwright Claim**

Plaintiff, in Claim VII, alleges Defendant violated California state law under the Cartwright Act. (Compl. at 24:15-25.) "Because the Cartwright Act has objectives identical to the federal antitrust acts, the California courts look to cases construing the federal antitrust laws for guidance in interpreting the Cartwright Act." Vinci v. Waste Mgmt., Inc., 36 Cal. App. 4th 1811, 43 Cal. Rptr. 2d. 337, n.1 (Cal. Ct. App. 1995). Typically, if a plaintiff is capable of maintaining a Sherman Act claim, the plaintiff is capable of maintaining a similar Cartwright Act claim. However, the laws are distinct. Dimidowich v. Bell & Howell, 803 F.2d 1473, 1478 (9th Cir. 1986). In this instance, although Plaintiff uses overly broad language to allege a Cartwright Act violation, Plaintiff has incorporated the elements of the Sherman Act violation and thus, the Court will allow Claim VII to stand at the pleading stage of the litigation. (Compl. at 24:20-25.)

#### **E. Unfair Competition Law Claim**

Plaintiff, in Claim VIII, alleges that Defendant has violated California's unfair competition law. (Compl. at 25:1-17.) A claim under California Business & Professions Code section 17200 is far broader than a federal antitrust claim, and thus Defendant's conduct may constitute a violation of section 17200 even if not rising for some technical reason to an antitrust violation. [\*17] Cel-Tech Comms., Inc. v. Los Angeles Cellular Tel. Co., 20 Cal. 4th 163, 187, 83 Cal. Rptr. 2d 548, 973 P.2d 527 (1999). Section 17200 defines "unfair competition" as "any unlawful, unfair or fraudulent business act or practice." CAL. BUS. & PROF. CODE § 17200. The California Supreme Court has consistently recognized the sweeping nature of section 17200, stating: "When a plaintiff who claims to have suffered injury from a direct competitor's "unfair" act or practice invokes section 17200, the word "unfair" in that section means conduct that threatens an incipient violation of an antitrust law." Cel-Tech, 20 Cal. 4th at 187. This Court finds that Plaintiff's pleading of a section 17200 violation is adequate to survive a motion to dismiss.

#### **F. Plaintiff's Unjust Enrichment Claim Fails as a Matter of Law**

Plaintiff, in Claim IX, alleges that Defendant has been unjustly enriched from the money and business given for purchases from iTunes or iPods. (Compl. ¶ 100.) Plaintiff further states that he is entitled to disgorgement of Defendant's ill-gotten gains. (Compl. ¶ 100.) Defendant argues that the unjust enrichment claim should be dismissed at a matter of law because Plaintiff has purchased a product in a transaction that creates a contract. (Motion to Dismiss at 17:24-25.) Under California law, an action for unjust enrichment is not possible where a contractual relationship exists between the two parties. Gerlinger v. Amazon.com, Inc., 311 F. Supp. 2d 838, 856 (N.D. Cal. 2004). By Plaintiff's [\*18] own statements, a contract under California law is made when consumers purchase either an iPod or a music file from iTunes. See CAL. COM. CODE §§ 2106(1), 2204(1). Therefore, Plaintiff's common law unjust enrichment claim is dismissed as a matter of law with prejudice.

#### **V. CONCLUSION**

For the reasons set forth above, the Court DENIES Defendant's Motion to Dismiss First, Second, Third, Fourth, Seventh, Eighth, and Tenth Claims. The Court GRANTS Defendant's Motion to Dismiss Plaintiff's Fifth and Sixth Claims with leave to amend. This Court GRANTS Defendants' Motion to Dismiss Plaintiff's Ninth Claim with prejudice. To avoid confusion as the case proceeds, on or before **October 11, 2005**, Plaintiff shall file and serve an amended complaint which contains only the allowed claims, including those that the Court has granted leave to amend if Plaintiff wishes to amend. Defendant shall file a response to the amended complaint no later than 15 days following the filing and service of the amended complaint.

Dated: September 9, 2005

/s/ James Ware

JAMES WARE

United States District Judge

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## Corey Airport Servs. v. City of Atlanta

United States District Court for the Northern District of Georgia, Atlanta Division

September 12, 2005, Decided; September 12, 2005, Filed

CIVIL ACTION NO. 1:04-CV-3243-CAP

### **Reporter**

2005 U.S. Dist. LEXIS 62370 \*

COREY AIRPORT SERVICES, INC., Plaintiff, v. THE CITY OF ATLANTA, et al., Defendants.

**Subsequent History:** Decision reached on appeal by [Corey Airport Servs. v. City of Atlanta, 181 Fed. Appx. 908, 2006 U.S. App. LEXIS 13063 \(11th Cir. Ga., May 24, 2006\)](#)

Motion granted by, in part, Motion denied by, in part [Corey Airport Servs. v. City of Atlanta, 2007 U.S. Dist. LEXIS 116595 \(N.D. Ga., Feb. 20, 2007\)](#)

Dismissed by [Corey Airport Servs. v. City of Atlanta, 2007 U.S. Dist. LEXIS 116596 \(N.D. Ga., May 23, 2007\)](#)

Motion granted by [Corey Airport Servs. v. City of Atlanta, 2007 U.S. Dist. LEXIS 116597 \(N.D. Ga., June 22, 2007\)](#)

## **Core Terms**

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discovery, motion to stay, interlocutory appeal, qualified immunity, certify, motion to amend, pretrial

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**Judges:** CHARLES A. PANNELL, JR., United States District Judge.

**Opinion by:** CHARLES A. PANNELL, JR.

## **Opinion**

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### **ORDER**

On July 12, 2005, the court entered an order ("July 12 Order") [Doc. No. 89] granting in part and denying in part various motions to dismiss filed by Clear Channel and several of its individual employees ("Clear Channel Defendants"), the City of Atlanta ("City"), and several individual employees of the City ("Atlanta City Defendants"). On July 15, the court entered an order [\*6] ("July 15 Order") [Doc. No. 90] granting in part and denying in part defendant Barbara Fouch's motion to dismiss. This matter is now before the court on the following motions: (1) the City and the Atlanta City Defendants' motion to stay discovery [Doc. No. 104]; (2) the City's motion to amend the court's July 12 Order to add certification for interlocutory appeal [Doc. No. 106]; (3) the Clear Channel Defendants' motion for an amendment of the July 12 Order to certify the order for interlocutory appeal [Doc. No. 107]; (4) the Clear Channel Defendants' motion to stay litigation pending appeal [Doc. No. 108]; (5) Fouch's motion for amendment of the July 15 Order so as to certify the order for interlocutory appeal and also motion to stay litigation [Doc. No. 109]; and (6) Corey's request for a pretrial conference [Doc. No. 115].

### I. The Motions To Amend [Doc. Nos. 106, 107, and 109]

In its motion [Doc. No. 106], the City seeks to have the court certify the following issue for interlocutory appeal: "Whether, under [42 U.S.C. § 1983](#), an unsuccessful bidder for a municipal contract is entitled to 'lost profits' when the municipality has wrongfully denied its bid." City's Brief at 9 [Doc. No. 106].

In their respective [\*7] motions [Doc. Nos. 107 and 109], the Clear Channel Defendants and Fouch seek to have the court certify the following issues for interlocutory appeal:

1. Whether the Parker state action doctrine requires active state supervision of the alleged anticompetitive conduct to immunize private parties from liability for antitrust claims when a municipality is the effective decisionmaker;
2. Whether there is a conspiracy exception to either the Parker state action doctrine or Noerr-Pennington immunity from antitrust claims;
3. Whether Corey defined a relevant market cognizable in antitrust law; and
4. Whether the Noerr-Pennington doctrine immunizes private parties from liability for [42 U.S.C. § 1983](#) equal protection conspiracy claims.

Clear Channel Defendants Brief at 8 [Doc. No. 107]; Fouch's Brief at 8 [Doc. No. 109]. "Under [28 U.S.C. § 1292\(b\)](#), the district court may certify an interlocutory order for appeal if the order (1) involves a controlling question of law, (2) as to which there is substantial ground for difference of opinion, and (3) an immediate appeal from the order may materially advance the ultimate termination of the litigation." [Harris v. Luckey](#), 918 F.2d 888, 892 (11th Cir. 1990). In this case, the court finds that none of the issues presented by the defendants satisfy [\*8] these three conditions. The court notes that, with regards to several of the issues presented, the defendants have misconstrued the plaintiff's complaint and the holding of the court in attempting to create a "substantial difference of opinion" where none exists. Accordingly, the court DENIES the City's motion to amend [Doc. No. 106]; DENIES the Clear Channel Defendants' motion to amend [Doc. No. 107]; and DENIES Fouch's motion to amend [Doc. No. 109].

### II. The Motions to Stay Discovery [Doc. No. 104, 108, and 109] and Corey's Motion for a Pretrial Conference [Doc. No. 115]

In the July 12 Order, the court held that, at this early stage of the litigation, the Atlanta City Defendants were not entitled to qualified immunity. The Supreme Court has held "that a district court's denial of a claim of qualified immunity, to the extent that it turns on an issue of law, is an appealable 'final decision' within the meaning of [28 U.S.C. § 1291](#) notwithstanding the absence of a final judgment." [Mitchell v. Forsyth](#), 472 U.S. 511, 526, 105 S. Ct. 2806, 2817, 86 L. Ed. 2d 411 (1985). In this case, the Atlanta City Defendants contend that the court's denial of their claims of qualified immunity turns on an issue of law, and, therefore, they have appealed. "The defense of

sovereign or qualified immunity [<sup>\*9</sup>] protects government officials not only from having to stand trial, but from having to bear the burdens attendant to litigation, including pretrial discovery. A district court, therefore, properly stays discovery pending appeal of a denial of immunity." *Blinco v. Green Tree Servicing, LLC*, 366 F.3d 1249, 1252 (11th Cir. 2004) (citations omitted).

In this case, the Atlanta City Defendants are currently appealing this court's denial of their claim to qualified immunity. The court holds that they are entitled to a stay in discovery pending the resolution of their appeal. Furthermore, the plaintiff's claims against the Atlanta City Defendants are inextricably intertwined with the claims against the City, the Clear Channel Defendants, and Fouch. Accordingly, the court will stay all discovery in this action pending the resolution of the Atlanta City Defendants' appeal. Corey argues that the court should not stay all discovery because the Atlanta City Defendants will ultimately be witnesses in this case even if the Eleventh Circuit determines that they are entitled to qualified immunity. Though this may be true, the court finds that it is prudent to stay all litigation in this case while the Atlanta City Defendants appeal so that the court can direct discovery in [<sup>\*10</sup>] accordance with the holding of the Eleventh Circuit. Corey chose to sue the Atlanta City Defendants in their individual capacities, and those individuals have the right to appeal this court's denial of their claim to qualified immunity. The court, therefore, will not entertain Corey's complaints about undue delay. For this reason, the court GRANTS the City and the Atlanta City Defendants' motion to stay discovery [Doc. No. 104]; GRANTS the Clear Channel Defendants' motion to stay litigation pending appeal [Doc. No. 108]; and GRANTS Fouch's motion to stay litigation [Doc. No. 109]. Discovery in this case is hereby stayed pending the resolution of the Atlanta City Defendants' appeal.

As to Corey's motion for a pretrial conference [Doc. No. 115], the court finds that it is unnecessary at this point to have such a conference given the court's ruling above. Accordingly, the motion [Doc. No. 115] is DENIED.

## Conclusion

For the foregoing reasons, the court:

- (1) GRANTS the City and the Atlanta City Defendants' motion to stay discovery [Doc. No. 104];
- (2) DENIES the City's motion to amend the court's July 12 Order to add certification for interlocutory appeal [Doc. No. 106];
- (3) DENIES the Clear Channel [<sup>\*11</sup>] Defendants' motion for an amendment of the July 12 Order to certify the order for interlocutory appeal [Doc. No. 107];
- (4) GRANTS the Clear Channel Defendants' motion to stay litigation pending appeal [Doc. No. 108];
- (5) DENIES in part and GRANTS in part Fouch's motion for amendment of the July 15 Order so as to certify that order for interlocutory appeal and motion to stay litigation [Doc. No. 109]; and
- (6) DENIES Corey's request for a pretrial conference [Doc. No. 115].

The Clerk of Court is directed to submit this file to the undersigned after the resolution of the Atlanta City Defendants' appeal to the Eleventh Circuit Court of Appeals.

SO ORDERED, this 12th day of September, 2005.

/s/ Charles A. Pannell, Jr.

CHARLES A. PANNELL, JR.

United States District Judge



## **K&R Nursing Servs. v. Genesis Health Ventures of Windsor, Inc.**

Superior Court of Connecticut, Judicial District of Hartford At Hartford

September 13, 2005, Decided ; September 15, 2005, Filed

CV030830546S

### **Reporter**

2005 Conn. Super. LEXIS 2473 \*; 2005 WL 2497414

K&R Nursing Services, Inc. et al. v. Genesis Health Ventures of Windsor, Inc. dba Windsor Hall and Genesis Health Ventures of Bloomfield, Inc. et al.

**Notice:** [\*1] THIS DECISION IS UNREPORTED AND MAY BE SUBJECT TO FURTHER APPELLATE REVIEW. COUNSEL IS CAUTIONED TO MAKE AN INDEPENDENT DETERMINATION OF THE STATUS OF THIS CASE.

**Prior History:** [K&R Nursing Servs. v. Genesis Health Ventures of Windsor, Inc., 2005 Conn. Super. LEXIS 346 \(Conn. Super. Ct., Feb. 7, 2005\)](#)

## **Core Terms**

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motion to strike, allegations, antitrust, monopolization, antitrust claim, plaintiffs', summary judgment motion, sufficient facts, anti trust law, defendants', memorandum, Pleadings, compete, survive, courts

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > General Overview

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

### **HN1[] Motions to Dismiss, Failure to State Claim**

On a motion to strike, a court must construe the facts in the complaint most favorably to the plaintiff. If facts provable in the complaint would support a cause of action, the motion to strike must be denied. Pleadings must be construed broadly and realistically, rather than narrowly and technically.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Civil Procedure > ... > Justiciability > Standing > General Overview

Standing to assert an antitrust claim requires a showing that a plaintiff has been injured in his business or property by reason of anything forbidden in the antitrust laws. A two-part test exists for courts to determine whether there is antitrust standing: as a necessary first step, courts must determine whether a plaintiff suffered an antitrust injury. If the answer to that question is yes, that must then determine whether any of the other factors, largely relating to the directness and identifiability of the plaintiff's injury, prevent the plaintiff from being an efficient enforcer of the antitrust laws.

Civil Procedure > Pleading & Practice > Pleadings > General Overview

### **HN3** **Pleading & Practice, Pleadings**

See [Conn. Gen. Prac. Book, R. Super. Ct. § 10-1.](#)

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Civil Procedure > ... > Defenses, Demurrers & Objections > Motions to Strike > General Overview

Civil Procedure > ... > Pleadings > Heightened Pleading Requirements > General Overview

### **HN4** **Regulated Practices, Trade Practices & Unfair Competition**

No heightened pleading requirements apply in antitrust cases.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### **HN5** **Regulated Practices, Trade Practices & Unfair Competition**

A plaintiff in an antitrust case is not required to allege, or prove, that it competes in precisely the same market.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Criminal Law & Procedure > ... > Acts & Mental States > Mens Rea > Specific Intent

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > State Regulation

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

### **HN6** **Monopolies & Monopolization, Actual Monopolization**

Monopolization under [Conn. Gen. Stat. § 35-27](#) is adequately pled by alleging some conduct permitting an inference of specific intent to monopolize. The same conclusion applies to claims of attempted monopolization, as well as unlawful restraint of trade, [Conn. Gen. Stat. § 35-28\(d\)](#).

**Judges:** Douglas S. Lavine Judge, Superior Court.

**Opinion by:** Douglas S. Lavine

## Opinion

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### DECISION ON MOTION TO STRIKE DATED APRIL 29, 2005

Pursuant to [Practice Book Section 10-39 et seq.](#), defendants moved on April 29, 2005, to strike Count Six of the plaintiffs' Substituted Revised Complaint. Subsequent to the filing of the motion to strike, plaintiff filed an Amended Substituted Revised Complaint, dated June 10, 2005. Defendants filed an objection to the motion strike on July 21, 2005, supported by a memorandum of law in opposition. On July 29, 2005, defendants filed a reply to plaintiff's objection.

This Court issued a memorandum of decision on a previous motion to strike setting out many of the essential facts as alleged in the complaint then pending. Knowledge of these facts is assumed.

In their April 29, 2005, Motion to Strike, defendants make two claims. First, they allege that the plaintiffs have failed to meet the minimum standing requirement for antitrust claims as a result of insufficient allegations of antitrust injury and [\*2] participation in the same market. Second, they allege that plaintiffs have failed to allege sufficient facts to support the claims of monopolization and unfair restraint of trade.

Plaintiffs dispute these arguments, and argue that Count Six sufficiently sets out the claims they wish to assert. Some of defendants' arguments, plaintiffs contend, are more properly asserted at a later time in a motion for summary judgment.

The Court agrees with the plaintiffs and denies the motion to strike.

#### *Standard on a Motion to Strike*

[HN1](#) [↑] On a motion to strike, the court "must construe the facts in the complaint most favorably to the plaintiff . . . If facts provable in the complaint would support a cause of action, the motion to strike must be denied." [Faulkner v. United Technologies Corp., 240 Conn. 576, 693 A.2d 293 \(1997\)](#). "Pleadings must be construed broadly and realistically, rather than narrowly and technically . . ." (citation omitted; internal quotation marks omitted), [Gazo v. Stamford, 255 Conn. 245, 260, 765 A.2d 505 \(2001\)](#).

#### *Allegations of Antitrust Injury and Participation in the Same Market*

Analysis of Count Six of the complaint persuades the [\*3] Court that, for purposes of the pending motion to strike, plaintiffs have adequately alleged an antitrust claim. See, in particular, paragraphs 58 through 78. [Assoc. General Contractors of Cal., Inc. v. California State Council of Carpenters, 459 U.S. 519, 74 L. Ed. 2d 723, 103 S. Ct. 897 \(1983\)](#). See also [Continental Orthopedic Appliances v. Health Ins., 956 F. Supp. 367, 371 \(E.D.N.Y. 1997\)](#).

[HN2](#) [↑] Standing to assert an antitrust claim requires a showing that plaintiff has been "injured in his business or property by reason of anything forbidden in the antitrust laws." [Wyatt Energy, Inc. v. Motiva Enterprises, LLC., 2002 Conn.Super LEXIS 3995 \(December 12, 2002, Hodgson, J.\) \(33 Conn. L. Rptr. 566\)](#) See [Balaklaw v. Lovell, 14 F.3d 793, 798 n.9 \(2d Cir. 1994\)](#), which sets out a two-part test for courts to determine whether there is antitrust standing: "As a necessary first step, courts must determine whether the plaintiff suffered an antitrust injury. If the answer to that question is yes, that must then determine whether any of the other factors, largely relating to the directness and identifiability of the plaintiff's injury, prevent the [\*4] plaintiff from being an efficient enforcer of the antitrust laws." Drawing all reasonable inferences in favor of plaintiffs, as the Court must, the Court concludes that plaintiffs have sufficiently alleged that K&R is a competitor or participant in the relevant market, see paragraphs 61 through 64 of Count Six, and that plaintiff has standing.

The Court concludes as well that K&R has sufficiently alleged an antitrust injury. See paragraphs 65 through 70 of Count Six. Defendants argue that plaintiffs' allegations lack sufficient facts to support the claim that the cost of care is going up, and the quality of care is going down, and note the differences between what is required in Federal practice and state practice. [Section 10-1 of the Practice Book](#), "Fact pleading," provides as follows: [HN3](#) [↑] "Each pleading shall contain a plain and concise statement of the material facts on which the pleader relies, but not of the evidence by which they are to be proved . . ." It is true that the plaintiffs' allegations in this regard are quite general, but as plaintiffs note, [HN4](#) [↑] no heightened pleading requirements apply in antitrust cases. [Todd v. Exxon Corp., 275 F.3d 191, 198 \(2d Cir. 2001\)](#). [\*5] The Court is persuaded that allegations are sufficient to survive the motion to strike, and that defendants will have ample opportunity through discovery--and then, if appropriate, a motion for summary judgment and/or trial--to explore and contest these allegations in detail.

Plaintiffs have also adequately alleged that K&R and defendants compete in substantially similar markets. The court is not persuaded that [HN5](#) [↑] plaintiffs must allege, or prove, that they compete in *precisely* the same market. [United States v. E. I. du Pont de Nemours & Co., 351 U.S. 377, 393, 76 S. Ct. 994, 100 L. Ed. 1264 \(1956\)](#); [Pepsico, Inc. v. Coca-Cola, 315 F.3d 101, 105 \(2nd Cir. 2002\)](#).

Finally, the Court concludes that K&R has adequately pleaded, for purpose of surviving the motion to strike, [HN6](#) [↑] monopolization under [Section 35-27](#), by alleging some conduct permitting an inference of specific intent to monopolize. [Plumbers Local 598 v. Morris, 511 F. Supp. 1298, 1308 \(E.D.Wash. 1981\)](#); [Strobl v. New York Mercantile Exchange, 561 F. Supp. 379, 384 \(S.D.N.Y. 1983\)](#). See also [Broadway Delivery Corp. v. United Parcel Service of America, Inc., 651 F.2d 122, 128](#) [\*6] (2d Cir.), cert. Denied, 454 U.S. 968, 70 L. Ed. 2d 384, 102 S. Ct. 512 (1981). The Court reaches the same conclusion with respect to the claims of attempted monopolization. [Shea v. First Federal Savings & Loan Ass'n. of New Haven, 184 Conn. 285, 304, 439 A.2d 997 \(1981\)](#), and unlawful restraint of trade, [Section 35-28\(d\)](#). See [Ajello v. Hartford Federal Sav. & Loan Asso., 32 Conn.Supp. 198, 347 A.2d 113 \(Conn.Super. 1975\)](#).

For all of these reasons, defendants' April 29, 2005, Motion to Strike is denied.

Douglas S. Lavine

Judge, Superior Court

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## Lde Corp. v. Dyno Nobel

United States District Court for the District of Wyoming

September 13, 2005, Decided; September 13, 2005, Filed

Case No. 04-CV-0137-J

**Reporter**

2005 U.S. Dist. LEXIS 60985 \*

LDE CORPORATION, Plaintiff, vs. DYNO NOBEL, INC., Defendant.

**Prior History:** [LDE Corp. v. Dyno Nobel Inc., 2005 U.S. Dist. LEXIS 60983 \(D. Wyo., Aug. 8, 2005\)](#)

### **Core Terms**

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patent, baseless, probable cause, immunity, patent infringement, antitrust, sham, summary judgment, infringement, prong, alleges, discovery, argues, underlying suit, Sherman Act, pre-filing, patentee, subjective motivation, matter of law, tort claim, parties, contractual relationship, summary judgment motion, district court, sham exception, instant case, bring suit, communications, pre-litigation, contacted

**Counsel:** [\*1] For Lde Corporation, Plaintiff: Donald A Degnan, Timothy P Getzoff, LEAD ATTORNEYS, HOLLAND & HART, Boulder, CO USA; Joseph T Jaros, LEAD ATTORNEY, HOLLAND & HART, Denver, CO USA; Michael Daniel Smith, LEAD ATTORNEY, QUESTAR EXPLORATION AND PRODUCTION COMPANY, Cheyenne, WY USA.

For Dyno Nobel Inc, Defendant: David M Bennion, Francis M Wikstrom, Raymond J Etcheverry, LEAD ATTORNEYS, PARSONS BEHLE & LATIMER, Salt Lake City, UT USA; Rick A Thompson, LEAD ATTORNEY, HATHAWAY & KUNZ, Cheyenne, WY USA.

**Judges:** ALAN B. JOHNSON, UNITED STATES DISTRICT JUDGE.

**Opinion by:** ALAN B. JOHNSON

### **Opinion**

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#### **MEMORANDUM OPINION REGARDING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT**

The above-entitled matter comes before the Court on defendant Dyno Nobel, Inc.'s Motion for Summary Judgment. The Court, having reviewed the motions and materials filed in support thereof and in opposition thereto, having heard oral argument, and being otherwise fully advised in the premises, **FINDS** and **ORDERS** as follows:

#### **I. Factual Background**

On October 24, 2002, Dyno Nobel, Inc. (the Defendant or Dyno), brought a civil action against LDE Corp. (Plaintiff or LDE) alleging that LDE had infringed Dyno's U.S. Patent No. 4,875,950 ('950 patent). The case was captioned *Dyno Nobel, Inc. v. LDE Corp.*, No. 02-CV-199 [\*2] (the patent litigation). On April 18, 2003, this Court held a

*Markman* hearing in the patent litigation. On August 27, 2003, this Court issued a Claim Construction Order. That Order was highly critical of Dyno's proposed construction of disputed claim terms and adopted, in large part, LDE's proposed constructions. On February 19, 2004, realizing the difficulty in maintaining its suit, Dyno entered into a stipulated judgment of non-infringement, which preserved Dyno's right to appeal.

Subsequently, on May 5, 2004, LDE filed a civil action against Dyno alleging two counts: (1) violation of [§ 2](#) of the Sherman Act ([15 U.S.C. § 2](#)); and (2) intentional interference with contract and prospective contractual relations. LDE argues that Dyno's patent infringement case was frivolous, and was an attempt to monopolize the explosives market.

LDE alleges that its introduction of the "SoftLoad" explosive to the explosives market threatened Dyno's market share of explosive products marketed to mines in the U.S. market. LDE asserts that Dyno cooked up the patent infringement litigation in an attempt to forestall LDE from bringing *Soft Load* to the market before Dyno could offer a comparable product. In support of this [\*3] allegation LDE recounts its successful test shot on April 11, 2002, of *Soft Load* at Peabody Energy's Black Thunder mine located near Gillette, Wyoming. LDE alleges that several Dyno employees witnessed the test blast, and in response drafted a confidential memorandum outlining their observations. LDE contends that this successful test was the catalyst for Dyno's patent infringement litigation.

LDE also alleges that Dyno intentionally contacted present and potential clients of LDE in an effort to discourage them from doing business with LDE in light of the then pending patent infringement litigation. LDE further alleges that Dyno contacted businesses with whom LDE had potential contractual relationships and a reasonable expectation of business advantages. LDE contends that due to Dyno's contacts, certain businesses stopped purchasing products from LDE, or did not continue, or enter into prospective, business relationships with LDE.

On July 7, 2004, this Court entered a final judgment in favor of LDE in the underlying patent infringement litigation, putting that case in a procedurally appealable posture. On that same day Dyno, served its notice of appeal in the patent litigation.

On July [\*4] 30, 2004, Dyno moved for summary judgment of LDE's claims, or in the alternative, a stay pending the outcome of its appeal of the patent litigation. Dyno argues that LDE has failed to satisfy the first prong of the "sham" litigation test--specifically that there was no probable cause to bring the suit in the first place.

LDE asserts that Dyno's summary judgment motion is premature because discovery has not been completed and Dyno has not provided any discovery regarding the second prong of a sham litigation suit--specifically Dyno's subjective intent in bringing the patent litigation. LDE further claims that there are no facts in the record concerning the reasonableness of Dyno's patent litigation, specifically: (1) the extent of Dyno's pre-filing knowledge of the prosecution history and prior art; (2) the extent of Dyno's pre-filing knowledge of LDE's product; (3) the scope of Dyno's pre-filing testing of LDE's product; or (4) whether Dyno received information and documents from third parties concerning its patent and LDE's product before it filed suit against LDE.

On November 1, 2004, this Court entered an order which stayed the instant case pending resolution of Dyno Nobel's appeal [\*5] in the Federal Circuit. Subsequently, the Federal Circuit dismissed the appeal, and on April 18, 2005 this Court ordered that the instant case be restored to the active docket. The Defendant's motion for summary judgment is now ripe for review.

## II. Standard of Review

Summary judgment is proper when there is no genuine issue of material fact to be resolved at trial. [Fed. R. Civ. P. 56\(c\)](#); [Nebraska v. Wyoming, 507 U.S. 584, 590, 113 S. Ct. 1689, 123 L. Ed. 2d 317 \(1993\)](#). Thus, a district court may grant summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to a judgment as a matter of law." [Fed. R. Civ. P. 56\(c\)](#); [Nelson v. Geringer, 295 F.3d 1082, 1086 \(10th Cir. 2002\)](#).

2002). "An issue of material fact is genuine where a reasonable jury could return a verdict for the party opposing summary judgment." Seymore v. Shawver & Sons, Inc., 111 F.3d 794, 797 (10th Cir. 1997).

In applying these standards, the district court will view the evidence in the light most favorable to the party opposing summary judgment. Jenkins v. Wood, 81 F.3d 988, 990 (10th Cir. 1996). The movant bears the initial burden of demonstrating the absence of evidence to support the non-moving party's claims. Celotex Corp. v. Catrett, 477 U.S. 317, 325, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986). When the non-moving party bears the burden of proof at trial, the burden then shifts to it to demonstrate the existence of an essential element [\*6] of its case. *Id.* To carry this burden, the non-moving party must go beyond the pleadings and designate specific facts to show there is a genuine issue for trial. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 251, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986); Ford v. West, 222 F.3d 767, 774 (10th Cir. 2000). The mere existence of a scintilla of evidence in support of the non-moving party's position is insufficient to create a "genuine" issue of disputed fact. Lawmaster v. Ward, 125 F.3d 1341, 1347 (10th Cir. 1997).

### III. Analysis

#### LDE's SHERMAN ACT CLAIM

LDE contends that Dyno has enlisted the courts, through the patent infringement litigation, to harass and stall the introduction of its SoftLoad product into the market. LDE argues that Dyno adopted objectively baseless and unreasonable interpretations of the claims in the '950 patent. LDE argues that Dyno's proposed interpretation of the '950 patent made the claims nonsensical, internally inconsistent and ignored the plain meaning of the words used in the claims. LDE relies heavily on this Court's Claim Construction, and its adoption of many of LDE's interpretations. LDE also points out that Dyno must have been aware all along that its interpretations were unreasonable and baseless, because Dyno did not appeal the findings in the Claim Construction. In essence, LDE claims that Dyno filed the patent infringement litigation in an effort to impose collateral, [\*7] anti-competitive injury rather than to obtain justifiable legal remedy. Specifically, LDE claims that Dyno filed the infringement litigation in an effort to impose collateral, anti-competitive injury rather than a justifiable legal remedy. LDE argues that Dyno's behavior is a violation of Section 2 of the Sherman Act.<sup>1</sup>

Dyno counters by arguing that it is immune from suit by virtue of the *Noerr Pennington* doctrine. Dyno further argues that the underlying suit was not objectively baseless.

#### A. The *Noerr-Pennington* Doctrine

The *Noerr-Pennington* immunity shields those who petition the government from antitrust liability. See Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127 (1961); accord Mine Workers v. Pennington, 381 U.S. 657, 669, 85 S. Ct. 1585, 14 L. Ed. 2d 626 (1965). Although the *Noer-Pennington* doctrine was created to immunize petitioning of administrative and legislative officials, the Court extended the immunity to "the approach of citizens ... to [the] courts." California Motor Transport Co. v. Trucking Unlimited, 404 U.S. 508, 510, 92 S. Ct. 609, 30 L. Ed. 2d 642 (1972); see also McGuire Oil Co. v. Mapco, Inc., 958 F.2d 1552, 1558-59 (11th Cir. 1992).

Under the *Noerr-Pennington* doctrine, private citizens may exercise their First Amendment rights to petition the government with immunity from antitrust liability. See Baltimore Scrap Corp. v. David Joseph Co., 237 F.3d 394,

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<sup>1</sup> Section 2 of the Sherman Act, 15 U.S.C. § 2, prohibits monopolization or attempts to monopolize: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a felony. . . ."

[398 \(4th Cir. 2001\)](#) (citing [Noerr, 365 U.S. at 136-39](#) and [Pennington, 381 U.S. at 669](#)). The Noerr Court emphasized that it is "neither unusual nor illegal for people to seek action on laws in the hope that they may bring about an advantage to themselves and a disadvantage to their [\*8] competitors . . ." [Noerr, 365 U.S. at 139](#).

## B. The Sham Exception

However, the Supreme Court suggested that the *Noerr-Pennington* immunity did not extend to "sham" activities. [Noerr, 365 U.S. at 144](#).<sup>2</sup> The Court did not extend immunity to suits that were "mere sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of a competitor." *Id.* In the patent context, the Federal Circuit held:

A patentee who brings an infringement suit may be subject to antitrust liability for the anti-competitive effects of that suit if the alleged infringer (the antitrust plaintiff) proves . . . that the infringement suit was a mere sham to cover what is actually nothing more than an attempt to interfere directly with the business relationships of a competitor . . . .

[Nobelpharma AB v. Implant Innovations, 141 F.3d 1059, 1068 \(Fed. Cir. 1998\)](#)(citations omitted).

In the present case LDE alleges that Dyno instituted a sham litigation, and should not enjoy *Noerr-Pennington* immunity.

What the term "sham" meant was squarely addressed by the Supreme Court in [Professional Real Estate Investors, Inc., v. Columbia Picture Industries, Inc.\(PRE\), 508 U.S. 49 \(1993\)](#); see also [Handgards, Inc. v. Ethicon, Inc., 601 F.2d 986 \(9th Cir. 1979\)](#) (addressing sham litigation in the patent context), cert. denied, 444 U.S. 1025 (1980). In PRE, the Court announced a two part test to determine whether a litigant had approached the courts with a sham allegation [\*9] holding:

First, the lawsuit must be objectively baseless in the sense that no reasonable litigant could realistically expect success on the merits. If an objective litigant could conclude that the suit is reasonably calculated to elicit a favorable outcome, the suit is immunized under *Noerr*, and an antitrust claim premised on the sham exception must fail. Only if challenged litigation is objectively meritless may a court examine the litigant's subjective motivation. Under this second part of our definition of sham, the court should focus on whether the baseless lawsuit conceals "an attempt to interfere directly with the business relationships of a competitor," through the "use [of] the governmental process -- as opposed to the outcome of that process -- as an anticompetitive weapon." This two-tiered process requires the plaintiff to disprove the challenged lawsuit's legal viability before the court will entertain evidence of the suit's economic viability. Of course, even a plaintiff who defeats the defendant's claim to *Noerr* immunity by demonstrating both the objective and the subjective components of a sham must still prove a substantive antitrust violation. Proof of a sham merely [\*10] deprives the defendant of immunity; it does not relieve the plaintiff of the obligation to establish all other elements of his claim.

*PRE*, 508 U.S. at 60-61 (internal citations omitted).

Under Federal Circuit precedent, which governs "all antitrust claims premised on the bringing of a patent infringement suit," plaintiffs must first establish the objective prong of the sham definition by clear and convincing evidence. See [Nobelpharma, 141 F.3d at 1069](#) and 1064. To establish that a lawsuit is objectively baseless, plaintiffs must prove that the purported sham litigation was "so baseless that no reasonable litigant could realistically expect to secure favorable relief." *PRE*, 508 U.S. at 62; see also [Mitek Surgical Products, Inc. v. Arthrex, Inc., 21 F. Supp. 2d 1309, 1318 \(D. Utah 1998\)](#). Furthermore, the Tenth Circuit has characterized the sham

<sup>2</sup> There is also an exception to the *Noerr-Pennington* immunity for litigation based on patents that are procured by fraud. See [Walker Process Inc. v. Food Machinery & Chemical Corp., 382 U.S. 172, 86 S. Ct. 347, 15 L. Ed. 2d 247 \(1965\)](#). This exception does not apply to the instant case.

exception to *Noerr-Pennington* immunity as "narrow." See [\*Bright v. Moss Ambulance Service, Inc.\*, 824 F.2d 819, 823 \(10th Cir. 1987\)](#).

Refining the concept of the objective prong of the sham litigation test, the Court posited that the doctrine of probable cause should guide courts in their analysis, stating: "Probable cause to institute civil proceedings requires no more than a 'reasonable belief that there is a chance that [a] claim may be held valid upon adjudication.'" *PRE*, 508 U.S. at 63 (quoting [\*Hubbard v. Beatty & Hyde, Inc.\*, 343 Mass. 258, 262, 178 N.E.2d 485 \(1961\)](#)). The Court also held that, "because the absence of probable cause is an essential element of the tort, [\*11] the existence of probable cause is an absolute defense." *PRE*, 508 U.S. at 63. If a suit is not objectively baseless, an antitrust defendant's subjective motivation for bringing suit is immaterial. [\*Nobelpharma\*, 141 F.3d at 1072](#).

From the outset of our analysis we note that it is the province of the court to determine, as a matter of law, whether probable cause existed in Dyno's patent litigation. *PRE*, 508 U.S. at 63 (citations omitted); see also [\*Director General of Railroads v. Kastenbaum\*, 263 U.S. 25, 28, 44 S. Ct. 52, 68 L. Ed. 146 \(1923\)](#) ("The question is not whether [the defendant] thought the facts to constitute probable cause, but whether the court thinks they did."). Moreover, the objective prong underlying the probable cause determination is a legal question to be determined by the Court. See [\*McGuire Oil\*, 958 F.2d at 1561 n.12](#) (quoting [\*Columbia Pictures Industries, Inc. v. Professional Real Estate Investors, Inc.\*, 944 F.2d 1525, 1532 \(9th Cir. 1991\)](#)); see also [\*In Re: Terazosin Hydrochloride Antitrust Litigation\*, 335 F.Supp. 2d 1336, 1356 \(S.D. Fla. 2004\)](#). Whether there was an objectively reasonable basis to bring suit is a proper determination at summary judgment.

## **1. The Temporal Aspect to Determining Probable Cause and Objective Baselessness: The Whole Record v. Date of Complaint**

The parties, however, argue contrary positions regarding the appropriate temporal context in which to determine whether a plaintiff had the requisite probable cause to bring suit. LDE argues that a determination of probable cause should not encompass information discovered subsequent to the filing [\*12] of the underlying Patent Litigation. LDE stakes out the position, both in its briefs and at oral argument, that the cutoff date for determining probable cause is the date of filing of the underlying patent litigation. Moreover, as discussed below, LDE petitions this Court for leave to engage in further discovery beyond that of the underlying Patent Litigation to determine the state of Dyno's knowledge at the time of filing. Dyno counters by arguing that this Court, at a minimum need only consult the record of the previously filed and decided Patent Litigation. Dyno contends that this Court need only consult the patent, the patent history and the alleged offending product to determine whether the underlying Patent Litigation was a sham. The answer lies somewhere in between.

### a. *In Re Relafen*

In the intervening time between the stay and the Federal Circuit's dismissal of Dyno's appeal, the District of Massachusetts faced a similar case. In [\*In Re Relafen Antitrust Litigation\*, 346 F.Supp. 2d 349 \(D. Mass. 2005\)](#), the defendant asserted that all of plaintiffs' claims were barred by the *Noerr-Pennington* doctrine.<sup>3</sup> The court examined the doctrine, including the exceptions, commonly known as the sham exception and the Walker Process exception, to determine if [\*13] the defendant's assertion possessed merit. LDE argues that *Relafen* held that an antitrust defendant's pre-filing knowledge was material to a determination of whether probable cause existed.

In *Relafen*, the court denied the defendant's motion for summary judgment, holding that "the facts tending to establish the existence or want of existence of probable cause were disputed." [\*Id. at 361\*](#) (citation omitted). The court cited the defendant's pre-filing knowledge at the time of filing. *Id.* The court went on to find that whether the defendant had the requisite probable cause became an issue that was best submitted to a jury. [\*Id. at 362\*](#). The court ultimately declined to rule on the objective baselessness of the underlying suit as a matter of law. *Id.*

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<sup>3</sup> Obviously this decision has no binding effect on this Court, and is consulted in an effort to flesh out a cogent analysis.

Here the underlying facts of the Patent Litigation are not in dispute. The patent, the patent history and the alleged infringing product were, and are, known quantities. Further, this Court's *Markman* analysis is also known--as are the arguments made during that process by both parties. In *Relafen* disputed facts remained undecided from the underlying infringement case specifically, whether the patent could have been anticipated. The unresolved question of fact remained [\*14] namely, whether a chemist of ordinary skill could have anticipated the patented product from a published source. *Relafen*, 346 F.Supp. 2d at 354-55. This disputed fact became the key fact in determining whether the infringement case was objectively baseless. Here the underlying Patent Litigation rested on claim interpretation, not on the validity of the patent itself.

Moreover, in *Relafen* the court did not separate its analysis between objective baselessness and subjective baselessness. Instead, the court dodged the objective prong and delved into the disputed nature of the defendant's knowledge. This discussion by the *Relafen* court was, in the Court's opinion, premature and does not comport with the standards enunciated in *PRE*. For example, the *Relafen* court stated:

in light of the disputed factual issues, the parties had not established the existence or want of probable cause as matter of law. Nor had [the defendant], whose submissions and oral argument focused solely on the first, objective prong of the sham exception, made the necessary showing that there were no trialworthy issues with respect to the second, subjective prong.

*In Re Relafen*, 346 F.Supp. 2d at 364.

Such a statement is problematic on several levels. First, it is well established that [\*15] the plaintiff in the antitrust action must prove the objective baselessness of the underlying suit. The *Relafen* court seemed to turn the burden on its head and place the burden of showing probable cause on the defendant.<sup>4</sup> Furthermore, the court did not examine, as a matter of law, the underlying suit and whether it was objectively baseless. Instead, the court subjected the defendant with the burden to show that there were no trialworthy issues "with respect to the second, subjective prong." *Id.* Whether or not there exists "trialworthy" issues regarding the subjective baselessness of the suit skips the first prong altogether.

Although it is true that the court in *Relafen* declined to rule as to whether there existed probable cause as a matter of law, it did not foreclose that argument altogether as suggested by the Plaintiff. In fact, the court noted that finding probable cause, and thus ruling on the objective baselessness of the underlying suit as a matter of law was "appropriate" as a "general matter," noting that the "specific circumstances . . . compelled a different conclusion." *Relafen*, 346 at 362. Those specific circumstances, as described by the court, regarded a disputed [\*16] factual issue--namely the defendant's reliance on company scientists.<sup>5</sup> In the instant case, it cannot be said that there is a dispute over the predicate facts of the underlying legal proceeding. See *PRE*, 508 U.S. at 64. The instant case has been through a *Markman* hearing and an appeal--no issues of material fact remain at issue. LDE has failed to show that a material fact remains from the Patent Litigation that would effect a determination of whether there was probable cause to bring suit.

In essence, LDE's argument regarding the time probable cause should be determined is a red herring. What LDE really desires is to reopen the discovery in the underlying suit--a necessary byproduct of determining the objective

<sup>4</sup> The *Relafen* court states: "a court may, in the course of resolving the underlying litigation, make findings tantamount to a finding that the [litigant's conduct] was objectively baseless, Judge Lindsay's findings were not clearly and convincingly of this sort. Judge Lindsay's findings did not, for example, describe conduct that was indefensible on its face. Rather, Judge Lindsay discredited SmithKline's claims only after the careful testing of trial." *In Re Relafen*, 346 F.Supp. 2d at 364. This seems to suggest that the trial court sitting for the underlying litigation must show, through its opinions and memorandum, that the suit is objectively baseless by clear and convincing evidence--or alternatively--that a plaintiff can rely on a trial court's findings in the underlying suit if they are clear and convincing. This too confuses what should be a straightforward analysis of the objective merits of the underlying patent litigation. An analysis which puts the burden squarely on the plaintiff.

<sup>5</sup> The defendant in *Relafen* relied heavily on the fact that it had survived summary judgment in the underlying patent infringement litigation to demonstrate that the suit was not objectively baseless. The court rejected their argument.

reasonableness at the time of filing. The real question is whether the underlying suit left disputed facts that would tend to establish, or not establish, probable cause. This then forms the basis for when a determination of probable cause should be made. Namely, probable cause is determined by the whole record below in the underlying case. See, e.g., [Covad Comm. Co. et al. v. Bell Atlantic Corp. et al.](#), 398 F.3d 666, 677, 365 U.S. App. D.C. 78 (D.C. Cir. 2005) (determining the PRE objective prong by examining the record of the underlying suit); *C.R. Bard*, 157 F.3d at 1369 (examining the "totality of evidence of sham litigation"); [\*17] [Amarel v. Connell](#), 102 F.3d 1494 (9th Cir. 1996) (examining the record of the underlying suits to determine objective baselessness).<sup>6</sup> Such an analysis keeps the objective prong objective by forcing the reviewing court to focus on the case and the suit, opposed to delving into a plaintiff's pre-filing knowledge and therefore its subjective motivations prematurely. With this in mind the Court now turns to the record of the Patent Litigation to determine whether LDE has shown by clear and convincing evidence that the underlying suit was objectively baseless.

### **C. Analysis of Dyno's Immunity Under *Noerr-Pennington***

We find that LDE has not established, by clear and convincing evidence, that Dyno's underlying patent litigation, given the totality of the circumstances, was objectively baseless. See PRE, 508 U.S. at 61. Indeed, the record of the litigation below, clearly demonstrates otherwise.

The underlying Claim Construction Order, which favored LDE, was not as clear cut as LDE has alleged. But for the placement of a single comma in the specification, the Claim Construction Order may very well have fallen the other way. As this Court noted in the Claim Construction Order:

The Court's interpretation is supported by the principles of normal English language [\*18] usage. When two adjectives precede a noun and the adjectives are not separated by a comma, the first adjective modifies the combined idea of the second adjective plus the noun. Thus, the noun in the phrase "fibrous vegetable protein additive" is "additive." "Fibrous vegetable protein" are adjectives that describe what type of additive is required. Furthermore, "additive," used as a noun, is defined as "a substance added in small amounts to something else to improve, strengthen, or otherwise alter it." Thus, according to the ordinary meaning of the words and the patentee's choice of phrasing, Claim 1 requires the use of "an additive," described as fibrous vegetable protein in nature; that is "added . . . to something else," here, the bulking agent.

Furthermore, a Claim Construction Order is a product of litigation that takes hundreds, if not thousands, of pages of briefs, memoranda and motions to determine. See [Q-Pharma v. The Andrew Jergens Company](#), 360 F.3d 1295 (Fed. Cir. 2004) ("Claim interpretation is not always an exact science, and it is not unusual for parties to offer competing definitions of even the simplest claim language."). Legislation, sausage making and Claim Construction seem to share similar traits. For LDE to assert that the construction [\*19] of the claim in the underlying patent litigation was clear from its face, and Dyno's interpretation per se baseless simply misstates the complexity of the *Markman* process. As long as the interpretations follow the standard canons of claim construction and are reasonably supported by intrinsic evidence, they are not baseless. See *id.*

Although not dispositive, the fact that Dyno did not engage in a pattern of litigation is relevant to the Court's decision. See PRE, 508 U.S. at 69-70 (Stevens, J. concurring); see also [Colorado Petrol. Marketers Assn. v. Southland Corp.](#), 476 F.Supp. 373 (D. Colo. 1979) ("pattern" of baseless suits unnecessary but probative). The Court notes that LDE only asserts that the Patent Litigation, which comprised but a single suit, violated the Sherman Antitrust Act. However, the Tenth Circuit has suggested that a single case, even if filed without probable cause and with anticompetitive intent, would not rise to the standard set by the Supreme Court in [California Motor Transport. Hydra-Tech Corp. et al. v. Sundstrand Corp.](#), 673 F.2d 1171, 1176-77 (10th Cir. 1982). The Court in *Hydro-Tech* indicated that to state a claim under Section Two of the Sherman Act the suit would have to rise to the category of an abuse of the judicial process, e.g. perjury, use of a patent obtained by fraud to exclude a competitor

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<sup>6</sup> Even cases prior to PRE examined the whole record of the underlying suit to determine whether it was a sham. See, e.g., [Coastal States Marketing, Inc. v. Hunt](#), 694 F.2d 1358, 1359 (5th Cir. 1983).

from the market, bribery, conspiracy with a licensing official, and a [\*20] pattern of baseless, repetitive claims. *Id.* at n.6 (citing [California Motor Trans., 404 U.S. at 508, 512-513](#)). Indeed, it is difficult to find a single case that would apply the sham exception under these particular circumstances and facts.

#### D. LDE's [Rule 56\(f\)](#) Petition

LDE argues that the court does not have enough evidence before it to make a finding of probable cause, insofar as the Dyno patent litigation is concerned. LDE also argues that Dyno's summary judgment motion is premature due to a lack of discovery on the issues. See [Fed. R. Civ. P. 56\(f\)](#). In its [Rule 56\(f\)](#) affidavit, LDE alleges that the following facts are essential to oppose Dyno's summary judgment motion:

(1) Dyno's pre-filing investigation (including the scope of its pre-filing claim interpretation and infringement analysis); (2) Dyno's knowledge of the prosecution history and prior art; (3) Dyno's knowledge of LDE's product; (4) Dyno's testing of LDE's product; (5) information and documents Dyno received from third parties concerning the patent and LDE's product; (6) admissions concerning Dyno's interpretation of its patent; (7) admissions concerning LDE's noninfringement of Dyno's patent; and (8) admissions concerning the scope of Dyno's patent.

A [Rule 56\(f\)](#) applicant is entitled to relief only if he or she shows, among [\*21] other things, that the discovery would uncover specific facts which would preclude summary judgment. [Maljack Prods. v. Goodtimes Home Video Corp., 81 F.3d 881, 888 \(9th Cir. 1996\)](#); see also [United States v. Smithfield Foods, Inc., 969 F. Supp. 975 \(E.D. Va. 1997\)](#) (denying a [Rule 56\(f\)](#) motion because additional discovery would not be dispositive to court's granting of summary judgment).

In *Q-Pharma*, the Federal Circuit Court of Appeals was faced with a similar argument. In that case Q-Pharma brought a civil action against Jergens alleging patent infringement of its '373 patent. After discovery, Q-Pharma voluntarily dismissed its patent infringement claim. Jergens then brought several counter-claims, including allegations that Q-Pharma's suit violated the Sherman Anti-Trust Act. The district court granted summary judgment in favor of Q-Pharma on Jergens' Sherman Act claim. Jergens appealed the judgment alleging that the district court did not allow enough time for discovery, and that, on the merits, Q-Pharma's underlying patent infringement suit was baseless. The Federal Circuit affirmed the district court's ruling.

In affirming, the Federal Circuit found that there was enough evidence to support a finding that Q-Pharma had probable cause to bring the patent infringement suit. The Federal Circuit held: "a reasonable litigant could--based on the '373 patent, its prosecution [\*22] history, and Jergens' advertising and labeling statements touting the therapeutic effects of the Curet (R) CoQ[10] lotion--expect to prevail on a claim alleging infringement." [Q-Pharma, 360 F.3d at 1305](#). The court also affirmed the district court's decision not to allow more discovery, holding:

Jergens' proposed discovery would only have been relevant to Q-Pharma's *subjective motivation* and therefore would not have altered the court's determination--based on the patent, its prosecution history, and Jergens' advertising and labeling statements made in regard to the accused product--that Q-Pharma's infringement claim was not objectively baseless.

*Id. at 1306* (emphasis added) (internal quotations omitted).

The Court finds the Federal Circuit's language in this case highly persuasive on several points. First, the Federal Circuit affirmed a finding of probable cause on the basis of the patent, its prosecution history, and the defendant's advertising and labeling statements. Nowhere in that list is Q-Pharma's subjective investigation into the actual merits of the suit, nor of the defendant's knowledge at the time of the suit. The Federal Circuit expressly turned down Jergen's invitation to dig deeper into the Q-Pharma's subjective [\*23] intent to simply determine whether probable cause existed.

In the instant case, LDE, in its [Rule 56\(f\)](#) affidavit, complains that the court does not have enough evidence to make a finding in favor of Dyno. The Court disagrees. The evidence sought by LDE would only pertain to the subjective

prong of the *PRE* test. Notably, LDE submits that the court needs: "Dyno's pre-filing investigation . . . Dyno's knowledge of prosecution history . . . prior art . . . LDE's product . . . Dyno's testing of LDE's product . . . information and documents Dyno received from third parties...[Dyno's] admissions concerning Dyno's interpretation of its patent . . . [Dyno's] admissions concerning LDE's noninfringement of Dyno's patent . . . [Dyno's] admissions concerning the scope of Dyno's patent." Each and every one of these requests regards Dyno's subjective motivation for bringing the underlying patent litigation. Evaluating Dyno's subjective motivation for bringing the patent litigation is only proper *after* a finding that the suit was objectively baseless. See *PRE*, 508 U.S. at 60 ("Only if challenged litigation is objectively meritless may a court examine the litigant's subjective motivation."). Additional evidence that would only [\*24] be applicable to the subjective prong would be unhelpful in our analysis and would not defeat a finding of summary judgment in this case.

Moreover, Dyno, in its memorandum in support of its claim interpretation, attached to its motion for summary judgment as exhibit 2, discusses the reasons and analysis of the '950 patent at issue. There Dyno related the intrinsic evidence, the extrinsic evidence and the relevant prosecution history. We are persuaded that this conforms with the standard set out in *Q-Pharma*. Furthermore, here, unlike in *Q-Pharma*, this Court held a *Markman* hearing to determine the claim construction. Contrast that with *Q-Pharma*, where the plaintiff voluntarily dismissed before a *Markman* hearing was held. To establish that a suit is objectively baseless is, necessarily, a high hurdle. If this hurdle were not placed as high as it was, any patentee would be chilled from protecting her valuable patent rights—a situation that would render a patent monopoly illusory.

The Court notes that a patentee has a strong interest in preserving the monopoly rights granted through the patent statutes and regulations. So great is this interest that a patentee is within her rights to enforce that monopoly [\*25] right to its outer fringes. It would be inconsistent to grant a patent monopoly, but hamstring the patentee by punishing enforcement actions. As the Federal Circuit observed:

Since the principal purpose of the patent system is to provide innovators with a property right upon which investment and other commercial commitments can be made, absent the *PRE* criteria the patentee must have the right of enforcement of a duly granted patent, unencumbered by punitive consequences should the patent's validity or infringement not survive litigation.

*C.R. Bard, Inc. v. M3 Systems, Inc.*, 157 F.3d 1340, 1369 (Fed. Cir. 1998) (citation omitted). It is clear from the evidence presented that Dyno's underlying patent infringement suit was not objectively baseless, and thus should enjoy the protections provided by *Noerr-Pennington*.

## **LDE'S CLAIMS OF INTENTIONAL INTERFERENCE WITH CONTRACT AND PROSPECTIVE CONTRACTUAL RELATIONS**

LDE also contends that Dyno intentionally interfered with prospective contractual relations and even interfered with existing contractual relations. LDE points out two specific instances where it alleges that Dyno's patent litigation intentionally and inappropriately interfered. LDE claims that discussions with Peabody Energy regarding the [\*26] expansion of *Soft Load* into other mines in the U.S. tortuously interfered with its contracts. Additionally, LDE contends that a joint venture agreement with Wesco were similarly halted due to the Dyno patent litigation. LDE alleges that Dyno contacted these and other LDE customers and encouraged them not to do business with LDE. Based on these allegations, LDE has alleged the tort of intentional interference with contract and prospective contractual relations.

A determination whether LDE's tort claims survive summary judgment is less clear than the Sherman Act Claim. LDE claims that Dyno contacted businesses that LDE had contractual, and potential contractual, relationships with to relate that components and services offered by LDE infringed Dyno's '950 patent. LDE alleges that these contacts were tortious because the underlying claim of infringement was objectively baseless and no reasonable litigant could have expected success.

### A. Cardtoons

One issue is whether the *Noerr-Pennington* immunity applies to LDE's claims which are not premised on the Sherman Act. In *Cardtoons, L. C., v. Major League Baseball Players Association*, 208 F.3d 885 (10th Cir. 2000), the Tenth Circuit held that the *Noerr-Pennington* [\*27] immunity did not apply outside of the Sherman Act. *Cardtoons, 208 F.3d at 893*. In *Cardtoons*, the Major League Baseball Players Association (MLBPA) sent a letter with a thinly veiled threat of litigation to Champs, a baseball card printer. The letter referenced color parody drawings of active members of the MLBPA, produced by Cardtoons, that Champs had contracted to print and market. MLBPA threatened to sue over "violating the valuable property rights of MLBPA and the players." *Id. at 886*. Champs, upon receiving the "cease and desist" letter, informed Cardtoons that it intended to stop printing the cards. Cardtoons immediately filed suit against MLBPA for tortious interference with the Champs contract. After successful litigation which declared that Cardtoons had a *First Amendment* right to print the parody cards, it returned to district court to pursue damages -all of Cardtoons claims stemmed from the allegations contained in the letter MLBPA sent to Champs. MLBPA defended, claiming that it was immune from liability under *Noerr-Pennington*. The district court agreed and entered summary judgment in favor of MLBPA. The Tenth Circuit reversed en banc.<sup>7</sup>

The Tenth Circuit [\*28] examined the underpinnings of the *Noerr-Pennington* immunity. The *Cardtoons* court held that the *Noerr-Pennington* immunity was based on two grounds, a statutory interpretation of the Sherman Act, and on the *First Amendment* right to petition. See *Cardtoons*, 208 F.3d at 888. The court held that outside of the Antitrust context, the first rationale does not apply. Similarly, the court found in the case of communications made between private individuals the second rationale does not hold, because no petition was made to the government, thus the *First Amendment* was not implicated.

The present case is highly distinguishable from *Cardtoons*. In this case, unlike *Cardtoons*, the threats of litigation were made pursuant to actual litigation-a distinction drawn by the Tenth Circuit itself in *Cardtoons*.<sup>8</sup> The Court cannot say that the threats made by Dyno were not concurrent with an actual petition to the government for redress, nor can the Court assert that the *First Amendment* right to petition was not implicated. Furthermore, the tort claims in the present case cannot be read independently of the antitrust claims. The two claims rely on whether the underlying patent litigation was objectively baseless. The Tenth Circuit also noted that pre-litigation threats in the antitrust [\*29] context grant immunity "under a construction of the Sherman Act, not the right to petition." *Id. at 892*. In the instant case the Court is presented with pre-litigation threats that matured into a petition to the courts for redress, which spawned an action under the Sherman Act. Therefore, the limitations on the *Noerr-Pennington* immunity, discussed in *Cardtoons*, do not control the present case.

As the Court observed above regarding the intertwined character of the tort claim and the antitrust claim, the Court cannot discount the fact that the entire case is brought in the patent context. Therefore, the better analysis of LDE's

<sup>7</sup> A Tenth Circuit panel of judges affirmed the district court's finding. However, Judge Ebel, in a prescient dissent disagreed with the panel. Judge Ebel questioned whether it was appropriate to extend *Noerr-Pennington* immunity to purely private threats of litigation. Judge Ebel offered a three-part test to determine whether private litigation threats should receive immunity under *Noerr-Pennington*. Under that test a litigant seeking *Noerr-Pennington* immunity would have to show that the threat was: (1) made in good faith; (2) was objectively reasonable; and (3) was a "proximate prologue to actual or imminent litigation." 182 F.3d at 1142. In the present case, Dyno would be able to establish, under our ruling today, all three of these elements. First, there is a presumption that patent infringement litigation is brought in good faith. See *C.R. Bard, Inc. v. M3 Systems, Inc.*, 157 F.3d 1340, 1369 (Fed. Cir. 1998) (citing *Virtue v. Creamery Package Mfg. Co.*, 227 U.S. 37-38, 33 S. Ct. 202, 57 L. Ed. 393, 1913 Dec. Comm'r Pat. 519 (1913)). Such a presumption is only overcome by affirmative evidence of bad faith. Here there has been no showing by LDE that Dyno's Patent Litigation was brought in bad faith. Second, as discussed at length, this Court feels that the underlying patent litigation was not objectively baseless. The Court assumes that an objectively reasonable standard would be substantially similar. Third, the threats of litigation were a "proximate prologue to actual or imminent litigation."

<sup>8</sup> "We hold . . . that because there was no petition of the government in the present case, the issue of immunity collapses into the issue of state law liability." *Cardtoons*, 208 F.3d at 893.

tort claims, and Dyno's potential liability, comes from [\*Globetrotter Software Inc. v. Elan Computer Group, Inc.\*, 362 F.3d 1367 \(Fed. Cir. 2004\)](#).

## B. *Globetrotters*

In *Globetrotters*, the defendant in a patent infringement case brought state-law tort counter-claims for tortious interference with prospective economic advantage and unfair competition against the plaintiff patentee. These claims were premised on the patentee's communications, via e-mail and letters, sent to the distributor of the defendant's allegedly infringing software. The Federal Circuit, held that the communications would be protected if they were made in good faith: "We have...adopted a similar [\*30] standard [as the other circuits] for pre-litigation communications alleging patent infringement holding that bad faith is not supported when the information [contained in the pre-litigation communication] is objectively accurate." [\*Globetrotters\*, 362 F.3d at 1377](#) (quoting [\*Golan v. Pingel Enter., Inc.\*, 310 F.3d 1360, 1371 \(Fed. Cir. 2002\)](#) (internal quotation marks omitted)). The court premised its holding on two rationales, namely, federal preemption and the [\*First Amendment\*](#) right to petition. [\*Globetrotters\*, 362 F.3d at 1377](#). The court held as follows:

The federal patent laws preempt state laws that impose tort liability for a patentholder's good faith conduct in communications asserting infringement of its patent and warning about potential litigation. In addition, the same [\*First Amendment\*](#) policy reasons that justify the extension of *Noerr* immunity to pre-litigation conduct in the context of federal [\*antitrust law\*](#) apply equally in the context of state-law tort claims.

*Id.*

Thus, the Federal Circuit applied *PRE*'s objectively baseless standard to pre-litigation communications alleging patent infringement. *Id.* Therefore, "a plaintiff claiming that a patent holder has engaged in a wrongful conduct by asserting claims of patent infringement must establish that the claims of infringement were objectively baseless." *Id.*

Here, as discussed above, the Court [\*31] found that Dyno's claims of patent infringement were not objectively baseless and thus, LDE's tort claims, under the *Globetrotter* '\$ standard, are properly dismissed.

The Court further notes that failure in the underlying case Patent Litigation, in a claim such as the one asserted by LDE, is not persuasive in a subsequent antitrust or tortious interference claim as the Supreme Court observed in *PRE*:

A winning lawsuit is by definition a reasonable effort at petitioning for redress and therefore not a sham. On the other hand, when the antitrust defendant has lost the underlying litigation, a court must resist the understandable temptation to engage in post hoc reasoning by concluding that an ultimately unsuccessful action must have been unreasonable or without foundation. The court must remember that even when the law or the facts appear questionable or unfavorable at the outset, a party may have an entirely reasonable ground for bringing suit.

*PRE*, 508 U.S. at 6 (internal quotations and citations omitted).

The Federal Circuit's ruling on Dyno's appeal in the patent infringement litigation does not, and should not, inform, or change, our decision in this case.

## IV. Conclusion

Therefore, because Dyno had probable [\*32] cause, meaning that it had an objectively reasonable belief in a chance of success to bring the underlying patent suit, the Court cannot say that this was a sham litigation. The Court further finds that the tort claims necessarily drop out because Dyno had a right to bring the underlying patent litigation. Thus, summary judgment should be granted for Dyno.

Dated this 13th day of September, 2005.

/s/ Alan B. Johnson

ALAN B. JOHNSON

UNITED STATES DISTRICT JUDGE

**ORDER GRANTING DEFENDANT'S MOTION FOR SUMMARY JUDGMENT**

For the reasons stated within this Court's Memorandum Opinion regarding defendant's Motion for Summary Judgment in the above-captioned matter, it is hereby

**ORDERED** that defendant Dyno Nobel's Motion for Summary Judgment shall be, and now is, **GRANTED**;

**ORDERED** that plaintiff LDE Corporation's Complaint in the above-captioned matter shall be, and now is, **DISMISSED** as to all claims with prejudice.

Dated this 13th day of September, 2005.

/s/ Alan B. Johnson

ALAN B. JOHNSON

UNITED STATES DISTRICT JUDGE

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## Texas v. Organon USA Inc. (In re Remeron End-Payor Antitrust Litig.)

United States District Court for the District of New Jersey

September 13, 2005, Decided ; September 13, 2005, Filed

Civil No. 02-2007 (FSH), Civil No. 04-5126 (FSH)

### **Reporter**

2005 U.S. Dist. LEXIS 27011 \*; 2005-2 Trade Cas. (CCH) P74,966

IN RE: REMERON END-PAYOR ANTITRUST LITIGATION; STATES AND COMMONWEALTHS OF TEXAS, et al., Plaintiffs, v. ORGANON USA INC. AND AKZO NOBEL N.V., Defendants.

**Prior History:** [In re Remeron Direct Purchaser Antitrust Litig., 367 F. Supp. 2d 675, 2005 U.S. Dist. LEXIS 7193 \(D.N.J., 2005\)](#)

[Walgreen Co. v. Organon, Inc. \(In re Remeron Antitrust Litig.\), 335 F. Supp. 2d 522, 2004 U.S. Dist. LEXIS 18364 \(D.N.J., 2004\)](#)

## **Core Terms**

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settlement, notice, End-Payor, Plaintiffs', class member, class action, consumers, antitrust, attorney's fees, damages, Defendants', purchasers, settlement fund, Generic, parties, patent, settlement agreement, expenses, cases, listing, risks, incentive award, Manufacturers, attorney general, depositions, opt-out, Payors, mailed, costs, negotiations

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

Civil Procedure > Settlements > Settlement Agreements

### [HN1](#) **Class Actions, Prerequisites for Class Action**

Under [Fed. R. Civ. P. 23](#), a court must engage in a two-step analysis in order to determine whether it should certify a class action for settlement purposes. First, the court must determine whether the plaintiffs have satisfied the prerequisites for maintaining a class action as set forth in [Fed. R. Civ. P. 23\(a\)](#). If the plaintiffs can satisfy these prerequisites, the court must then determine whether the alternative requirements of [Fed. R. Civ. P. 23\(b\)\(2\)](#) or [23\(b\)\(3\)](#) are met. [Fed. R. Civ. P. 23\(a\)](#), advisory committee's note.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

Civil Procedure > Settlements > Settlement Agreements

### [HN2](#) **Class Actions, Prerequisites for Class Action**

Confronted with a request for settlement-only class certification, a district court need not inquire whether the case, if tried, would present intractable management problems, [Fed. R. Civ. P. 23\(b\)\(3\)\(D\)](#), for the proposal is that there be no trial.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN3](#) **Class Actions, Prerequisites for Class Action**

[Fed. R. Civ. P. 23\(a\)](#) provides that class members may maintain a class action as representatives of a class if they show a court that: (1) the class members are so numerous that joinder of all members is impracticable; (2) the action addresses questions of law or fact common to the class; (3) the claims or defenses of the class representatives are typical of the claims or defenses of the class; and (4) the class representative parties will fairly and adequately protect the interests of the class.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

Civil Procedure > Special Proceedings > Class Actions > Judicial Discretion

#### [HN4](#) **Class Actions, Prerequisites for Class Action**

Courts will ordinarily discharge the prerequisite of numerosity in a class action if a class is so large that joinder of all members is impracticable. The plaintiff need not precisely enumerate the potential size of the proposed class, nor is the plaintiff required to demonstrate that joinder would be impossible. Moreover, it is proper for the court to accept common sense assumptions in order to support a finding of numerosity.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN5](#) **Class Actions, Prerequisites for Class Action**

Numbers in excess of 40, particularly those exceeding 100 or 1,000 have sustained the numerosity requirement for a class action.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN6](#) **Class Actions, Prerequisites for Class Action**

The threshold commonality inquiry under [Fed. R. Civ. P. 23\(a\)\(2\)](#) is whether there are any questions of fact or law that are common to the class. Commonality does not require an identity of claims or facts among class members. Rather, the commonality requirement will be satisfied if the named plaintiffs share at least one question of fact or law with the grievances of the prospective class. Even where individual facts and circumstances do become important to the resolution, class treatment is not precluded. The threshold of commonality is not high.

Antitrust & Trade Law > Regulated Practices > Private Actions

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN7** [blue download icon] Regulated Practices, Private Actions

Antitrust actions often present common questions of law and fact, and are, therefore, frequently certified as class actions.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN8** [blue download icon] Class Actions, Prerequisites for Class Action

The United States Court of Appeals for the Third Circuit has set a low threshold for satisfying the typicality requirement holding that if the claims of the named plaintiffs and class members involve the same conduct by the defendant, typicality is established.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN9** [blue download icon] Class Actions, Prerequisites for Class Action

The typicality requirement for a class action does not mandate that all putative class members share identical claims. Plainly, there is nothing in [Fed. R. Civ. P. 23\(a\)\(3\)](#) which requires named plaintiffs to be clones of each other or clones of other class members.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN10** [blue download icon] Class Actions, Prerequisites for Class Action

A requirement of [Fed. R. Civ. P. 23\(a\)](#) is that the representative parties will fairly and adequately protect the interests of the class. [Fed. R. Civ. P. 23\(a\)\(4\)](#). The United States Court of Appeals for the Third Circuit has held that adequate representation depends on two factors: (i) the plaintiff's attorney must be qualified, experienced, and generally able to conduct the proposed litigation, and (ii) the plaintiff must not have interests antagonistic to those of the class.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN11** [blue download icon] Class Actions, Prerequisites for Class Action

Once the requirements of [Fed. R. Civ. P. 23\(a\)](#) are met, [Fed. R. Civ. P. 23\(b\)\(3\)](#) permits the maintenance of a class action if a court finds (1) that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and (2) that a class action is superior to other available methods for the fair and efficient adjudication of the controversy.

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### **HN12** [blue download icon] Class Actions, Prerequisites for Class Action

The [Fed. R. Civ. P. 23\(b\)\(3\)](#) predominance inquiry tests whether proposed classes are sufficiently cohesive to warrant adjudication by representation.

Antitrust & Trade Law > Regulated Practices > Private Actions

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN13](#) [ ] **Regulated Practices, Private Actions**

Antitrust actions involving common questions of liability for monopolization have frequently been held to predominate for the preliminary stage of class certification. The presence of individual questions does not mean that the common questions of law and fact do not predominate.

Civil Procedure > Special Proceedings > Class Actions

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN14](#) [ ] **Special Proceedings, Class Actions**

To satisfy due process, notice to class members must be reasonably calculated under all the circumstances, to apprise interested parties of the pendency of an action and afford them an opportunity to present their objections.

Civil Procedure > Special Proceedings > Class Actions

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN15](#) [ ] **Special Proceedings, Class Actions**

In [Fed. R. Civ. P. 23\(b\)\(3\)](#) actions, class members must receive the best notice practicable under the circumstances.

Civil Procedure > Special Proceedings > Class Actions

Constitutional Law > ... > Fundamental Rights > Procedural Due Process > Scope of Protection

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

#### [HN16](#) [ ] **Special Proceedings, Class Actions**

In a class action, for those whose names and addresses cannot be determined by reasonable efforts, notice by publication suffices under both [Fed. R. Civ. P. 23\(c\)\(2\)](#) and under the Due Process Clause.

Business & Corporate Compliance > ... > Medical Treatment > Patient Confidentiality > Medical Records Under HIPAA

### [\*\*HN17\*\*](#) [blue icon] **Patient Confidentiality, Medical Records Under HIPAA**

The privacy of consumers who purchase prescription medication is protected under the provisions of the Health Insurance Portability and Accountability Act of 1996 (HIPAA), [42 U.S.C.S. § 1320d-2](#). HIPAA protects protected health information from disclosure. "Protected health information" means individually identifiable health information that is maintained and/or transmitted in any form or medium. [45 C.F.R. § 160.103 \(2004\)](#). Pharmacists are health care providers covered by the Act. Patient authorization is required for disclosure of protected health information. Improper disclosure may subject the provider to civil and/or criminal penalties. [42 U.S.C. §§ 1320d-5](#) and [1320d-6](#).

Civil Procedure > Settlements > Settlement Agreements

Governments > State & Territorial Governments > Employees & Officials

Governments > State & Territorial Governments

Governments > Police Powers

### [\*\*HN18\*\*](#) [blue icon] **Settlements, Settlement Agreements**

States, by their Attorneys General, have the authority to settle and release indirect purchaser claims in a parens patriae or other representative capacity. A state has a quasi-sovereign interest in the health and well being -- both physical and economic -- of its residents in general. That federal authority is supplemented by state statutory provisions and case law.

Civil Procedure > Special Proceedings > Class Actions

### [\*\*HN19\*\*](#) [blue icon] **Special Proceedings, Class Actions**

All Attorneys' General have authority to represent consumers, depending on the state, in at least one of the following four ways: (1) parens patriae authority expressly conferred by the state legislature, (2) authority expressly conferred by the state legislature that is the functional equivalent of parens patriae authority, (3) judicially recognized authority to represent consumers, or (4) authority to proceed as a class representative of consumers pursuant to [Fed. R. Civ. P. 23](#).

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### [\*\*HN20\*\*](#) [blue icon] **Settlements, Settlement Agreements**

The United States Court of Appeals for the Third Circuit affords an initial presumption of fairness for a settlement if a court finds that: (1) the negotiations occurred at arm's length; (2) there was sufficient discovery; (3) the proponents of the settlement are experienced in similar litigation; and (4) only a small fraction of the class objected.

Antitrust & Trade Law > Consumer Protection

Civil Procedure > Settlements > Settlement Agreements

Governments > State & Territorial Governments > Employees & Officials

Antitrust & Trade Law > Regulated Practices > Private Actions > Purchasers

## **HN21** [ ] Antitrust & Trade Law, Consumer Protection

The participation of State Attorneys General in a settlement furnishes extra assurance that consumers' interests are protected.

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

## **HN22** [ ] Settlement Agreements, Validity of Agreements

A class action may be settled under [Fed. R. Civ. P. 23\(e\)](#) upon a judicial finding that the settlement is fair, reasonable, and adequate. [Fed. R. Civ. P. 23\(e\)\(1\)\(C\)](#). Under [Fed. R. Civ. P. 23\(e\)](#), a court must determine whether the settlement is within a range that responsible and experienced attorneys could accept considering all relevant risks and factors of litigation. The range recognizes the uncertainties of law and fact in any particular case and the concomitant risks and costs necessarily inherent in taking any litigation to completion.

Civil Procedure > Settlements > Settlement Agreements

## **HN23** [ ] Settlements, Settlement Agreements

Because a settlement represents an exercise of judgment by the negotiating parties, cases have consistently held that the function of a court reviewing a settlement is neither to rewrite the settlement agreement reached by the parties nor to try the case by resolving issues left unresolved by the settlement. The temptation to convert a settlement hearing into a full trial on the merits must be resisted.

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

## **HN24** [ ] Settlement Agreements, Validity of Agreements

To determine whether a settlement is fair, reasonable and adequate under [Fed. R. Civ. P. 23\(e\)](#), courts in the Third Circuit apply a nine-factor test. These factors are: (1) the complexity, expense, and likely duration of the litigation; (2) the reaction of the class to the settlement; (3) the stage of the proceedings and the amount of discovery completed; (4) the risks of establishing liability; (5) the risks of establishing damages; (6) the risks of maintaining the class action through the trial; (7) the ability of the defendants to withstand a greater judgment; (8) the range of reasonableness of the settlement fund in light of the best possible recovery; and (9) the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

## **HN25** [ ] Special Proceedings, Class Actions

When providing notice of a proposed settlement to class action members, the law does not require that a charity that may receive left over funds be disclosed in the notice to the class.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

#### **HN26** [ ] **Special Proceedings, Class Actions**

Information regarding conditions that may terminate a class action settlement need not be detailed in the notice to the class.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements > Modification of Agreements

#### **HN27** [ ] **Special Proceedings, Class Actions**

Minor modifications may be necessary to a proposed class action settlement agreement (indeed may be favorable to the class), and additional class notice is not always required because, e.g., of the cost of notice that would take recovered money from the class.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

#### **HN28** [ ] **Special Proceedings, Class Actions**

The United States Court of Appeals for the Third Circuit has approved proposed class action settlement allocations based on expenditures rather than damages.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

#### **HN29** [ ] **Special Proceedings, Class Actions**

In examining the stage of the litigation at which a proposed class action settlement is reached, the proper question for approval of a settlement is whether counsel had an adequate appreciation of the merits of the case before negotiating.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### **HN30** [blue icon] Special Proceedings, Class Actions

The pursuit of early settlement is a tactic that merits encouragement; it is entirely appropriate to reward expeditious and efficient resolution of disputes. Early settlements benefit everyone involved in the process and everything that can be done to encourage such settlements, especially in complex class action cases, should be done.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### **HN31** [blue icon] Special Proceedings, Class Actions

The risks of establishing liability and damages factors in a proposed class action settlement survey the potential risks and rewards of proceeding to litigation in order to weigh the likelihood of success against the benefits of an immediate settlement.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > ... > Class Actions > Prerequisites for Class Action > General Overview

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### **HN32** [blue icon] Special Proceedings, Class Actions

Because the prospects for obtaining certification have a great impact on the range of recovery one can expect to reap from a class action, this factor in a proposed class action settlement measures the likelihood of obtaining and keeping a class certification if the action were to proceed to trial.

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### **HN33** [blue icon] Settlements, Settlement Agreements

Many settlements are approved where a settling defendant has the ability to pay greater amounts.

Civil Procedure > Special Proceedings > Class Actions

Civil Procedure > Settlements > Settlement Agreements

Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements

### [\*\*HN34\*\*](#) [blue] Special Proceedings, Class Actions

A court evaluating a proposed class action settlement should consider whether the settlement represents a good value for a weak case or a poor value for a strong case. In the process, however, a court must avoid deciding or trying to decide the likely outcome of a trial on the merits.

[Antitrust & Trade Law > Regulated Practices > Private Actions](#)

[Civil Procedure > Special Proceedings > Class Actions](#)

[Civil Procedure > Settlements > Settlement Agreements](#)

[Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements](#)

### [\*\*HN35\*\*](#) [blue] Regulated Practices, Private Actions

To evaluate the propriety of an antitrust class action settlement's monetary component, a court should compare the settlement recovery to the estimated single damages. Although in certain circumstances a plaintiff class may recover treble damages if it prevails at trial, that result is far from certain.

[Civil Procedure > Special Proceedings > Class Actions](#)

[Civil Procedure > Special Proceedings > Class Actions > Judicial Discretion](#)

[Civil Procedure > Settlements > Settlement Agreements](#)

[Civil Procedure > Settlements > Settlement Agreements > Validity of Agreements](#)

### [\*\*HN36\*\*](#) [blue] Special Proceedings, Class Actions

As with settlement agreements, courts consider whether distribution plans are fair, reasonable, and adequate. In evaluating the formula for apportioning a settlement fund, a court keeps in mind that district courts enjoy broad supervisory powers over the administration of class action settlements to allocate the proceeds among the claiming class members equitably.

[Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees](#)

### [\*\*HN37\*\*](#) [blue] Attorney Fees & Expenses, Reasonable Fees

The United States Court of Appeals for the Third Circuit has set forth with specificity the factors, known as the Gunter factors, that a court should consider in evaluating requested attorneys' fees in a common fund case. The Gunter factors need not be applied in a formulaic way, and their weight may vary on a case-by-case basis. The Gunter factors include (1) the size of the fund created and number of persons benefitting from the settlement, (2) the presence/absence of substantial objections to the fee, (3) the skill of Plaintiffs' counsel, (4) complexity and duration of the litigation, (5) the risk of nonpayment, (6) amount of time devoted to the litigation, and (7) awards in similar cases.

[Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > General Overview](#)

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN38**  **Costs & Attorney Fees, Attorney Fees & Expenses**

The courts do not hesitate to grant attorneys' fees despite the presence of objections when the rationale for awarding fees outweighs the objections.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN39**  **Attorney Fees & Expenses, Reasonable Fees**

The absence of meaningful class member objection to a proposed counsel fee in a proposed class action settlement ordinarily supports the reasonableness of the request.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN40**  **Attorney Fees & Expenses, Reasonable Fees**

The circumstances surrounding a difficult settlement increase the complexity of a case for a counsel fee.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN41**  **Attorney Fees & Expenses, Reasonable Fees**

In comparing a requested attorney's fee award in a class action with amounts awarded in similar actions, a court's analysis is two-pronged. First, the court compares the actual award requested to other awards in comparable settlements. Second, the court ensures that the award is in line with what an attorney would have received if the fee was negotiated on the open market.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN42**  **Attorney Fees & Expenses, Reasonable Fees**

A district court may not rely on a formulaic application of the appropriate range in awarding attorney's fees but must consider the relevant circumstances of the particular case. A comparison of awards in similar cases is only a factor in determining the appropriateness of a fee award. In considering this factor, a court notes the survey of fee awards that have occurred in similar cases.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

**HN43**  **Attorney Fees & Expenses, Reasonable Fees**

Courts within the Third Circuit often award attorney's fees of 25 percent to 33 percent of the recovery.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

#### [HN44](#) [blue download icon] Attorney Fees & Expenses, Reasonable Fees

When deciding on appropriate attorney's fee levels in common-fund cases, courts must do their best to award counsel the market price for legal services, in light of the risk of nonpayment and the normal rate of compensation in the market at the time. The object is to give the lawyer what he would have gotten in the way of a fee in an arm's length negotiation. Consequently, courts should look to the private market when assessing the reasonableness of the percentage fee.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

#### [HN45](#) [blue download icon] Attorney Fees & Expenses, Reasonable Fees

A one-third contingency fee for attorneys is generally standard in individual cases.

Civil Procedure > ... > Costs & Attorney Fees > Attorney Fees & Expenses > Reasonable Fees

#### [HN46](#) [blue download icon] Attorney Fees & Expenses, Reasonable Fees

A lodestar crosscheck for attorney's fees is not a Gunter factor but is a suggested practice. When performing the lodestar crosscheck, the United States Court of Appeals for the Third Circuit has recognized that multiples ranging from one to four are frequently awarded in common fund cases when the lodestar method is applied. The district courts may rely on summaries submitted by the attorneys and need not review actual billing records.

Civil Procedure > ... > Costs & Attorney Fees > Costs > General Overview

#### [HN47](#) [blue download icon] Costs & Attorney Fees, Costs

Counsel in common fund cases is entitled to reimbursement of expenses that were adequately documented and reasonably and appropriately incurred in the prosecution of the case.

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**Judges:** Honorable Faith S. Hochberg, United States District Judge.

**Opinion by:** Faith S. Hochberg

## Opinion

**OPINION**

This matter is before the Court upon a settlement agreement between the manufacturers of the anti-depressant drug Remeron, Organon USA Inc. and Akzo Nobel N.V. (Defendants or Organon), and the end-payor purchasers of Remeron along with all Attorney Generals of the United States of America and territories. The settling parties seek (1) final approval of their class action settlement agreement and plan of distribution, (2) final certification of an end-payor settlement class pursuant to [Fed. R. Civ. P. 23](#), and (3) award of attorneys' fees to Plaintiffs' Counsel, reimbursement of litigation expenses, and incentive awards to named Plaintiffs. The Court preliminarily approved the settlement on January 25, 2005 after a preliminary fairness hearing on December 1, 2004. The final Fairness Hearing was conducted on June 28, 2005.

**I. BACKGROUND****[\*2] A. The Litigation****1. The Complaint**

In 2002, end-payor purchasers of Remeron filed class action complaints against Defendants. Complaints were filed by United Food and Commercial Workers Local 56 Health & Welfare Fund, Board of Trustees of United Food and Commercial Workers Local 56 Health & Welfare Fund, Vista Healthplan, Inc., Gayle Taylor, Dianne Mason and Robert Kapella (End-Payor Plaintiffs or Plaintiffs). These complaints were followed by a Consolidated Class Action Complaint on September 11, 2002, and thereafter by an Amended Consolidated Class Action Complaint (Complaint) in *In re Remeron End-Payor Antitrust Litigation*, Master Docket No. 02-CV-2007 (D.N.J.), filed January 5, 2004.

The Complaint alleges violations of the Sherman Act, [15 U.S.C. § 2](#), and violations of state antitrust and/or unfair competition statutes. It alleges that Defendants (a) obtained United States Patent No. 5,977,099 ('099 patent) through fraud on the United States Patent and Trademark Office (PTO), (b) improperly listed the 099 patent in the United States Food and Drug Administration's (FDA's) "Approved Therapeutic Equivalence Evaluations" (Orange Book) to preserve [\*3] their monopoly, (c) improperly delayed the listing of that patent in the Orange Book to prolong their monopoly, and (d) thereafter improperly commenced lawsuits asserting sham claims of patent infringement under the Hatch-Waxman Act, [21 U.S.C. § 355](#), and the United States patent laws against generic drug companies (Generic Manufacturers), which sought permission to market generic versions of Organon's antidepressant drug, Remeron.

The Complaint alleges that Defendants took these several actions in order to forestall the market entry of FDA-approved generic versions of Remeron (i.e. generic mirtazapine). As a result, end-payor purchasers -- composed of Third-Party Payors (such as health benefit funds, HMOs, health insurers and hospitals), governmental entities, and individual consumers -- were allegedly required to purchase brand-name Remeron at monopoly prices instead of being able to purchase generic mirtazapine at a fraction of the price. Absent Defendants' illegal activities, it is alleged that patients would have been able to purchase lower-priced generic mirtazapine earlier, resulting in a savings of millions of dollars.

**2. Extensive Discovery and Litigation [\*4] Prior to Settlement**

This litigation was complex and hotly contested from the outset, beginning with Defendants' initial unsuccessful efforts to obtain a stay from the Magistrate Judge. On December 18, 2002, this Court granted summary judgment in favor of certain Generic Manufacturers with respect to Organon's patent claims against them. Following that decision, class action complaints and individual complaints were filed by various direct purchasers of Remeron (Direct Purchasers), who are not a part of this litigation or settlement.

The Court then entered a case management Order on June 18, 2003, coordinating discovery in the End-Payor class actions, the Direct Purchaser cases, and the antitrust counterclaims filed by the Generic Manufacturers. Additional coordination and case management Orders were issued on July 16, 2003; August 11, 2003; and December 11, 2003, and several Orders regarding discovery were issued September 26, 2003; December 23, 2003; January 15, 2004; January 16, 2004; February 3, 2004; February 10, 2004; and February 13, 2004.

On December 3, 2003, the Court granted Defendants' motion to dismiss several antitrust counterclaims by Generic Manufacturers including [\*5] the (a) allegation that the 099 patent had been improperly listed by Defendants in the FDA's Orange Book for anticompetitive reasons, and (b) allegation that the Defendants' patent litigation against the Generic Manufacturers was baseless and brought for anticompetitive purposes to prolong Defendants' monopoly.

Overall, discovery was extensive. Approximately 800,000 pages of documents and data were produced by Defendants and third parties. Documents produced included hundreds of thousands of pages relating to Defendants' various anti-generic strategies for Remeron; Defendants' internal patent planning and life cycle management strategy; Defendants' regulatory and Orange Book listing strategies; Defendants' clinical development files, which contained additional documentation regarding other regulatory exclusivity strategies for Remeron; Defendants' patent files, including file wrapper and patent prosecution history documentation; and numerous scientific and medical articles and other publications which impacted upon the issues of non-infringement and invalidity of the 099 patent. End-Payor Plaintiffs' briefs revealed extensive research into the various legal and regulatory issues [\*6] in this case, including an analysis of various FDA regulations and the case law interpreting those regulations.

End-Payor Plaintiffs' counsel pressed Defendants on the adequacy of their document production at a hearing on December 19, 2003, through a Notice of Deposition of Corporate Defendants Pursuant to *Fed. R. Civ. P. 30(b)(6)*, and through a letter brief on February 2, 2004. They took depositions of numerous current or former employees of the Defendants. These included many high-level executives and employees, who were deposed on complicated and highly technical issues relating to Defendants' various legal, regulatory, marketing and other anti-generic strategies for Remeron. Plaintiffs also consulted heavily with counsel for the Direct Purchasers, counsel for the Generic Manufacturers, and the State Attorneys General. In all, over 50 depositions were taken.

The End-Payor Plaintiffs also provided extensive discovery, including *Rule 26 Initial Disclosures* on October 15, 2002, answers to interrogatories on September 8, 2003, supplemental voluminous document production, and deposition testimony by the two institutional End-Payor Plaintiff Class [\*7] Representatives (Vista Healthplan, Inc. and United Food & Commercial Workers Local 56 Health & Welfare Fund). End-Payor Plaintiffs also engaged and met extensively with economic and other experts to develop support for theories of liability and to measure the monetary harm suffered by End-Payors of Remeron.

Defendants moved to dismiss or stay the End-Payor Plaintiffs' Consolidated Amended Complaint on November 14, 2002. End-Payor Plaintiffs filed a comprehensive Memorandum in Opposition to Defendants' Motion to Dismiss or Stay on January 17, 2003, and a Notice of Supplemental Authority in opposition on February 6, 2003, as well as a letter brief regarding subsequent authority on April 25, 2003, and a letter brief on further supplemental authority on June 3, 2003. Defendants filed their Reply Memorandum in Support of Motion to Dismiss or Stay on February 21, 2003, and filed a response to End-Payor Plaintiffs' April 25 letter brief on May 8, 2003, and a response to End-Payor Plaintiffs' June 3 letter brief on June 5, 2003.

Defendants opposed End-Payor Plaintiffs' motion for leave to file the End-Payor Plaintiffs' Consolidated Amended Complaint. End-Payor Plaintiffs filed an extensive [\*8] Memorandum of Law in Support of Plaintiffs' Motion for Leave to Amend on November 18, 2003. After briefing and oral argument, the Court granted End-Payor Plaintiffs' motion for leave to amend on December 31, 2003. Following oral argument, Defendants' initial motion to dismiss was denied as moot in light of End-Payor Plaintiffs' Amended Consolidated Complaint, by Order dated January 15, 2004.

Defendants thereafter moved to dismiss End-Payor Plaintiffs' Amended Consolidated Class Action Complaint on January 20, 2004. End-Payor Plaintiffs moved to certify a nationwide class of End Payors, including consumers as

well as public (non-federal) and private institutional End Payors, on October 27, 2003. End-Payor Plaintiffs filed a comprehensive Memorandum of Law in Support of Plaintiffs' Motion for Class Certification, together with a detailed and extensive Declaration from Harvard University health economist Professor Richard G. Frank in support of class certification. The Court had not issued a ruling on these two motions at the time of the proposed settlement.

As the End-Payor Plaintiffs were developing their case, the working group of State Attorneys General were conducting their own [\*9] economic and factual investigation relating to the claims, underlying events, and conduct alleged by the End-Payor Plaintiffs and others. Beginning in March 2003, the Office of the Attorney General of Texas issued Civil Investigative Demands (CIDs) for documents and answers to written interrogatories to the Defendants and to third parties, including the Generic Manufacturers. A multi-state working group of State Attorneys General that was formed during the summer of 2003 conducted a targeted review of the 200 CD-ROMs of document images produced in response to the CIDs. The working group also reviewed transcripts of depositions and hearings from the patent litigation and the End-Payor and Direct Purchaser litigation. The State Attorneys General also researched and analyzed may legal and regulatory issues involving patents, the FDA and the Hatch-Waxman process. In addition, the State Attorneys General gathered data relating to purchases of Remeron from their state agencies, including their state Medicaid programs, as well as sales and pricing data from the Defendants and the Generic Manufacturers, and retained economists to analyze the data and create damages estimates. The State Attorneys [\*10] General undertook extensive legal research and analysis and consulted with economic and intellectual property law experts regarding the theories of liability at issue in this case.

## B. Mediation and Settlement

In December 2003, the parties began to explore the possibility of settlement with the working group of State Attorneys General. The settlement negotiations included a multi-day global settlement mediation before Judge Politan in January 2004. This was followed by a series of settlement discussions between Defendants' and End-Payor Plaintiffs' counsel in coordination with the working group of State Attorneys General. These discussions laid the groundwork, but settlement was not achieved until the end of a two-day settlement conference before this Court. The broad outlines of this agreement were discussed with the Court in chambers on February 18, 2004.

For the next half year, the End-Payor Plaintiffs and the States together engaged in further negotiations with Defendants to craft and finalize the detailed written settlement agreement. Other negotiations included crafting and finalizing the escrow agreement, the proposed preliminary approval order, the proposed final judgment, [\*11] and the class notice of the proposed settlement. The working group of State Attorneys General, in conjunction with the Federal Trade Commission, engaged in many further negotiations with Defendants to draft and finalize the Stipulated Injunction. State Attorneys General who were not involved in the working group were later invited to join the settlement.

## C. Preliminary Approval of the Settlement and Execution of the Notice Plan

On October 20, 2004, End-Payor Plaintiffs and the Plaintiff States filed their Memorandum in Support of End-Payor Plaintiffs' and States' Motion for Preliminary Approval of Proposed Settlement. Contemporaneous with the filing of that Memorandum, a Complaint including all of the 50 States, the District of Columbia, and all U.S. territories was filed with the Court, along with the fully executed settlement agreement.<sup>1</sup>

[\*12] On November 17, 2004, the Court issued an Order requesting End-Payor Plaintiffs and Plaintiff States submit a brief addressing in further detail their proposed Notice Plan. On November 24, 2004, End-Payor Plaintiffs and Plaintiff States submitted a Supplemental Memorandum in Further Support of Plaintiffs' Motion for Preliminary Approval that addressed the issues raised. On December 1, 2004, the Court held a hearing on the proposed

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<sup>1</sup> *States and Commonwealths of Texas, Florida, Oregon, et al. v. Organon USA Inc. and Akzo Nobel N. V.*, Civil Action No. 04-5126 (FSH) (Complaint filed Oct. 20, 2004).

preliminary approval of the settlement. At that hearing, the Court requested that the parties develop a proposed Plan of Distribution and include details regarding that plan in the notices, which the parties did. On January 14, 2005, the End-Payor Plaintiffs and Plaintiff States submitted a Second Supplemental Memorandum in Further Support of Plaintiffs' Motion for Preliminary Approval, setting forth the proposed Plan of Distribution and revised notices. On January 24, 2005, the Court followed up with an e-mail to the parties seeking additional information regarding certain language in the proposed order and the notice. End-Payor Plaintiffs and Plaintiff States responded to the Court's questions by return e-mail and revised the long-form and summary notices [\*13] in response to the Court's inquiries.

On January 25, 2005, the Court entered an Order Conditionally Certifying Settlement Class, Preliminarily Approving Proposed Settlement, and Preliminarily Approving Representation of Attorneys General. In compliance with the settlement agreement and the Court's January 25, 2005 Order, Defendants paid \$ 35 million into escrow on February 1, 2005.

Then the Notice Plan was carried out. The claims administrator, Complete Claim Solutions (CCS), mailed 13,431 notice packages to Third-Party Payor (TPP) class members. As of May 25, 2005, with the cooperation of the pharmacies, CCS had caused to be mailed 854,046 notice packets to potential consumer class members. The media consultant retained by CCS published the summary notice in national publications, such as *Reader's Digest*, *Parade*, *USA Today* and *USA Weekend*. To provide adequate coverage for class members residing in one of the United States Territories, the media consultant published summary notice in *El Nuevo Dia*, the Pacific Daily News and the Virgin Islands Daily News. The media consultant also published the summary notice in an industry periodical, *National Underwriter*, to reach TPP class [\*14] members. Additionally, CCS contacted 22,643 physicians, and numerous mental health, senior and women's organizations soliciting their assistance in notifying their members of the settlement. CCS distributed Public Service Announcements (PSAs) to 1,000 radio stations. As of May 25, 2005, 60 radio stations reported airing the PSAs a total of 11,179 times. CCS designed and developed a website for potential class members to obtain information and for consumer class members to file a claim online; and CCS set up and operates a toll-free 800 telephone number to answer class members' questions. As of May 25, 2005, over 40,000 visits have been made to the website and nearly 30,000 calls have been made to the toll-free telephone number.

#### D. The Settlement Terms

A copy of the settlement agreement and its exhibits were filed with the Court on October 20, 2004 with the motion by End-Payor Plaintiffs and States for preliminary settlement approval.

##### 1. Monetary Payments And Distributions

The settlement provides for settlement payments by Defendants in a total amount of up to Thirty-Six Million Dollars (\$ 36,000,000.00) (Settlement Consideration) consisting of: (1) Thirty-Three Million [\*15] Dollars (\$ 33,000,000.00) that Defendants paid into an escrow account on February 1, 2005, plus any interest, dividends and other distributions and payments earned on that sum while in escrow (Settlement Fund); (2) Two Million Dollars (\$ 2,000,000.00) that Defendants paid on February 1, 2005 into a separate escrow account to pay for costs and expenses of settlement class notice and future costs of settlement administration, plus any interest, dividends and other distributions and payments earned on that sum while in escrow (Notice Fund); and (3) up to One Million Dollars (\$ 1,000,000.00) that the Defendants will pay to the States following the effective date of the settlement agreement for their reasonable attorneys' fees and expenses incurred in their investigations of Defendants relating to this matter and in connection with the approval and administration of this settlement.

###### a. The Settlement Fund

On February 1, 2005, Defendants deposited into escrow the sum of Thirty-Three Million Dollars (\$ 33,000,000.00). This Settlement Fund may be used for purposes of distribution to the members of the settlement class and the Plaintiff States, payment of further notice or administrative [\*16] costs in excess of the amount of the Notice Fund

up to \$ 500,000.00, and payment of End-Payor Plaintiffs' attorneys' fees and costs, and incentive awards for the class representatives.

Under the Plan of Distribution, the net settlement amount (the settlement fund less notice and claims administration costs, attorneys' fees, expenses, and incentive awards) will be allocated as follows: 32.8% to consumers, 16.5% to state governmental purchasers, and 50.7% to TPPs. End-Payor Plaintiffs' Co-Lead Counsel have applied to the Court for an attorneys' fees award from the Settlement Fund equal to \$ 7.8 million (23.6% of the Settlement Fund) plus 23.6% of interest that has accrued on the Settlement Fund, as well as reimbursement of almost \$ 500,000.00 in expenses (including expert fees and costs). Attorneys' fees and expenses will be distributed by End-Payor Plaintiffs' Co-Lead Counsel among the ten law firms that initiated and litigated these End Payor cases. In addition, End-Payor Plaintiffs seek an award of incentive awards to the Class Representatives in the amount of Seventy-Five Thousand Dollars (\$ 75,000.00).

b. The Notice Fund

Defendants deposited into escrow a separate amount of Two [\*17] Million Dollars (\$ 2,000,000.00) used exclusively for the payment of notice and administrative fees and costs reasonably incurred for the purpose of providing notice of settlement to members of the settlement class, processing claims and administering the settlement, paying any taxes and tax expenses with respect to the escrow accounts, and paying reasonable fees and costs to the escrow agent.

c. Payment to State Attorneys General

After the effective date of the settlement agreement, Defendants will reimburse the Plaintiff States for their reasonable attorneys' fees and expenses incurred in connection with their investigations of Defendants relating to this matter, as well as their future reasonable attorneys' fees and expenses to be incurred in connection with settlement approval and administration. The aggregate amount of all such fees and expenses of all Plaintiff States that shall be reimbursable shall not exceed One Million Dollars (\$ 1,000,000.00).

d. Any Unclaimed Money

Any amount in the Settlement Fund that remains after payment of all claims, Court-approved fees, costs, expenses, and incentive awards, and any supplemental distribution to settlement class members and Court-approved [\*18] supplemental fees and costs, will be distributed to charitable organizations or state agencies that provide health or legal services to settlement class members, as recommended by End-Payor Plaintiffs' Co-Lead Counsel and/or State Liaison Counsel and approved by the Court.

**2. Injunctive Relief**

Defendants have agreed to an injunction prohibiting certain future conduct (Injunction), which will become effective when the settlement agreement becomes effective. The Injunction, which was negotiated by the Plaintiff States in conjunction with the Federal Trade Commission states, *inter alia*, that Defendants (a) "shall not seek, maintain, certify to, or take any other action in furtherance of, the listing or continued listing of any Patent in the Orange Book where the listing of such Patent in the Orange Book violates Applicable Law" and (b) "shall not" provide to the FDA "Listing Information that [is] false or misleading."

**3. Release of Claims**

Members of the settlement class (who have not made valid and timely elections to exclude themselves from the settlement class) release and discharge forever the Defendants from all claims which could have been asserted from the facts [\*19] and circumstances giving rise to this case, from the beginning of time through January 25, 2005 (the date this Court preliminarily approved the Settlement Agreement).

**II. ANALYSIS**

## A. Class Certification for Purposes of Settlement

In its Order preliminarily approving the settlement agreement, the Court conditionally certified the Settlement Class, defined in the settlement agreement as:

All End Payors (including any assignees of such End Payors) who purchased and/or paid all or part of the purchase price of Mirtazapine Products in the United States during the period beginning June 15, 2001 through January 25, 2005 (the date of the Preliminary Approval Order). Excluded from the Settlement Class are (i) Defendants and any of their subsidiaries and affiliates, (ii) all federal governmental entities, agencies and instrumentalities, and (iii) all wholesalers and retailers and all persons or entities that purchased Mirtazapine Products primarily for purposes of resale.

The Court also preliminarily approved the following as Class Representatives:

United Food and Commercial Workers Local 56 Health & Welfare Fund, and Board of Trustees of United Food and [\*20] Commercial Workers Local 56 Health & Welfare Fund, a health benefit fund operated for the benefit of present and retired members of the union local and their families;

Vista Healthplan, Inc., a health maintenance organization that provides comprehensive healthcare benefits to its members; and

Gayle Taylor, Dianne Mason, and Robert Kapella, all of whom are consumers who purchased Remeron during the Class Period.

**HN1** Under [Rule 23 of the Federal Rules of Civil Procedure](#), the Court must engage in a two-step analysis in order to determine whether it should certify a class action for settlement purposes. First, the Court must determine whether the End-Payor Plaintiffs and Plaintiff States have satisfied the prerequisites for maintaining a class action as set forth in [Fed. R. Civ. P. 23\(a\)](#). If the End-Payor Plaintiffs and Plaintiff States can satisfy these prerequisites, the Court must then determine whether the alternative requirements of [Rule 23\(b\)\(2\)](#) or [23\(b\)\(3\)](#) are met. See [Fed. R. Civ. P. 23\(a\)](#) advisory committee's note. **HN2** "Confronted with a request for [\*21] settlement-only class certification, a district court need not inquire whether the case, if tried, would present intractable management problems, see [Fed. Rule Civ. Proc. 23\(b\)\(3\)\(D\)](#), for the proposal is that there be no trial." [Amchem Prods., Inc. v. Windsor](#), 521 U.S. 591, 619, 117 S. Ct. 2231, 138 L. Ed. 2d 689 (1997).

### 1. The Requirements of [Rule 23\(a\)](#)

**HN3** [Rule 23\(a\)](#) provides that class members may maintain a class action as representatives of a class if they show the court that:

- (a) the class members are so numerous that joinder of all members is impracticable;
- (b) the action addresses questions of law or fact common to the class;
- (c) the claims or defenses of the class representatives are typical of the claims or defenses of the class; and
- (d) the class representative parties will fairly and adequately protect the interests of the class.

#### a. Numerosity

**HN4** Courts will ordinarily discharge the prerequisite of numerosity if the class is so large that "joinder of all members is impracticable." [Hanlon v. Chrysler Corp.](#), 150 F.3d 1011, 1019 (9th Cir. 1998). "The plaintiff need not precisely enumerate the potential size of the proposed [\*22] class, nor is the plaintiff required to demonstrate that joinder would be impossible." [Cannon v. Cherry Hill Toyota, Inc.](#), 184 F.R.D. 540, 543 (D.N.J. 1999); accord [Wachtel v. Guardian Life Ins. Co.](#), 223 F.R.D. 196, 211 (D.N.J. 2004). Moreover, "it is proper for the court to accept common sense assumptions in order to support a finding of numerosity." [Cumberland Farms, Inc. v. Browning-Ferris Indus.](#), 120 F.R.D. 642, 646 (E.D. Pa. 1988) (citation omitted); accord [In re Nasdaq Market-Makers Antitrust Litig.](#), 169 F.R.D. 493, 509 (S.D.N.Y. 1996).

Here, the plaintiff class consists of End Payors, including consumers, who paid all or part of the price of Remeron in the United States during the class period. "There can be no serious question that joinder of all these parties,

geographically dispersed throughout the United States, would be impracticable." [In re Corrugated Container Antitrust Litig.](#), 80 F.R.D. 244, 247 (S.D. Tex. 1978). Hundreds of thousands of class members have received notice and tens of thousands have filed proofs of claim across. The class thus easily fulfills the numerosity requirement. [\*23] [HN5](#) "Numbers in excess of forty, particularly those exceeding one hundred or one thousand have sustained the [ numerosity] requirement." [Weiss v. York Hosp.](#), 745 F.2d 786, 808 n.35 (3d Cir. 1984).

#### b. Commonality

[HN6](#) The threshold commonality inquiry is whether there are any questions of fact or law that are common to the class. [Fed. R. Civ. P. 23\(a\)\(2\)](#). "Commonality does not require an identity of claims or facts among class members." [Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.](#), 259 F.3d 154, 183 (3d Cir. 2001). Rather, "the commonality requirement will be satisfied if the named plaintiffs share at least one question of fact or law with the grievances of the prospective class." "Even where individual facts and circumstances do become important to the resolution, class treatment is not precluded." [Baby Neal for & by Kanter v. Casey](#), 43 F.3d 48, 57 (3d Cir. 1994). *Id. at 57*. "The threshold of commonality is not high." [In re School Asbestos Litig.](#), 789 F.2d 996, 1010 (3d Cir. 1986).

In this case, many common questions exist. They include, *inter alia*, (1) what is the relevant [\*24] product market?; (2) did Defendants have market power in that market?; and (3) did Defendants unlawfully monopolize that market? [HN7](#) Antitrust actions often present common questions of law and fact, and are, therefore, frequently certified as class actions. See, e.g., [Transamerican Ref. Corp. v. Dravo Corp.](#), 130 F.R.D. 70, 73 (S.D. Tex. 1990) (antitrust price-fixing claims and common law fraud); [Cusick v. NVNederlandsche Combinatie Voor Chemische Industrie](#), 317 F. Supp. 1022, 1024 (E.D. Pa. 1970) (consumer class action charging monopolization). The commonality requirement is satisfied here.

#### c. Typicality

[HN8](#) The Third Circuit has "set a low threshold for satisfying" the typicality requirement holding that "if the claims of the named plaintiffs and class members involve the same conduct by the defendant, typicality is established." [Newton v. Merrill Lynch, Pierce, Fenner & Smith, Inc.](#), 259 F.3d 154, 183-84 (3d Cir. 2001); accord [Baby Neal v. Casey](#), 43 F.3d 48, 58 (3d Cir. 1994) (stating "cases challenging the same unlawful conduct which affects both the named plaintiffs and the putative class usually satisfy the typicality [\*25] requirement").

[HN9](#) The typicality requirement "does not mandate that all putative class members share identical claims." [Newton](#), 259 F.3d at 184; see also [Hassine v. Jeffes](#), 846 F.2d 169, 176-77 (3d Cir. 1988). Plainly, "there is nothing in [Rule 23\(a\)\(3\)](#) which requires named plaintiffs to be clones of each other or clones of other class members." [Advocate Health Care v. Mylan Labs., Inc. \(In re Lorazepam & Clorazepate Antitrust Litig.\)](#), 202 F.R.D. 12, 27 (D.D.C. 2001); accord [In re Catfish Antitrust Litig.](#), 826 F.Supp. 1019, 1036 (N.D. Miss. 1993).

In this case, the Class Representatives' and the class members' claims are identically predicated upon Defendants' alleged actions of improper listing and late listing of the 099 Patent in the Orange Book, fraud on the PTO, and filing of allegedly baseless patent infringement lawsuits against Generic Manufacturers. Thus, "there are no differences as to the type of relief sought or the theories of liability upon which plaintiffs will proceed." [In re Corrugated Container Antitrust Litig.](#), 80 F.R.D. 244 (S.D. Tex. 1978). The Class Representatives' claims and those of the class members arise from the same [\*26] course of conduct. "Since the various claims alleged appear to stem from a single course of conduct . . . we cannot conclude that the district court abused its discretion in holding that the typicality requirement was met." [Grasty v. Amalgamated Clothing and Textile Workers Union](#), 828 F.2d 123, 130 (3d Cir. 1987). Accordingly, the Class Representatives' claims are typical of those of the class members.

#### d. Adequacy of Representation

[HN10](#) The final requirement of [Rule 23\(a\)](#) is that "the representative parties will fairly and adequately protect the interests of the class." [Fed. R. Civ. P. 23\(a\)\(4\)](#). The Third Circuit has held that "adequate representation depends on two factors: (i) the plaintiff's attorney must be qualified, experienced, and generally able to conduct the proposed litigation, and (ii) the plaintiff must not have interests antagonistic to those of the class." [Hoxworth v. Blinder](#),

Robinson & Co., 980 F.2d 912, 923 (3d Cir. 1992); accord In re Warfarin Sodium Antitrust Litig., 391 F.3d 516, 532 (3d Cir. 2004); Wetzel v. Liberty Mutual Ins. Co., 508 F.2d 239, 247 (3d Cir. 1975). [\*27]

As to the first factor, End-Payor Plaintiffs' counsel have successfully prosecuted numerous antitrust class actions. Plaintiffs' Co-Lead Counsel, Arthur M. Kaplan, is a graduate of the Harvard Law School (J.D., *cum laude*, 1970) and has been active in antitrust and other complex litigation. Mr. Kaplan was Co-Lead Counsel for plaintiffs in the In re Nasdaq Market-Makers Antitrust Litig., 187 F.R.D. 465 (S.D.N.Y. 1998), in which plaintiffs achieved settlements totaling \$ 1.027 billion.<sup>2</sup> End-Payor Plaintiffs' Co-Lead Counsel Joseph H. Meltzer likewise is experienced. Mr. Meltzer is a graduate of the Temple University School of Law (J.D., *cum laude*) and has focused his practice exclusively on antitrust and complex class action litigation. In addition to prominent roles in prosecuting several major antitrust class actions to successful conclusions, including In re Sorbates Direct Purchaser Antitrust Litig., C98-4886 (N.D. Cal. 2001) (settlements exceeding \$ 92 million), Mr. Meltzer was appointed Co-Lead Counsel in Ryan-House v. GlaxoSmithKline plc, C.A. 2:02cv442 (E.D. Va.), a pharmaceutical antitrust class action brought on behalf of end payors of the [\*28] prescription medication Augmentin which recently settled for \$ 29 million. End-Payor Plaintiffs' Acting Co-Lead Counsel Jeffrey S. Istvan is a 1992 graduate of the University of Virginia School of Law, where he was a Hardy Cross Dillard Scholar. Following a federal judicial clerkship, he has been active in antitrust and consumer class actions. Mr. Istvan was sole lead counsel in Parsky v. Wachovia Bank, N.A., 2001 WL 535786 (C.C.P. Phila. May 8, 2001), a consumer class action that recently settled for approximately than \$ 23 million and worked on several large antitrust class actions, including In re Copper Antitrust Litig., M.D.L. No. 1303 (7th Cir. 2004) (appeal pending); In re Polypropylene Carpet Antitrust Litig., 93 F. Supp. 2d 1348 (N.D. Ga. 2000) (settlements totaling \$ 50 million); and In re Commercial Explosives Antitrust Litig., 945 F. Supp. 1489 (D. Utah 1996) (settlements totaling \$ 77 million).

[\*29] The State Attorneys General, as counsel for the Plaintiff States, have considerable expertise in complex antitrust *parens patriae* and class action litigation. State Liaison Counsel Patricia A. Conners, Director of the Antitrust Division of the Florida Attorney General's Office and past Chair of the National Association of Attorneys General ("NAAG") Multistate Antitrust Task Force. She was an Assistant Attorney General in the Antitrust Division, working on such notable cases as Florida v. Borden, Inc., the 1989 school milk bid-rigging cases that resulted in a \$ 36 million recovery for Florida school boards and Florida v. Abbott Laboratories, Inc., the first of the so-called Infant Formula cases, and the *Disposable Contact Lens Litigation*, which settled in 2002 for \$ 80 million. She has practiced antitrust law exclusively since 1987. State Liaison Counsel Kim Van Winkle is an Assistant Attorney General in the Office of the Attorney General of Texas, where she has practiced antitrust law exclusively since 1998. Ms. Van Winkle graduated in 1997 with honors from the University of Texas School of Law, with a joint Master of Public Affairs degree from the Lyndon B. Johnson [\*30] School of Public Affairs. She has participated in the investigation and litigation of numerous complex, multistate antitrust cases, including In re Buspirone Antitrust Litigation, No. 01-CV-1 1401, MDL 1413 (S.D.N.Y. Mar. 7, 2003) (final approval granted for \$ 100 million settlement of end-payor action alleging monopolization of drug markets through patent abuse). These attorneys are qualified, experienced, and have skillfully worked on this litigation.

The Class Representatives' interests are not antagonistic to those of the absent class members. The central issues in this case are critical to the claims of both groups. In proving these common issues, the Class Representatives further the absent class members' claims no less than their own. Cf. In re Cardizem CD Antitrust Litig., 218 F.R.D. 508, 518 (E.D. Mich. 2003) ("Each Class member . . . has a common interest in establishing that he, she, or it was financially injured by Defendants' conduct and in an aggregate damages computation"); In re Warfarin Sodium Antitrust Litig., 212 F.R.D. 231, 251 (D. Del. 2002), aff'd, 391 F.3d 516 (3d Cir. 2004) ("The named plaintiffs share [\*31] a strong interest in establishing liability of defendant, seeking the same type of damages

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<sup>2</sup> In In re Nasdaq Market-Makers Antitrust Litig., 187 F.R.D. at 474, the court in approving that settlement stated, "it is difficult to conceive of better representation than the parties to this action achieved." Likewise, in Advocate Health Care v. Mylan Labs. Inc. (In re Lorazepam & Clorazepate Antitrust Litig.), 2003 U.S. Dist. LEXIS 12344, 2003 WL 22037741, at \*6 (D.D.C. June 16, 2003), in which Mr. Kaplan was co-counsel for the class of direct purchasers, the Court in approving settlement characterized counsel as "among the best and most experienced antitrust litigators in the country."

(compensation for overpayment) for the same type of injury (overpayment for warfarin sodium"). Further, "it is difficult to imagine a better representative of the retail consumers within a state than the state's attorney general." *In re Antibiotic Antitrust Actions*, 333 F. Supp. 278, 280 (S.D.N.Y. 1971); accord *FTC v. Mylan Labs., Inc. (In re Lorazepam & Clorazepate Antitrust Litig.)*, 205 F.R.D. 369, 387 (D.D.C. 2002) (stating the plaintiff states "have evidenced a genuine interest in this litigation, and are qualified and experienced."). States, acting through their attorneys general, have frequently been held to be the "best representatives of the consumers residing within their jurisdictions." *In re Ampicillin Antitrust Litig.*, 55 F.R.D. 269, 274 (D.D.C. 1972); see also *West Virginia v. Chas Pfizer & Co., Inc.*, 440 F.2d 1079, 1089-91 (2d Cir. 1971). Thus, the adequacy requirement has been met.

## 2. The Requirements of Rule 23(b)(3)

**HN11** [↑] Once the requirements of *Rule 23(a)* are met, *Rule 23(b)(3)* permits the maintenance of a class action if "the court [\*32] finds [a] that the questions of law or fact common to the members of the class predominate over any questions affecting only individual members, and [b] that a class action is superior to other available methods for the fair and efficient adjudication of the controversy."

**HN12** [↑] "The *Rule 23(b)(3)* predominance inquiry tests whether proposed classes are sufficiently cohesive to warrant adjudication by representation." *Amchem Prods. v. Windsor*, 521 U.S. 591, 623, 117 S. Ct. 2231, 138 L. Ed. 2d 689 (1997). As the Supreme Court has observed, "predominance is a test readily met in certain cases alleging . . . violations of the antitrust laws." *Amchem*, 521 U.S. at 625. In particular, **HN13** [↑] "antitrust actions involving common questions of liability for monopolization . . . have frequently been held to predominate for the preliminary stage of class certification." *Lorazepam & Clorazepate*, 202 F.R.D. at 29. "The presence of individual questions . . . does not mean that the common questions of law and fact do not predominate." *Eisenberg v. Gagnon*, 766 F.2d 770, 786 (3d Cir. 1985).

### a. Questions of Law and Fact Common to the Class Predominate

"As is true in many [\*33] antitrust cases, the alleged violations of the antitrust laws at issue here respecting . . . monopolization relate solely to Defendants' conduct, and as such proof for these issues will not vary among class members." *Lorazepam & Clorazepate*, 202 F.R.D. at 29 (internal quotation marks and citation omitted). As the Third Circuit held in *In re Linerboard Antitrust Litig.*, 305 F.3d 145 (3d Cir. 2002), cert. denied, 538 U.S. 977, 123 S. Ct. 1786, 155 L. Ed. 2d 666 (2003) that "common issues . . . predominate here because the inquiry necessarily focuses on defendants' conduct, that is, what defendants did rather than what plaintiffs did." *Id. at 163* (citation omitted); see also *Warfarin Sodium*, 391 F.3d at 528. "The common questions of law, the elements of the monopolization claim fully enumerated, . . . dwarf, rather than merely predominate over, any individual questions." *Sollenbarger v. Mountain States Tel. and Tel. Co.*, 121 F.R.D. 417, 427 (D.N.M. 1988); see also *Davis v. Southern Bell Tel. Co.*, 1993 U.S. Dist. LEXIS 20033, 1993 WL 593999, \*7 (S.D. Fla. Dec. 23, 1993) ("The issues of antitrust violation, injury, and damages all turn [\*34] on class-wide proof").

In this case, the claims of all class members arise from the same facts giving rise to the same legal claims, as discussed in the above sections on commonality and typicality. Accordingly, the predominance requirement is satisfied.

### b. A Class Action is Superior to Other Available Methods

"In the case of consumers, the class members here have little interest in individually controlling the prosecution or defense of separate actions,' *Fed. R. Civ. P. 23(b)(3)(A)*, because each consumer has a very small claim in relation to the cost of prosecuting a lawsuit." *Warfarin Sodium*, 212 F.R.D. at 251. Indeed, "where it is not economically feasible to obtain relief . . . aggrieved persons may be without any effective redress unless they employ the class action device." *Deposit Guar. Nat'l Bank v. Roper*, 445 U.S. 326, 339, 100 S. Ct. 1166, 63 L. Ed. 2d 427 (1980).

In contrast to the inefficiency of duplicative individual lawsuits, "the efficacy of resolving all plaintiffs' claims in a single proceeding is beyond discussion." *Sollenbarger v. Mountain States Tel. and Tel. Co.*, 121 F.R.D. 417, 436

(D.N.M. 1988). "The [\*35] class action mechanism offers substantial economies of time, effort and expense for the litigants as well as the Court." *In re Terazosin Hydrochloride, 220 F.R.D. 672, 700 (S.D. Fl. 2004)*.

In this very expensive litigation involving hundreds of thousands documents, it would not have been economically feasible for many plaintiffs to seek individual redress. Judicial economy as well as fairness to Defendants makes the litigation of such claims in one action far more desirable than numerous separate actions litigating the same issues.

Because the End-Payor Plaintiffs and Plaintiff States have satisfied all of the requirements under *Fed. R. Civ. P. 23(a)* and the requirements of *Fed. R. Civ. P. 23(b)(3)*, this Court certifies the proposed class for purposes of this settlement.

## B. The Notice of Settlement

The settlement class members are entitled to notice of the proposed settlement and an opportunity to be heard. See *Fed. R. Civ. P. 23(e); Phillips Petroleum Co. v. Shutts, 472 U.S. 797, 105 S. Ct. 2965, 86 L. Ed. 2d 628 (1985)*.

The notice period in this case [\*36] began on March 14, 2005, and continued for forty-five (45) calendar days until April 27, 2005. Under the settlement agreement and Preliminary Approval Order, settlement class members had that Notice Period of 45 days to submit any requests to opt-out of the class and until May 28, 2005 to submit objections.

### 1. Notice Plan

The Notice Plan consisted of multiple components designed to reach consumers through paid print and broadcast media through Public Service Announcements, earned media, and direct mailed notice (to the extent that information could be obtained) to purchasers of Remeron. The media plan provided an estimated reach of more than 90 percent, and frequency realized may have been as much as 2.5 times.<sup>3</sup>

#### [\*37] a. Published Notice

Syndicated data, audited data and proprietary research from the National Mental Health Association and the National Foundation for Depressive Illness were reviewed to identify the media vehicles that would most effectively deliver the message to potential class members in the U.S. and its territories (specifically, Guam, U.S. Virgin Islands, and Puerto Rico). The resulting plan was that the summary notice (about 1 page) be placed in a combination of national Sunday Supplements, *USA Today*, and *Reader's Digest* to reach consumers, plus an insertion in *National Underwriter* to reach Third-Party Payors. The Notice Plan's consumer published media schedule was based upon techniques specifically designed for legal notification.

The long-form notice (several pages) provides detailed information about the proposed settlement, including a summary of the monetary and injunctive terms, the allocation percentages, the requested attorneys' fees, litigation costs and incentive awards, and detailed information on the terms of the releases. In addition, the long-form notice provides information about the fairness hearing date, and Settlement Class members' rights to [\*38] object or opt out (and deadlines and procedures). Finally, the long-form notice included a Claim Form to be completed and returned by Class members. The Claim Form also is available on a dedicated website, [www.RemeronSettlement.com](http://www.RemeronSettlement.com), or by calling a toll-free 800 telephone number provided in the long-form notice and the summary notice.

#### b. Mailed Notice

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<sup>3</sup> Measurement of the notice program is provided in terms of *reach and frequency*. *Reach* is the estimated percentage of a target audience reached through a specific media vehicle or combination of media vehicles. *Frequency* is the estimated average number of times an audience is exposed to advertising vehicles carrying the message.

Direct mail notices consisted of mailing the settlement notice packet (including the long-form notice and a Claim Form) to inform potential class members of their rights and how they could participate in the class action. This direct mail settlement notice packet was sent to all potential TPP class members included in CCS' proprietary TPP mailing database, which includes 13,431 TPPs (e.g., insurance companies, healthcare and welfare funds, self-insureds, etc.) and record keepers (e.g., third-party administrators and pharmacy benefit managers).

In addition, potential consumer class members were contacted by direct mail with the assistance of pharmacies and psychiatrists. Many potential class members were mailed a settlement notice packet by their pharmacy and/or psychiatrist. Twenty-six large national pharmacies participated in mailing [\*39] settlement notice packets to their customers who purchased Remeron and mirtazapine during the claim period, including 14 of the top 25 drug chains, 6 of the top 7 mass merchant pharmacies, and 3 of the top 6 supermarket pharmacies. In all, more than 850,000 settlement notice packets were mailed to potential class members through this program. This direct mail program provided an opportunity to reach those class members who may have missed the summary notice in their newspapers.

c. News Media

CCS implemented a campaign to expand notice through free or "earned" media which included contacting consumer groups such as AARP, mental health groups such as the National Alliance for the Mentally Ill, National Federation for Depressive Illnesses, National Mental Health Association, National Community Pharmacists Association, and issuing a press release over Businesswire. The State Attorneys General have undertaken further efforts to expand notice through the news media. A number of Attorneys General issued press releases about the settlement, notice and claims process, including the toll-free telephone numbers and website address. These press releases were run in newspapers and broadcast on [\*40] the radio.

d. Toll-Free Telephone Number

Complete Claims Solutions has obtained a toll-free telephone number that allows callers to request the notice of settlement and obtain a Claim Form. It also allows them to find out other information about the settlement. This number was included in the summary notice, the notice of settlement, and on the website, [www.RemeronSettlement.com](http://www.RemeronSettlement.com).

e. Internet Website

In addition to the media outlets described above, Complete Claims Solutions developed and maintains a website at [www.RemeronSettlement.com](http://www.RemeronSettlement.com), which can be accessed by the settlement class members. This website includes the summary notice and long-form notice and a Claim Form.

f. Results of Notice Effort

CCS received nearly 65,000 individual consumer claims and 1,156 TPP claims. In addition, over 40,000 visits have been made to the settlement website, and approximately 30,000 telephone calls have been made to the toll-free number.

## 2. The Notice Plan Meets the Requirements of Due Process

"In order [HN14](#) to satisfy due process, notice to class members must be reasonably calculated under all the circumstances, to apprise interested parties of the pendency of the action and afford them an [\*41] opportunity to present their objections." [\*In re AremisSoft Corp. Sec. Litig.\*, 210 F.R.D. 109, 119 \(D.N.J. 2002\)](#) (internal quotations and citation omitted). [HN15](#) In [\*Rule 23\(b\)\(3\)\*](#) actions, "class members must receive the best notice practicable under the circumstances." [\*Id. at 119-20\*](#) (quoting [\*Fed. R. Civ. P. 23\(c\)\(2\)\(B\)\*](#)); see also [\*Varacallo v. Massachusetts Mut. Life Ins. Co.\*, 226 F.R.D. 207, 225 \(D.N.J. 2005\)](#).

The notice forms are similar to those successfully used in numerous other class settlements. See, e.g., [\*In re Toys "R" Us Antitrust Litig.\*, 191 F.R.D. 347 \(E.D.N.Y. 2000\)](#); [\*In re Linerboard Antitrust Litig.\*, 321 F. Supp. 2d 619, 627](#)

(E.D. Pa. 2004). This Court reviewed the summary notice and the long-form notice in detail and suggested several changes, which were made, prior to the preliminary approval of the settlement. The final product is clear and comprehensive, and is written in simple terminology. The notices "fairly, accurately, and neutrally describe the claims and parties in the litigation, the terms of the proposed settlement and the identity of persons [\*42] entitled to participate in it," and apprise affected class members of their options with regard to the proposed settlement. Foe v. Cuomo, 700 F. Supp. 107, 113 (E.D.N.Y. 1988).

**HN16** [↑] For those whose names and addresses cannot be determined by reasonable efforts, notice by publication suffices under both Rule 23(c)(2) and under the Due Process Clause. Carlough v. Amchem Products, Inc., 158 F.R.D. 314, 325 (E.D. Pa. 1993) (citing Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, 317-18, 70 S. Ct. 652, 94 L. Ed. 865 (1950)). Under the circumstances of this case, where End-Payor Plaintiffs, Plaintiff States and Defendants have limited and/or incomplete access to the names or addresses of End-Payers who purchased Remeron during the Class Period,<sup>4</sup> the law requires reasonably feasible notice by publication coupled with such mailed notice. The plan is allocated \$ 2 million for this task and for processing returned Claims Forms, spending over \$ 750,000 on publication notice alone. The Notice Plan meets the requirements of due process.

### [\*43] C. Final Approval of Class Action Settlement

#### 1. State Attorneys' General Authority to Settle All Consumer Claims

Plaintiff **HN18** [↑] States, by their Attorneys General, have the authority to settle and release indirect purchaser claims in a *parens patriae* or other representative capacity. "A State has a quasi-sovereign interest in the health and well being -- both physical and economic -- of its residents in general." Alfred L. Snapp & Son, Inc. v. Puerto Rico, 458 U.S. 592, 607, 102 S. Ct. 3260, 73 L. Ed. 2d 995 (1982). That federal authority is supplemented by state statutory provisions and case law. **HN19** [↑] All Attorneys' General have authority to represent consumers, depending on the state, in at least one of the following four ways: (1) *parens patriae* authority expressly conferred by the state legislature, (2) authority expressly conferred by the state legislature that is the functional equivalent of *parens patriae* authority, (3) judicially recognized authority to represent consumers, or (4) authority to proceed as a class representative of consumers pursuant to Fed. R. Civ. P. 23. See, e.g., In re Lorazepam & Clorazepate Antitrust Litig. ("Lorazepam"), 205 F.R.D. at 386-87. [\*44]

#### 2. Settlements That Meet Certain Conditions Are Presumed Fair

**HN20** [↑] The Third Circuit affords an initial presumption of fairness for a settlement "if the court finds that: (1) the negotiations occurred at arm's length; (2) there was sufficient discovery; (3) the proponents of the settlement are experienced in similar litigation; and (4) only a small fraction of the class objected." In re Cendant Corp. Litig., 264 F.3d 201, 233 n. 18 (3d Cir. 2001). As discussed in Part I above, this case has seen heated litigation between the parties and the review of hundreds of thousands of documents and dozens of depositions. The Plaintiffs' lawyers involved have a great deal of experience in antitrust litigations such as these, as discussed in Part II(A)(1)(d), and favor settlement. Defendants' Counsel, including Dean Ringel of Cahill, Gordon, & Reindel and Joseph Rebein of Shook, Hardy & Bacon, are prominent litigators from successful law firms and also favor settlement.

The Court is also satisfied with the qualifications of State Attorneys General who also favor settlement. Furthermore, **HN21** [↑] "the participation of the State Attorneys General furnishes extra assurance that

<sup>4</sup> **HN17** [↑] The privacy of consumers who purchase prescription medication is protected under the provisions of the Health Insurance Portability and Accountability Act of 1996 (HIPAA), Public Law 104-91. 42 U.S.C. § 1320d-2. HIPAA protects "protected health information" from disclosure. "Protected health information" means individually identifiable health information that is maintained and/or transmitted in any form or medium. 45 C.F.R. § 160.103 (2004). Pharmacists are health care providers covered by the act. Patient authorization is required for disclosure of "protected health information." Improper disclosure may subject the provider to civil and/or criminal penalties. 42 U.S.C. § 1320d-5 and 6. Thus, End-Payor Plaintiffs and Plaintiff States were unable to obtain a list of potential class members for a direct mail campaign and instead had to rely on pharmacies and psychiatrists to forward notices to their customers and patients.

consumers' [\*45] interests are protected." *In re Toys "R" Us Antitrust Litig.*, 191 F.R.D. 347, 351 (E.D.N.Y. 2000); accord *New York v. Reebok Int'l. Ltd.*, 96 F.3d 44, 48 (2d Cir. 1996) (noting that Attorneys General in *parens* actions are motivated by concern for the public interest); *Wellman v. Dickinson*, 497 F. Supp. 824, 830 (S.D.N.Y. 1980).

Finally, there have been few objectors to the settlement, as discussed in Part II(C)(4)(b). This Court determines that an initial presumption of fairness attaches, although such finding is not dispositive.

### 3. Standard for Court Approval of Settlement

**HN22**[]

A class action may be settled under *Rule 23(e)* upon a judicial finding that the settlement is "fair, reasonable, and adequate." *Fed. R. Civ. P. 23(e)(1)(C)*. Under *Rule 23(e)*, this Court must determine whether the settlement is within a range that responsible and experienced attorneys could accept considering all relevant risks and factors of litigation. See *Walsh v. Great Atlantic and Pacific Tea Co.*, 96 F.R.D. 632, 642 (D.N.J. 1983). The range "recognizes the uncertainties of law and fact in any [\*46] particular case and the concomitant risks and costs necessarily inherent in taking any litigation to completion." *Newman v. Stein*, 464 F.2d 689, 693 (2d Cir. 1972).

**HN23**[]

Because a settlement represents an exercise of judgment by the negotiating parties, cases have consistently held that the function of a court reviewing a settlement is neither to rewrite the settlement agreement reached by the parties nor to try the case by resolving issues left unresolved by the settlement. *Bryan v. Pittsburgh Plate Glass Co.*, 494 F.2d 799, 801 (3d Cir. 1974); *Bullock v. Administrator of Kircher's Estate*, 84 F.R.D. 1, 4 (D.N.J. 1979). "The temptation to convert a settlement hearing into a full trial on the merits must be resisted." *Bell Atlantic Corp. v. Bolger*, 2 F.3d 1304, 1315 (3d Cir. 1993).

**HN24**[]

To determine whether the settlement is fair, reasonable and adequate under *Rule 23(e)*, courts in the Third Circuit apply the nine-factor test enunciated in *Girsh v. Jepson*, 521 F.2d 153, 157 (3d Cir. 1975), and recently reaffirmed in *Warfarin Sodium*, 391 F.3d at 534-35. These factors are:

- (a) The complexity, [\*47] expense, and likely duration of the litigation;
- (b) the reaction of the class to the settlement;
- (c) the stage of the proceedings and the amount of discovery completed;
- (d) the risks of establishing liability;
- (e) the risks of establishing damages;
- (f) the risks of maintaining the class action through the trial;
- (g) the ability of the defendants to withstand a greater judgment;
- (h) the range of reasonableness of the settlement fund in light of the best possible recovery; and
  
- (i) the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation.

*Id.* (quoting *Girsh*, 521 F.2d at 156-57).<sup>5</sup>

### **[\*48] 4. Evaluation of the Settlement Under Applicable Standards**

#### a. The Complexity, Expense and Likely Duration of the Litigation

By reaching a favorable settlement prior to dispositive motions or trial, the End-Payor Plaintiffs and Plaintiff States avoided significant expense and delay, and ensured recovery. An "antitrust action is arguably the most complex

<sup>5</sup> When evaluating settlements in *parens patriae* actions brought by state Attorneys General under either the *Clayton Act* or comparable state laws, courts have generally utilized the standards used to analyze private class action settlements under *Rule 23*. See, e.g., *In re Toys "R" Us Antitrust Litig.*, 191 F.R.D. at 352; *New York by Vacco v. Reebok Int'l.*, 903 F. Supp. 532, 535 (S.D.N.Y. 1995); *In re Minolta Camera Prod. Antitrust Litig.*, 668 F. Supp. 456 (D. Md. 1987).

action to prosecute." *In re Linerboard Antitrust Litig.*, 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350, at \*10 (E.D. Pa. June 2, 2004) (citations omitted); see also *Nichols v. Smithkline Beecham Corp.*, 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616, at \*12 (E.D. Pa. Apr. 22, 2005) (same). This litigation involves complicated patent, regulatory, and antitrust laws, including interpretation of provisions of the *Hatch Waxman Act* and their application to antitrust law.

Although the End-Payor Plaintiffs have conducted a substantial amount of discovery, significant additional work would be necessary if this case proceeded beyond the current 12b6 and class certification stages. First, expert witness reports and depositions would need to be undertaken. Then, summary judgment motions would need to be resolved. In the Direct Purchaser case, which recently came to [\*49] a preliminary settlement, thousands of pages of materials were filed with this Court on summary judgment issues such as market definition, market power, and improper / late listing in the FDA Orange Book. These issues would most likely come up again in the End-Payor Plaintiffs' litigation.

Furthermore, a trial on the merits of the action would entail considerable expense: Market definition alone would require dozens of hours of testimony at this stage. Finally, trial would likely not end the litigation, given the right to appeal. This factor weighs in favor of the settlement. See *In re Linerboard Antitrust Litig.*, 292 F. Supp. 2d 631, 642 (E.D. Pa. 2003) (noting that the "protracted nature of class action antitrust litigation means that any recovery would be delayed for several years," and thus settlement's "substantial and immediate benefits" to class members favors settlement approval); *Slomovics v. All for a Dollar, Inc.*, 906 F. Supp. 146, 149 (E.D.N.Y. 1995) (where litigation is potentially lengthy and will result in great expense, settlement is in the best interest of the class members).

#### b. The Reaction Of The Settlement Group

As described [\*50] above in Part II(B)(1)(b), CCS sent out 13,431 notices to third-party payors, and caused the mailing of more than 850,000 notices to potential consumer class members across the country. In addition, CCS developed and maintained a website and a toll-free telephone "hotline" to provide information about the settlement and arranged for publication of the summary notice over a period of approximately six weeks in selected publications throughout the country.

In response, no TPP excluded itself from the settlement,<sup>6</sup> and about 70 individual consumers timely submitted Requests for Exclusion. Given that the TPP portion of the class is made up largely of sophisticated managed care companies, the fact that not one of them wishes to exclude itself is strong evidence of a positive reaction to the settlement. Equally strong evidence is the very low number of consumer opt-outs relative to the hundreds of the thousands notified and the tens of thousands who submitted claims forms.

[\*51] Also relevant is the number of objections. Eight individuals and two TPPs filed objections.<sup>7</sup> [\*52] This Court has considered all of the objectors' written submissions<sup>8</sup> and the three oral arguments that were made at the Fairness Hearing. The non-monetary objections that have been filed are the following: (1) the name of the charity that would receive left over funds has not been disclosed, (2) Rider A, a confidential attachment to the settlement agreement containing provisions regarding the number of opt-outs that would lead to termination of the settlement, was not disclosed, (3) consumer information should have been subpoenaed from the ten largest retail pharmacies

<sup>6</sup> Five TPPs did initially opt out, but they soon entered into an agreement with the parties to request that the Court permit them to rescind their notices of exclusion. That agreement is reflected in a Memorandum of Understanding filed with the Court that guaranteed \$ 450,000 more to the Settlement Fund, instead of going to Plaintiffs' Attorneys' Fees. The Court granted the request.

<sup>7</sup> Two objections were filed on behalf of TPPs, Health Care Service Corporation and certain Blue Cross entities; and eight were filed by consumers, Eugene Clasby, Roberta Geha, Rhonda Marcus, Nadine Street, William L. Bedford, Susan Ruth Hall, Dot K. Kensinger, and Robert L. Kensinger. The objections by the latter five individuals were filed by the same attorney, Stephen Tsai, who spoke at the Fairness Hearing.

<sup>8</sup> As some objection points are entirely unsupported, too vague to comprehend, or clearly without merit, the Court only writes on those objections that require some explanation.

and those consumers should have received direct payments without having to file Claims Forms, and (4) the settlement should not contain a boilerplate provision that allows for modification of the settlement without notice to the class, despite agreement by the settling parties and Court approval, and (5) 30 days after the 45-day notice period was an insufficient amount of time to object to the settlement and the 45-day notice period was an insufficient amount of time to opt-out of the settlement.

These objections are considered in turn. First, [HN25](#) when providing notice, the law does not require that the charity that may receive left over funds be disclosed in notice to the class. See [\*Mangone v. First USA Bank, 206 F.R.D. 222, 230 \(S.D. Ill. 2001\)\*](#) ("Courts have broad discretion in distributing unclaimed class funds, and where the parties agree on the distribution of unclaimed class funds, the court should defer to that method of distribution.") (citing [\*Wilson v. Southwest Airlines, Inc., 880 F.2d 807, 815-16 \(5th Cir. 1989\)\*](#) (where parties agree to distribution of unclaimed class fund, and agreed distribution is equitable, court will defer to such agreement)). More importantly, this objection is moot as the claims administrator has advised that there are no surplus funds because of the high response to the notice.

Second, Courts have held that [HN26](#) information regarding conditions that [\*53] may terminate a settlement need not be detailed in the notice to the class. See [\*In re Warfarin Sodium Antitrust Litig., 212 F.R.D. 231, 253 \(D. Del. 2002\)\*](#) (stating that notice did not need to include details on "the confidential opt-out' threshold beyond which defendant reserved the right to withdraw from the settlement"). The Court, the Attorneys General, and Class Counsel know the contents of Rider A and agreed to its sealing in the interest of consummating the settlement. The Rider has no legitimate bearing on a class member's decision to opt-out of the settlement, object, or file a claims form.

Third, the suggested subpoenas of the top 10 retail pharmacies is unnecessary given that 14 of the top 25 pharmacy chains, 3 of the top 6 supermarket, and 6 of the top 7 mass merchant retailers voluntarily participated in searching their databases for Remeron purchasers and sending notices with Claims Forms to them. This process led to 800,000 notices being sent and nearly 65,000 consumer claims being filed. As to the objector's additional suggestion to automatically distribute money to those who purchased Remeron through a top 10 pharmacy, this Court will not favor one [\*54] group of class members over another. See, e.g., [\*In re Diet Drugs Prods. Liab. Litig., 93 Fed. Appx. 338, 343 \(3d Cir. 2004\)\*](#) ("a class action settlement cannot arbitrarily prefer one group of plaintiffs over another -- because such a rule would be inimical to the very principles of class advocacy"). In addition, there are practical problems with the suggestion, including those associated with blindly sending checks to addresses that may be outdated.

Fourth, the boilerplate provision that allows for modification of the settlement without notice to class is satisfactory and necessary. The class is protected from adverse modifications by [Rule 23](#) and the requirements of due process, regardless of what the provision says, and the Court is charged with enforcing these protections. [HN27](#) Minor modifications may be necessary to a settlement agreement (indeed may be favorable to the class), and additional class notice is not always required because, e.g., of the cost of notice that would take recovered money from the class. See [\*In re Prudential Ins. Co. of Am. Sales Practices Litig., 962 F. Supp. 450, 473 n.10\*](#) ("Class members need not be informed of the [amendment [\*55] to the settlement agreement] because the [settlement] is only more valuable with these changes"). In this case, the adjustment that was made to the settlement that favored the class, after notice went out, was followed by additional notice and by opportunity for any opt-outs to return to the class in order to partake in the additional recovery.<sup>9</sup>

Fifth, 30 days after a 45-day notice period is a sufficient amount of time to object to the settlement. This Court suggested this deadline to Plaintiffs' Counsel shortly after the preliminary fairness hearing. Many district courts have set a similar deadline in antitrust class action settlements. In [\*In re Augmentin Antitrust Litig.\*](#) (Case No. 02-CV-442, E.D. Va.), Judge Morgan approved a forty-five day notice period and set the opt-out and objection deadline two weeks from the close of the notice period. In [\*In re Buspirone Antitrust Litig.\*](#) (Case No. 01-CV-7951-JGK, S.D.N.Y),

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<sup>9</sup> See *supra* note 6.

Judge Koeltl set the opt-out and objection deadline forty-five [\*56] days after the notice date. And in *In re Lorazepam & Clorazepate Antitrust Litig.* (Case No. 99-276-TFH/JMF, D.D.C.), Judge Hogan also set the objection deadline forty-five days after the notice date. Indeed, the objector Health Care Service Corporation, submitted its objection on May 16, 2005, two weeks before the May 28, 2005 objection deadline, thus revealing the adequacy of the objection period.

As to the opt-out deadline, this Court passes no judgment because the issue is moot. Of over 800,000 notices only two objections were made stating insufficient time to opt-out during the 45-day notice period. On the other hand, at least 65,000 class members chose not to opt-out, as evidenced by their filing of claims forms. At the Fairness Hearing, both objectors on this issue took the opportunity to be heard. Counsel to Health Care Service Corporation informed the Court at the Fairness Hearing that, despite objecting, the company did not wish to opt-out. Counsel to Nadine Street, the other objector in this regard, also spoke at the Fairness Hearing. Rather than expressing a desire to opt-out of the settlement, the lawyer requested additional time to forge an objection to Plaintiffs' [\*57] motion for attorneys' fees, which the Court granted, as discussed in Part II(E)(1)(b). Thus, the issue is moot.

Six additional objection points were made pertaining to the class's compensation. They are the following: (1) one group in the class (TPPs or individual consumers) is getting more than its fair share than the other group, (2) the Plan of Distribution's reliance on "expenditures" rather than "damages" is inappropriate and unfairly benefits TPPs, (3) claim rates of the TPPs or individual consumers should not be considered in distributing monies between the two groups, (4) money should "spill over" from the individual consumers' allocation to the TPPs' allocation before any money is made available for a *cy pres* distribution, (5) the individual consumers are not receiving sufficient compensation, and (6) class members from states whose antitrust laws do not provide for the recovery of damages to indirect purchasers should not receive compensation.

These objections are also considered in turn. First, both the TPP group and the individual consumer group make the same argument that the other group is getting more than it should. Two (of two) TPP objectors contend that they [\*58] are entitled to more than the Plan of Distribution's dedicated 50.7%, while at the same time five (of seven) individual consumers contend that the individuals are entitled to more than the Plan of Distribution's dedicated 32.8%. As discussed in Part II(D), the Court finds the Plan of Distribution to be fair. These conflicting objections are without merit.<sup>10</sup>

Second, the reasons put forth as to why reliance on "expenditures" would be inappropriate is inapplicable here. The objector, Eugene Clasby, is concerned that damages based on the end-payors [\*59] "expenditures" would be skewed in favor of TPPs because such a measurement would not discount for co-payments paid by individual consumers or for certain rebates received by TPPs. However, the "expenditures" data used in this case in fact does factor in these offsets. Furthermore, [HN28](#)<sup>11</sup> the Third Circuit has approved settlement allocations based on expenditures rather than damages, see [\*In re Warfarin Sodium Antitrust Litig.\*, 391 F.3d at 539](#), and this precise objection by Eugene Clasby was overruled in [\*Nichols v. SmithKline Beecham Corp.\*, 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616, \\*18 \(E.D. Pa. Apr. 22, 2005\)](#).

Third, claim rates were not a factor in determining the Plan of Distribution's distribution percentages. The allocation is based on each group's expenditures. That TPPs might be more likely to claim their damages did not give them a higher percentage of the Settlement Fund.

Fourth, the issue of "spill over" from individual consumers to TPPs prior to any *cy pres* distribution is moot. The claims administrator has reported that consumer claims already exceed the amount available to them by a very wide margin, thus no funds remain for a *cy pres* distribution or a transfer [\*60] to the TPPs.

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<sup>10</sup> Several objectors also objected that they did not have access to the economic reports that were the basis of the Plan of Distribution, and objector Eugene Clasby made a motion to this effect. As a result, the Court ordered that End-Payor Plaintiffs make this underlying information available prior to the Fairness Hearing, which they did. The objection was not pursued at the Fairness Hearing and one TPP objector, the Blue Cross entities, withdrew its relevant objections.

Fifth, the individual consumers are receiving adequate compensation. They are receiving an estimated \$ 8.1 million in the aggregate which, based on the estimated number of claims filed, will result in each claiming consumer receiving approximately 34 cents for every dollar spent on Remeron. Discounting for litigation risk, cost, and delay, as discussed in Part I and Part II(C)(4), this Court cannot find that such a recovery is inadequate.

Sixth, class members from states whose antitrust laws do not provide for the recovery of charges to indirect purchasers should still receive compensation if the parties agreed to it. An important part of a settlement like this one is that Defendants achieve "total peace," thus all potential plaintiffs must be compensated in order to preclude future litigation attempts and allow such a settlement to consummate. See *In re Chicken Antitrust Litig.*, 669 F.2d 228, 238 (5th Cir. 1982). Furthermore, Plaintiffs are being compensated not just for state antitrust law violations but also for the common law claim of unjust enrichment. These two objectors, both represented by Stephen Tsai, provide no legal authority for their position [\*61] nor do they at all consider that the Settlement Fund would likely have been much smaller if end-payors from certain states were barred from compensation (assuming the settlement would still have been consummated at all). The objection is without merit.

#### c. The Stage of the Proceedings and the Amount of Discovery Completed

**HN29** [↑] In examining the stage of the litigation at which a settlement was reached, the proper question is "whether counsel had an adequate appreciation of the merits of the case before negotiating." *Warfarin Sodium*, 391 F.3d at 537. Under this standard, End-Payor Plaintiffs and the Plaintiff States were clearly in a position to make the necessary risk assessments in the context of settlement negotiations. As discussed in Part I, End-Payor Plaintiffs conducted an extensive economic and factual investigation, including review hundreds of thousands of pages of documents and data produced by Defendants and third parties, taking depositions of many current or former employees of the Defendants, and consultation with counsel for the Direct Purchasers, counsel for the Generic Manufacturers, the State Attorneys General, and others.

The Office of the Attorney General [\*62] of Texas also began an investigation into Defendants' alleged Remeron monopoly maintenance practices in March 2003, and a multi-state working group was formed in July 2003 with several other State Attorneys General to pursue that investigation. The investigation included issuance of Civil Investigative Demands to Defendants and third parties, and review of documents produced. In cooperation with the Federal Trade Commission, the Plaintiff States conducted interviews of experts, potential experts, and potential witnesses. The Plaintiff States reviewed and analyzed thousands of documents from the Defendants' voluminous production, and read numerous deposition and hearing transcripts.

**HN30** [↑] "The pursuit of early settlement is a tactic that merits encouragement; it is entirely appropriate to reward expeditious and efficient resolution of disputes." *In re Vitamins Antitrust Litig.*, 1999 U.S. Dist. LEXIS 21963, 1999 WL 1335318, at \*4 (D.D.C. Nov. 23, 1999). "Early settlements benefit everyone involved in the process and everything that can be done to encourage such settlements, especially in complex class action cases, should be done." *In re M.D.C. Holdings Sec. Litigation*, 1990 U.S. Dist. LEXIS 15488, 1990 WL 454747, at \*7 (S.D. Cal. Aug. 30, 1990) [\*63]. Given the extensive amount of time devoted to this case, End-Payor Plaintiffs and Plaintiff States have obtained sufficient information to adequately evaluate the merits of their claims.

#### d & e. The Risks of Establishing Liability and Damages

**HN31** [↑] These two factors "survey the potential risks and rewards of proceeding to litigation in order to weigh the likelihood of success against the benefits of an immediate settlement." *Warfarin Sodium*, 391 F.3d at 537. End-Payor Plaintiffs and the Plaintiff States initially proceeded against Defendants on four theories of antitrust liability: (1) Fraud on the PTO in connection with the prosecution and obtaining of the 099 patent; (2) wrongful listing of the 099 patent in the Orange Book; (3) sham patent litigation against generic competitors based on the 099 patent; and (4) late listing of the 099 patent.

This Court issued a series of rulings that limited the possibility of Plaintiffs achieving ultimate success on the merits. First, regarding the Generic Manufacturers' claims against Organon, the Court on December 3, 2003 dismissed those antitrust claims that were based on the theory that the 099 Patent [\*64] was improperly listed in the Orange

Book. The Court held that "the then existing statute and regulation, [21 U.S.C. §§ 355\(b\)\(1\)](#) and [\(c\)\(2\)](#) and [21 C.F.R. § 314.53\(b\)](#), gave Organon a reasonable basis for listing in the Orange Book." [Organon Inc. v. Mylan Pharms., Inc., 293 F. Supp. 2d 453, 459 \(D.N.J. 2003\)](#). The Court also dismissed the allegations that Organon initiated sham patent infringement lawsuits against the Generic Manufacturers, ruling that Organon's infringement theory was reasonable, in large part because of the existence at the time of three district court decisions allowing such claims against Generic Manufacturers.

Although these rulings were made in the litigation involving the Generic Manufacturers, this Court applied those rulings to the Direct Purchaser litigation (and, by inference, to this litigation) under the doctrine of collateral estoppel or the doctrine of law of the case. [Walgreen Co. v. Organon, Inc. \(In re Remeron Antitrust Litig.\), 335 F. Supp. 2d 522, 526, n.4 \(D.N.J. 2004\)](#). This Court also dismissed the Direct Purchasers' antitrust claims based on fraud on the PTO in that Opinion.

As a result of [\*65] these rulings, the late listing claim is, for practical purposes, the only remaining claim in End-Payor Plaintiffs' and the Plaintiff States' case.<sup>11</sup> Without this settlement, this final claim would need to survive summary judgment, where the definition of the relevant antitrust market would be the dominant threshold issue. In the Direct Purchaser case, this Court denied the Direct Purchaser class's motion for summary judgment regarding their proposed antitrust market definition and whether the Defendants had monopoly power in that market. [In re Remeron Direct Purchaser Antitrust Litig., 367 F.Supp.2d 675 \(D.N.J. 2005\)](#). This Court held that the "direct evidence" the plaintiffs put forth was, on its own, insufficient to establish monopoly power. Thus, unless End-Payor Plaintiffs could perhaps put forth more convincing direct evidence than that of the Direct Purchaser plaintiffs, End-Payor Plaintiffs would need to use the traditional market definition approach in order to demonstrate monopoly power, thus increasing the risk of losing of merits and significantly increasing the amount of discovery and expert analysis needed.

[\*66] Finally, trial itself would be risky to Plaintiffs on their one surviving claim. See e.g., [In re Brand Name Prescription Drugs Antitrust Litig., 186 F.3d 781, 785 \(7th Cir. 1999\)](#) (plaintiff class suffered directed verdict after eight weeks of trial); [United States Football League v. Nat'l Football League, 644 F.Supp. 1040 \(S.D. N.Y. 1986\), aff'd, 842 F.2d 1335 \(2d Cir. 1988\)](#) (antitrust jury awarded \$ 1.00 in nominal damages to successful plaintiffs). These risks of proving liability and damages weigh in favor of approving this settlement.

#### f. Risks of Maintaining Class Action Status Through Trial

[HN32](#) [↑] "Because the prospects for obtaining certification have a great impact on the range of recovery one can expect to reap from the [class] action, this factor measures the likelihood of obtaining and keeping a class certification if the action were to proceed to trial." [Warfarin Sodium, 391 F.3d at 537](#) (internal quotes and citation omitted). The End-Payor Plaintiffs moved for class certification on October 27, 2003. As a result of the settlement discussions that began shortly thereafter, the Defendants' response to the class [\*67] certification motion was extended to April 12, 2004. The Defendants never filed their response, as the settlement had been tentatively reached by the time their response was due. Consequently, the record does not reflect vigorous opposition, but class certification throughout trial is not guaranteed. This factor neither favors nor disfavors settlement.

#### g. Defendants' Ability to Withstand a Greater Judgment

The parties do not contend that Defendants could not withstand a larger judgment. However, [HN33](#) [↑] many settlements have been approved where a settling defendant has had the ability to pay greater amounts. See, e.g., [Warfarin Sodium, 391 F.3d at 538](#) ("The fact that DuPont could afford to pay more does not mean that it is obligated to pay any more than what the . . . class members are entitled to under the theories of liability that existed at the time the settlement was reached."); [Young Soon Oh v. AT & T Corp., 225 F.R.D. 142, 150-51 \(D.N.J. 2004\)](#); [In re Linerboard Antitrust Litig., 321 F. Supp. 2d 619, 632 \(E.D. Pa. 2004\)](#); [Erie County Retirees Assoc. v. County of Erie,](#)

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<sup>11</sup> To the extent End-Payor Plaintiffs and the Plaintiff States would advance an "overall scheme" claim, finding such a scheme would likely be predicated upon proving the late listing claim.

[Pennsylvania, 192 F. Supp. 2d 369, 376 \(W.D. Pa. 2002\)](#); [\[\\*68\] Lazy Oil Co. v. Witco Corp., 95 F. Supp. 2d 290, 318 \(W.D. Pa. 1997\)](#). This factor does not favor nor disfavor settlement.

h & i. The range of reasonableness of the settlement fund in light of the best possible recovery and all the attendant risks of litigation.

[HN34](#) [↑] A court evaluating a proposed class action settlement should also consider "whether the settlement represents a good value for a weak case or a poor value for a strong case." [Warfarin Sodium, 391 F.3d at 538](#); [Girsh, 521 F.2d at 157](#) (court must examine the range of reasonableness of the settlement fund to a possible recovery in light of all the attendant risks of litigation); see also [Hammon v. Barry, 752 F. Supp. 1087, 1095 \(D.D.C. 1990\)](#) (court must "evaluate the strengths and weaknesses of class members' claims within the framework of their likelihood of establishing liability and damages at trial"). In the process, however, a court must "avoid deciding or trying to decide the likely outcome of a trial on the merits." [In re National Student Marketing Litigation, 68 F.R.D. 151, 155 \(D.D.C. 1974\)](#).

Continued litigation of this lawsuit would require further [\[\\*69\]](#) decisions by the Court on (a) End-Payor Plaintiffs' pending class certification motion, (b) Defendants' pending motion to dismiss the End-Payor Plaintiffs' Amended Consolidated Complaint, (c) future summary judgment motions, and (d) at trial.

#### (i) Estimated Damages

On the basis of estimates by End-Payor Plaintiffs' expert economists, the maximum antitrust single damages totaled \$ 109,704,738.00. Economists retained by the Plaintiff States reached a similar estimate of antitrust single damages for settlement purposes. These estimates likely overstate the amount of damages that would be available to Plaintiffs absent this settlement, because they were compiled before the Court issued its decisions that effectively limited End-Payor Plaintiffs' and Plaintiff States' claims to only a late listing claim. This claim has a shorter period of antitrust injury than some of the others.

#### (ii) Comparison of the Settlement Amount to Estimated Damages and Weighed Against the Risks of Non-Recovery

In order [HN35](#) [↑] to evaluate the propriety of an antitrust class action settlement's monetary component, a court should compare the settlement recovery to the estimated single damages. [In re Ampicillin Antitrust Litigation, 82 F.R.D. 652, 654 \(D.D.C. 1979\)](#) [\[\\*70\]](#) (citing [Detroit v. Grinnell Corp., 495 F.2d 448 \(2d Cir. 1974\)](#)). Although in certain circumstances a plaintiff class may recover treble damages if it prevails at trial, that result is far from certain. Moreover, in the present case, End-Payor Plaintiffs and Plaintiff States represent consumers pursuant to state laws that provide for varying levels of recovery -- some provide only for recovery of equitable relief, and many do not provide for recovery of treble damages.

As the Second Circuit emphasized in [Detroit v. Grinnell Corp, 495 F.2d at 455](#), an antitrust class action settlement may be approved even if the settlement amounts to a small percentage of the single damages sought, if the settlement is reasonable relative to other factors, such as the risk of no recovery. "In fact there is no reason, at least in theory, why satisfactory settlement could not amount to a hundredth or even a thousandth part of a single percent of the potential recovery." *Id.*

Relative to maximum estimated damages of \$ 109,704,738, the Settlement Consideration represents about one-third of single damages, quite a substantial recovery, especially given that three of the [\[\\*71\]](#) initial four theories of antitrust liability can no longer be advanced. This recovery must, of course, be weighed against the substantial risks of continued litigation, including future risks at summary judgment and trial. The Court is satisfied that the settlement agreement accounts for the risks inherent in this complex litigation and provides appropriate relief in light of these risks.

#### j. Conclusion

Given this Court's analysis, the Court concludes that the nine-factor test utilized by the Third Circuit is satisfied. The settlement is fair, adequate, and reasonable under [Federal Rule of Civil Procedure 23\(e\)](#).

#### D. Approval Of The Plan of Distribution

**HN36** [↑] "As with settlement agreements, courts consider whether distribution plans are fair, reasonable, and adequate." *FTC v. Mylan Labs., Inc. (In re Lorazepam & Clorazepate Antitrust Litig.)*, 205 F.R.D. 369, 381 (D.D.C. 2002); see also *In re Vitamins Antitrust Litig.*, 2000 U.S. Dist. LEXIS 8931, 2000 WL 1737867, at \*6 (D.D.C. Mar. 31, 2000). "In evaluating the formula for apportioning the settlement fund, the Court keeps in mind that district courts enjoy broad supervisory powers over the administration of class [\*72] action settlements to allocate the proceeds among the claiming class members equitably." *Hammon v. Barry*, 752 F. Supp. 1087, 1095 (D.D.C. 1990) (internal quotation marks and citations omitted); accord *In re "Agent Orange" Prod. Liability Litig.*, 818 F.2d 179, 181 (2d Cir. 1987).

At the Court's request, End-Payor Plaintiffs' Co-Lead Counsel and State Liaison Counsel jointly proposed a Plan of Distribution to the Court. As described in the long form notice, the Plan of Distribution is as follows:

32.8% of the Net Settlement Fund will be allocated to consumers ("Consumer Fund"), 16.5% of the Net Settlement Fund will be allocated to state governmental purchasers ("State Fund"), and 50.7% of the Net Settlement Fund will be allocated to Third-Party Payors ("TPP Fund"). Consumers who submit valid claims will receive a *pro rata* share of the Consumer Fund based on the amount he or she paid for Mirtazapine Products during the Class Period, and on how many other consumers file valid claims, and the amount they paid for Mirtazapine Products during the Class Period. Third-Party Payors who submit valid claims will receive a *pro rata* share of the [\*73] TPP Fund based on the amount paid by that entity for Mirtazapine Products during the Class Period and on how many other Third-Party Payors file valid claims, and the amount they paid for Mirtazapine Products during the Class Period. The maximum payment to any Class Member may be limited to 100% of the amount that Class Member paid for Mirtazapine Products during the Class Period.

This distribution plan was based on Plaintiffs' expert economists' findings, using data produced by defendants and the Plaintiff States, as well as CMS statistics and data from other reliable sources. These calculations were performed in anticipation of the mediation of this case, and they were used in the mediation and submitted to the Court confidentially during the mediation.

Kim Van Winkle, Liaison Counsel for the Plaintiff States, informed the Court by affidavit and orally at the Fairness Hearing that she reviewed the proposed allocation on behalf of consumers and the Plaintiff States and concluded it is fair, reasonable and adequate for consumers and Plaintiff States. Similarly, Kevin Love, counsel for Vista Healthplan Inc., informed the Court that he reviewed the proposed allocation, and also concluded [\*74] that it is fair, reasonable and adequate for TPPs. Mr. Love retained and consulted with a separate expert economist for TPPs only in reaching his conclusion.

As the Plan of Distribution appears fair based on the experts' calculations, and all three groups of Plaintiffs including the Attorneys General support it, and the few related objections that have been made were overruled in Part II(C)(4)(b), this Court gives the plan final approval.

#### E. Plaintiffs' Motion for Award of Attorneys' Fees, Interest, Reimbursement of Expenses, and Incentive Awards.

Class Counsel request that the Court award attorney fees in the amount of \$ 7.8 million plus interest accrued on that amount since it has been held in escrow. The \$ 7.8 million requested fee represents 23.6% of the \$ 33 million Settlement Fund.<sup>12</sup> Class Counsel also request recovery of reasonable litigation expenses and incentive awards to named Plaintiffs.

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<sup>12</sup> Class Counsel initially indicated they would request up to 25% of the Settlement Fund, as indicated in the notice that was sent to the class. They later reduced that number by providing \$ 450,000 more to the class in order to prevent the terms of Rider A from terminating, as described in footnote 6.

[\*75] 1. Attorneys' Fees and Interest

This Court first finds that the percentage of fund method is the proper method for compensating Plaintiffs' Counsel in this common fund case. See, e.g., *Krell v. Prudential Ins. Co. of Am. (In re Prudential Ins. Co. Am. Sales Practice Litig. Agent Actions)*, 148 F.3d 283, 333 (3d Cir. 1998) (stating "the percentage of recovery method is generally favored in cases involving a common fund, and is designed to award fees from the fund in a manner that rewards counsel for success and penalizes it for failure"); *Welch & Forbes, Inc. v. Cendant Corp. (In re Cendant Corp. Prides Litig.)*, 243 F.3d 722, 734 (3d Cir. 2001) (stating "the percentage-of-recovery method has long been used in this Circuit in common-fund cases").

**HN37** [↑] The Third Circuit set forth with specificity the factors that a court should consider in evaluating such requested attorneys' fees in *Gunter v. Ridgewood Energy Corp.*, 223 F.3d 190, 195 (3d Cir. 2000) (overturning a decision that reduced a requested fee of 25% of the recovered fund to 18%). The *Gunter* factors "need not be applied in a formulaic way, and their weight may vary on a case-by-case basis." *Oh v. AT & T Corp.*, 225 F.R.D. 142, 146 (D.N.J. 2004) [\*76] (citing *Gunter*, 223 F.3d at 195). The *Gunter* factors include (a) the size of the fund created and number of persons benefitting from the settlement, (b) the presence/absence of substantial objections to the fee, (c) the skill of Plaintiffs' counsel, (d) complexity and duration of the litigation, (e) the risk of nonpayment, (f) amount of time devoted to the litigation, (g) awards in similar cases. See *Gunter*, 223 F.3d at 195; *In re Aremissoft Corp. Sec. Litig.*, 210 F.R.D. 109, 129 (D.N.J. 2002).

## a. The size of the fund created and the number of persons benefitted by the settlement

Pursuant to the parties' settlement agreement, the class will obtain an immediate and certain benefit of \$ 33 million plus accrued interest, less attorneys fees, expenses and incentive award payments as awarded by the Court. Over 65,000 individuals and entities will receive significant financial benefit, without having to go through the time, expense, and risk of continued litigation.

## b. The presence or absence of substantial objections to the request for fees

In response to the Notice Plan, only one TPP and seven individual consumers objected to the [\*77] payment of the requested attorneys' fees. Of the seven individuals, four are represented by the same counsel and filed near verbatim statements.<sup>13</sup> The presence of a handful of objections does not mean that the requested fee should be denied. Cf. *In re Lloyd's American Trust Fund Litig.*, 2002 U.S. Dist. LEXIS 22663, 2002 WL 31663577, \*3, \*38 (S.D.N.Y. Nov. 26, 2002) (approving fee request of 28% of settlement fund, even though 18% of class members filed objections to the settlement on one or more grounds); *In re Auto. Refinishing Paint Antitrust Litig.*, 2004 U.S. Dist. LEXIS 29162 (E.D. Pa. Oct. 13, 2004) (stating that, where nearly 60,000 notices sent out and only three objections were received, the vast majority of the class members had no objection, which counseled in favor of a 32% fee award).

The single TPP objection was filed by Health Care Service Corporation. In its papers, it objected that 30 [\*78] days after the close of the 45-day Notice Period was an insufficient amount of time to file its objections and that Class Counsel do not deserve their fee request. These objections were made without any legal support and were made in a total of three sentences. The TPP's objections are overruled. 30 days after the close of the 45-day Notice Period is a sufficient amount of time to forge an objection, as discussed in Part II(C)(4)(b). Further, Plaintiffs' Counsel did provide support in the record for their time spent litigating case and their contribution to the litigation process has been explained throughout this Opinion.

Objector Nadine Street initially objected that the (a) distribution to Plaintiffs' Counsel should be reduced to 15%, and that (b) Ms. Street did not have sufficient information to further support its objection because the deadline for filing

<sup>13</sup> These are the objections of Dot K. Kensigner, William L. Bedford III, Susan Ruth Hall, and Robert L. Kensinger, represented by Stephen Tsai.

objections coincided with Plaintiffs' deadline for filing its motion for attorneys' fees. As a result, at the Fairness Hearing, the Court granted an extension of time to file objections regarding attorneys' fees so that End-Payor Plaintiffs' brief in support of attorneys' fees could be more fully considered by objectors.

Only [\*79] Ms. Street took this opportunity, filing a second objection which further explained her claim that only a 15% distribution to Plaintiffs' Counsel was warranted. The bases were essentially that several law firms were not necessary to litigate Plaintiffs' claims and that Plaintiffs' papers in favor of their fee request were deficient. Based on the complexity of this case as explained in Part I and Part II(C)(4), and based on the supporting documentation in favor of granting Plaintiffs' attorney fees request, this Court finds Ms. Streets's objections to be without merit.<sup>14</sup>

[\*80] The nearly identical objections of Dot K. Kensinger, William L. Bedford III, Susan Ruth Hall, and Robert L. Kensinger claimed that Class Counsel should not be allowed a percentage of the \$ 33 million Settlement Fund that was created but rather such fund should first be discounted by the 16.5% portion going to the State Attorneys General. The objections state that the State Attorneys General "are already being paid \$ 1 million in fees for their recovery of the 16.5% that is being paid to the states."

The Court understands the thrust of the objection; however, Plaintiffs' Counsel were largely responsible for creating a \$ 35 million benefit for the class (\$ 33 million Settlement Fund and \$ 2 million Notice Fund). Class Counsel took the lead in creating that fund for the states. The States Attorneys General have not objected to Class Counsel's fees and have endorsed the settlement. The objection is without merit.

The remaining objectors are Rhonda Marcus and Robert Geha. Both of them take issue with the percentage of recovery counsel requests but provide little substantiation of why the percentage is excessive. In light of the consideration of the below factors that consider Plaintiffs' [\*81] Counsel fee award, these two objections are also without merit. **HN38**<sup>↑</sup> The courts do not hesitate to grant attorneys' fees despite the presence of objections when the rationale for awarding fees outweighs the objections. See e.g., *Nichols v. Smithkline Beecham Corp.*, 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616, at \*21 (E.D. Pa. Apr. 22, 2005) (awarding 30% fee despite six substantive objections to settlement, three of which mentioned attorneys' fees); *Oh*, 225 F.R.D. at 152 (awarding fee despite three objections); *In re Rite Aid Corp. Sec. Litig.*, 396 F.3d 294, 305 (3d Cir. 2005) (affirming district court's finding that only two objections weighed in favor of awarding fee); *Varacallo*, 226 F.R.D. at 251 (awarding fee despite almost 50 objections in large class case).

**HN39**<sup>↑</sup> The absence of meaningful class member objection to the proposed fee ordinarily supports the reasonableness of the request. See *In re Rite Aid Corp. Secs. Litig.*, 146 F. Supp. 2d 706, 735 (E.D. Pa. 2001); *In re Orthopedic Bone Screw Prods. Liab. Litig.*, 2000 U.S. Dist. LEXIS 15980, 2000 WL 1622741, at \*6 (E.D. Pa. 2000). Further, a working group of State Attorneys General, who worked alongside Class Counsel, [\*82] have concluded that the proposed settlement terms, including Class Counsel's request for attorneys' fees, is fair and appropriate.

#### c. The skill of Plaintiffs' counsel

This settlement was achieved by Class Counsel who include some of the preeminent antitrust firms in the country with decades of experience in prosecuting and trying complex actions, as described in Part II(A)(1)(d). Class Counsel have considerable experience in FDA regulatory matters through other generic drug litigations. The settlement result achieved is a reflection of counsel's skill and expertise. See *In re Warfarin Sodium Antitrust Litig.*, 212 F.R.D. 231, 261 (D. Del. 2002) (class counsel "showed their effectiveness through the favorable cash settlement they were able to obtain"); see also *In re Ikon Office Solutions, Inc. Sec. Litig.*, 194 F.R.D. 166, 194 (E.D. Pa. 2000) (awarding 30% fee and stating "the most significant factor in this case is the quality of representation, as

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<sup>14</sup> Ms. Street also objected to the agreement between the litigating parties and five TPPs that initially opted out of the settlement which stated that, *inter alia*, Defendants would advance up to \$ 500,000 if they rescinded their notices of exclusion. By Order dated June 24, 2005, this Court rejected that part of the agreement, and the five TPPs were afforded absolutely no special treatment in exchange for returning to the class. Thus, Ms. Street's objection as to this point had been resolved before the objection was filed. See also *supra* notes 6 and 9 and accompanying text.

measured by the quality of the result achieved, the difficulties faced, the speed and efficiency of the recovery, the standing, experience and expertise of the counsel, the skill and professionalism with [\*83] which counsel prosecuted the case and the performance and quality of opposing counsel").

d. The complexity and duration of the litigation

"As to the complexity of the case, an antitrust class action is arguably the most complex action to prosecute." *In re Linerboard Antitrust Litig.*, 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350, at \*10 (E.D. Pa. June 2, 2004) (quoting *In re Motorsports Merchandise Antitrust Litig.*, 112 F. Supp. 2d 1329, 1337 (N.D. Ga. 2000)). This matter is extremely complicated, involving the patent, regulatory and antitrust laws, including interpretation of complex provisions of the *Hatch Waxman Act*, as discussed throughout this Opinion.

The discovery process in this case was difficult. Class Counsel (i) reviewed over 800,000 million documents, (ii) for a time, held regular lengthy conference calls with Defendants that resulted in contentious debate and multiple motions to compel, which were briefed and argued before the Court, and (iii) participated in over fifty depositions, most of which were technical and complicated covering subjects such as Orange Book listing protocol and the science relating to the chemical composition of mirtazapine products.

[\*84] Further, [HN40](#)[] the circumstances surrounding a difficult settlement increase the complexity of a case. Cf. *Reinhart v. Lucent Techs., Inc.* (*In re Lucent Techs., Inc., Sec. Litig.*), 327 F. Supp. 2d 426, 434 (D.N.J. 2004). Here, they were lengthy and difficult. Class Counsel coordinated the settlement on behalf of End-Payor Plaintiffs and among 56 states and territories. Class Counsel also dealt with the negotiation of opt-out members. Class Counsel's ability to successfully navigate these hurdles enabled the settlement to come to fruition.

e. The risk of nonpayment

The instant case was presented with significant obstacles since its filing. If the settlement is not consummated, class members may very well receive nothing. End-Payor Plaintiffs and the Plaintiff States proceeded against Defendants on four theories of liability: (1) Fraud on the U.S. Patent and Trademark Office ("PTO") in connection with the prosecution and obtaining of the 099 patent; (2) wrongful listing of the 099 patent in the Orange Book; (3) sham patent litigation against generic competitors based on the 099 patent; and (4) late listing of the 099 patent. As described in Part II(C)(4), three of these claims face dismissal by [\*85] this Court due to dismissals of such claims in the Generic Manufacturer and Direct Purchaser cases. The Plaintiffs would most likely have been left with their late listing claim and would still have to defeat summary judgment and win at trial. Accordingly, risk of non-payment in this case weigh heavily in favor of approving the requested fee.

f. The amount of time devoted to the litigation

Plaintiffs' counsel have spent over 12,000 combined hours in prosecuting this case on behalf of the class. The complexity of this action required a significant amount of work by a number of attorneys. Class Counsel performed investigations, filed complaints, fought motions to dismiss, filed briefing in support of class certification, participated in extensive and contentious discovery including the review of hundreds of thousands of documents and the conduct of dozens of depositions. Class Counsel's "efforts in posturing this case for trial . . . played a role in spurring the settlement, [and] produced a substantial payout to the class." *In re Newbridge Networks Sec. Litig.*, 1998 U.S. Dist. LEXIS 23238, \*11 (D.D.C. Oct. 22, 1998).

Moreover, counsel worked for the class to finalize [\*86] the settlement, to oversee claims administration, and will have to work on any future appellate issues. Work was allocated in this case between several law firms.

g. Awards in similar cases

[HN41](#)[] In comparing the award in this action with amounts awarded in similar actions, a court's analysis is two-pronged. First, the court compares the actual award requested to other awards in comparable settlements. Second, the court ensures that the award is in line with what an attorney would have received if the fee was negotiated on the open market.

(i) The fee requested here is similar or lower to fees awarded in comparable settlements

**HN42** [↑] "A district court may not rely on a formulaic application of the appropriate range in awarding fees but must consider the relevant circumstances of the particular case." *Welch & Forbes, Inc. v. Cendant Corp. (In re Cendant Corp. Prides Litig.)*, 243 F.3d 722, 736 (3d Cir. 2001). A comparison of awards in similar cases is only a factor in determining the appropriateness of a fee award. See *Gunter*, 223 F.3d at 195. In considering this factor, the Court notes the survey of fee awards that have occurred in similar cases. See, e.g., *In re Rite Aid Corp. Sec. Litig.*, 396 F.3d 294, 306-07 (3d Cir. 2005) [\*87] (review of 289 settlements demonstrates "average attorney's fees percentage [of] 31.71%" with a median value that "turns out to be one-third"); *Cullen v. Whitman Medical Corp.*, 197 F.R.D. 136, 150 (E.D. Pa. 2000) ("the award of one-third of the fund for attorneys' fees is consistent with fee awards in a number of recent decisions within this district"); *Varacallo v. Mass. Mut. Life. Ins. Co.*, 226 F.R.D. 207, 249 (D.N.J. 2005) ("Many courts, including several in the Third Circuit, have considered 25% to be the standard "benchmark" figure for attorney fee awards in class action lawsuits, with adjustments up or down for significant case-specific factors")); *In re Linerboard Antitrust Litig.*, 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350 at \*14 ("The above figures are in accord with a recent Federal Judicial Center study that found that in federal class actions generally median attorney fee awards were in the range of 27 to 30 percent.").

**HN43** [↑] Courts within the Third Circuit often award fees of 25% to 33% of the recovery. See, e.g., *In re Linerboard Antitrust Litig.*, 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350 (E.D. Pa. 2004) (approving 30% fee of a \$ 202 million settlement in [\*88] an antitrust class action); *Nichols v. SmithKline Beecham Corp.*, 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616 (E.D. Pa. 2005) (approving 30% fee of the \$ 65 million settlement in similar pharmaceutical antitrust action); *In re ATI Technologies Inc. Sec. Litig.*, 2003 U. S. Dist. LEXIS 7062 (E.D. Pa. Apr. 28, 2003) (awarding 30% of fund); *In re Cell Pathways, Inc.*, 2002 U.S. Dist. LEXIS 18359 (E.D. Pa. Sept. 24, 2002) ("A thirty percent fee is very comparable to awards in similar cases, providing further support for approval of the fee petition"); *Blackman v. O'Brien Envtl. Energy, Inc.*, 1999 U.S. Dist. LEXIS 7160 (E.D. Pa. May 11, 1999) (35% fee awarded). The percentage fee requested in this case (23.6% of the fund) is consistent with other cases.

Moreover, Class Counsel's fee request compares favorably to fees awarded in similar pharmaceutical antitrust actions. See *House v. GlaxoSmithKline PLC*, 2005 U.S. Dist. LEXIS 33711, No. 2:02cv442 (E.D. Va. Jan. 10, 2005) (awarding a fee of 25% of the \$ 29 million indirect purchaser [\*89] settlement fund); *In re Relafen Antitrust Litig.*, 2004 U.S. Dist. LEXIS 28801, Master File No. 01-12239-WGY, Order and Final Judgment (D. Mass. April 9, 2004) (awarding fees of 33 1/3% of \$ 175 million of settlement fund).

(ii) The fee requested here is consistent with a privately negotiated contingent fee in the marketplace

**HN44** [↑] "When deciding on appropriate fee levels in common-fund cases, courts must do their best to award counsel the market price for legal services, in light of the risk of nonpayment and the normal rate of compensation in the market at the time." *In re Synthroid Marketing Litig.*, 264 F.3d 712, 718 (7th Cir. 2001). "The object . . . is to give the lawyer what he would have gotten in the way of a fee in an arm's length negotiation." *In re Continental Illinois Sec. Litig.*, 962 F.2d 566, 572 (7th Cir. 1992).

Consequently, courts should look to the private market when assessing the reasonableness of the percentage fee. See *In re RJR Nabisco Sec. Litig.*, 1992 U.S. Dist. LEXIS 12702, MDL No. 818, 1992 WL 210138, \*7 (S.D.N.Y. Aug. 24, 1992) ("What should govern [fee] awards is . . . what the market pays in similar cases"). **HN45** [↑] A one-third contingency fee is generally standard [\*90] in individual cases. See, e.g., *In re Copley Pharm., Inc.*, 1 F. Supp. 2d 1407, 1412 (D. Wyo. 1998); see also *In re Aetna Sec. Litig.*, 2001 U.S. Dist. LEXIS 68 (E.D. Pa. Jan. 4, 2001) ("thirty percent is in line with what is routinely privately negotiated in contingency fee tort litigation"). The requested fee award of 23.6% is below that general standard.

h. Lodestar Cross-check

**HN46** [↑] A lodestar cross-check is not a Gunter factor but is a "suggested practice." *Welch & Forbes, Inc. v. Cendant Corp. (In re Cendant Corp. Prides Litig.)*, 243 F.3d at 735 (3d Cir. 2001). When performing the lodestar

cross-check, the Third Circuit has recognized that "multiples ranging from one to four are frequently awarded in common fund cases when the lodestar method is applied." [Krell v. Prudential Ins. Co. of Am. \(In re Prudential Ins. Co. Am. Sales Practice Litig. Agent Actions\), 148 F.3d at 341](#) (quoting 3 Herbert Newberg & Albert Conte, Newberg on Class Actions, § 14.03 at 14-5 (3d ed. 1992)). "The district courts may rely on summaries submitted by the attorneys and need not review actual billing records." [In re Rite Aid Corp. Sec. Litig., 396 F.3d at 306-07](#) (footnote omitted).

The record demonstrates that Class [\*91] Counsel's lodestar in this case is \$ 4,506,294.25, resulting in a multiplier of 1.73. An examination of recently approved multipliers reveals that the multiplier requested here is on the low end of the spectrum. See, e.g., [Nichols v. SmithKline Beecham Corp., 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616, \\*24 \(E.D. Pa. Apr. 22, 2005\)](#) (approving multiplier of 3.15); [In re Linerboard Antitrust Litig., 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350, \\*4 \(E.D. Pa. June 2, 2004\)](#) (approving a 2.66 multiplier); [Weiss v. Mercedes-Benz of N. Am., Inc., 899 F. Supp. 1297, 1304 \(D.N.J.\), aff'd, 66 F.3d 314 \(3d Cir. 1995\)](#) (approving a 9.3 multiplier); [In re Rite Aid Corp. Secs. Litig., 146 F. Supp. 2d 706, 736 \(E.D. Pa. 2001\)](#) (multiple of over 6). This lodestar cross check corroborates the result of the percentage of fund method.

#### i. Conclusion

Taking into consideration the above factors, this Court awards Plaintiffs' Counsel \$ 7.8 million of the Settlement Fund, plus 23.6% of the accrued interest on the Settlement Fund.

#### 2. Reimbursement of Reasonable Expenses

In addition to their request for Attorneys' fees, Plaintiffs' Counsel seek reimbursement of \$ 494,683.73 in [\*92] expenses. [HN47](#) [↑] "Counsel in common fund cases is entitled to reimbursement of expenses that were adequately documented and reasonably and appropriately incurred in the prosecution of the case." [In re Cendant Corp., 232 F. Supp. 2d 327, 343 \(D.N.J. 2002\)](#) (quoting [In re Safety Components Int'l, Inc., 166 F. Supp. 2d 72, 104 \(D.N.J. 2001\)](#); [Abrams v. Lightolier, Inc., 50 F.3d 1204, 1225 \(3d Cir. 1995\)](#)).

Upon review of the affidavits submitted in support of this request, the Court finds the requested amount to be fair and reasonable. Plaintiffs' Counsel's expenses reflect costs expended for purposes of prosecuting this litigation, including substantial fees for experts; substantial costs associated with creating and maintaining an electronic document database; travel and lodging expenses; copying costs; and the costs of deposition transcripts. Reimbursement of similar expenses is routinely permitted. See e.g., [Oh v. AT & T Corp., 225 F.R.D. 142, 154 \(D.N.J. 2004\)](#) (finding the following expenses to be reasonable: "(1) travel and lodging, (2) local meetings and transportation, (3) depositions, (4) photocopies, (5) messengers and [\*93] express services, (6) telephone and fax, (7) Lexis/Westlaw legal research, (8) filing, (10) postage, (11) the cost of hiring a mediator, and (12) NJ Client Protection Fund relating to *pro hac vice*").

#### 3. Incentive Awards to Named Plaintiffs

Finally, Plaintiffs' Counsel request the approval of \$ 75,000 in incentive awards to the five Class Representatives. They seek \$ 30,000 for each of the two TPPs and \$ 5,000 for each of three individual consumers. "Like the attorneys in this case, the class representatives have conferred benefits on all other class members and they deserve to be compensated accordingly." [In re Linerboard Antitrust Litig., 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350 at \\*18](#) (citation omitted). In the instant action, the Class Representatives, spent a significant amount of their own time and expense litigating these cases for the benefit of the absent members of the settlement class, and as is recognized by a multitude of courts, their efforts should not go unrecognized. See e.g., [FTC v. Mylan Labs., Inc. \(In re Lorazepam & Clorazepate Antitrust Litig.\), 205 F.R.D. 369, 400 \(D.D.C. 2002\)](#) ("Incentive awards are not uncommon in class action litigation and particularly where . . . [\*94] . a common fund has been created for the benefit of the entire class. . . . In fact, courts routinely approve incentive awards to compensate named plaintiffs for the services they provided and the risks they incurred during the course of the class action litigation") (internal quotations and citation omitted).

In the detailed notice sent to Class members, Class Counsel indicated they would seek incentive awards in an amount not to exceed \$ 100,000.00. No class members objected. The amounts requested are similar to amounts awarded in similar settlements. See e.g., [\*Nichols, 2005 U.S. Dist. LEXIS 7061, 2005 WL 950616 at \\*24\*](#) (approving \$ 5,000 to each third-party payor named plaintiff, \$ 2,500 to each consumer named plaintiff); [\*In re Linerboard Antitrust Litig., 2004 U.S. Dist. LEXIS 10532, 2004 WL 1221350, \\*18 \(E.D. Pa. 2004\)\*](#) (approving \$ 25,000 to each representative of the classes). The named Plaintiffs complied with all reasonable demands and provided significant assistance to counsel in the prosecution of this case. The requested incentive awards are both appropriate and reasonable.

### **III. CONCLUSION**

For the foregoing reasons, (a) End-Payor Plaintiffs' and Plaintiff States' motion for final [\*95] approval of settlement, and (b) Class Counsel for End-Payor Plaintiffs' motion for attorneys' fees of \$ 7.8 million (plus accrued interest), litigation expenses, and incentive award to Class Representatives are granted.

September 13, 2005

Faith S. Hochberg

**Hon. Faith S. Hochberg, U.S.D.J.**

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## [Harrison Aire, Inc. v. Aerostar Int'l](#)

United States Court of Appeals for the Third Circuit

March 7, 2005, Argued ; September 16, 2005, Filed

Nos. 04-2904 & 04-3052

### **Reporter**

423 F.3d 374 \*; 2005 U.S. App. LEXIS 19903 \*\*; 2005-2 Trade Cas. (CCH) P74,930

HARRISON AIRE, INC., Appellant in No. 04-2904, v. AEROSTAR INTERNATIONAL, INC.; RAVEN INDUSTRIES, INC., Appellants in No. 04-3052.

**Subsequent History:** US Supreme Court certiorari denied by [Harrison Aire v. Aerostar Int'l, 2006 U.S. LEXIS 2263 \(U.S., Mar. 20, 2006\)](#)

**Prior History:** [\[\\*\\*1\]](#) On Appeal from the United States District Court for the Eastern District of Pennsylvania. D.C. Civil Action No. 02-cv-01258. (Honorable Michael M. Bayson).

[Harrison Aire, Inc. v. Aerostar Int'l, Inc., 316 F. Supp. 2d 186, 2004 U.S. Dist. LEXIS 8431 \(E.D. Pa., 2004\)](#)

## **Core Terms**

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fabric, aftermarket, balloon, Aire, replacement, customers, monopoly power, pricing, antitrust, summary judgment, manufacturers, manual, monopolization, lifecycle, consumers, costs, supracompetitive, competitors, repair, relevant market, third-party, barriers, ride, maintenance manual, replacement part, anti trust law, hot air, allegations, monopolist, purchasing

## **LexisNexis® Headnotes**

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Civil Procedure > Appeals > Standards of Review > De Novo Review

Civil Procedure > ... > Jurisdiction > Subject Matter Jurisdiction > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > General Overview

Civil Procedure > ... > Summary Judgment > Appellate Review > Standards of Review

Civil Procedure > Appeals > Appellate Jurisdiction > Final Judgment Rule

Civil Procedure > Appeals > Standards of Review > General Overview

[HN1](#)  **Standards of Review, De Novo Review**

The appellate court's summary judgment standard of review is plenary. The appellate court draws all reasonable inferences in favor of the non-moving party.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Attempts to Monopolize > General Overview

Civil Procedure > Judgments > Summary Judgment > Evidentiary Considerations

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

Civil Procedure > ... > Summary Judgment > Opposing Materials > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Evidence > Inferences & Presumptions > General Overview

## [\*\*HN2\*\*](#) Monopolies & Monopolization, Attempts to Monopolize

**Antitrust law** limits the range of permissible inferences that can be drawn from ambiguous evidence. To avoid deterring pro-competitive behavior, certain inferences may not be drawn from circumstantial evidence in an antitrust case. To survive a motion for summary judgment, an antitrust plaintiff must produce economically plausible evidence supporting the elements of its claim. If the plaintiff's theory is economically senseless, no reasonable jury could find in its favor, and summary judgment should be granted.

Antitrust & Trade Law > Sherman Act > General Overview

Evidence > Admissibility > Circumstantial & Direct Evidence

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

## [\*\*HN3\*\*](#) Antitrust & Trade Law, Sherman Act

Under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), monopolization consists of: (1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development as a consequence of a superior product, business acumen, or historic accident. Monopoly power is defined as the power to control prices or exclude competition. More precisely, it is the power to charge a price higher than the competitive price without inducing so rapid and great an expansion of output from competing firms as to make the supracompetitive price untenable. Monopoly power can be demonstrated with either direct evidence of supracompetitive pricing and high barriers to entry or with structural evidence of a monopolized market. Because direct proof is only rarely available, courts more typically examine market structure in search of circumstantial evidence of monopoly power.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Evidence > Inferences & Presumptions > General Overview

Antitrust & Trade Law > Sherman Act > General Overview

#### **HN4** [down arrow] **Monopolies & Monopolization, Actual Monopolization**

Competitive markets are characterized by both price and quality competition, and a firm's comparatively high price may simply reflect a superior product. Therefore, when dealing with a heterogeneous product or service, a reasonable finder of fact cannot infer monopoly power just from higher prices.

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Evidence > Inferences & Presumptions > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

#### **HN5** [down arrow] **Regulated Practices, Market Definition**

In a typical case under [§ 2](#) of the Sherman Act, [15 U.S.C.S. § 2](#), monopoly power is inferred from a firm's possession of a dominant share of a relevant market that is protected by entry barriers. Plaintiffs relying on market share as a proxy for monopoly power must plead and produce evidence of a relevant product market, of the alleged monopolist's dominant share of that market, and of high barriers to entry. Additional factors are relevant in the aftermarket context. Aftermarket monopolization cases require a more comprehensive analysis because market share data standing alone is not necessarily a reliable proxy for monopoly power.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Civil Procedure > ... > Summary Judgment > Burdens of Proof > General Overview

#### **HN6** [down arrow] **Monopolies & Monopolization, Actual Monopolization**

In broad terms, the United States Supreme Court's decision in Kodak stands for the proposition that market reality is the touchstone of antitrust analysis. Where the plaintiff comes forward with concrete evidence of a monopolized market, the defendant bears a substantial burden in showing that it is entitled to summary judgment. On the more specific issue of aftermarket monopolization, Kodak held that primary market competition does not necessarily preclude monopoly power in the relevant aftermarket where a unilateral policy change targets "locked-in" customers. But Kodak does not transform every firm with a dominant share of the relevant aftermarket into a monopolist. To create a triable question of aftermarket monopoly power, the plaintiff must produce hard evidence dissociating the competitive situation in the aftermarket from activities occurring in the primary market.

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > Regulated Practices > Market Definition > General Overview

Antitrust & Trade Law > ... > Market Definition > Relevant Market > Product Market Definition

Antitrust & Trade Law > Regulated Practices > Market Definition > Relevant Market

#### **HN7** [down arrow] **Monopolies & Monopolization, Actual Monopolization**

In considering the effect of primary market competition on aftermarket behavior, courts address at the outset the relevant market definition. Some courts have viewed the primary and aftermarket as comprising a single relevant product market. But this may not always be the case. Relevant market definition is a function of reasonably

available product substitutes. Products are included in a single relevant market when they have the ability--actual or potential--to take significant amounts of business away from each other. The proper inquiry focuses on the existence of monopoly power, that is, whether competition in the equipment market will significantly restrain power in the service and parts market. One important consideration is whether a unilateral change in aftermarket policy exploits locked-in customers. However, an "aftermarket policy change" is not the sine qua non of a Kodak claim. An aftermarket policy change is an important consideration, but only one of several relevant factors.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Tying Arrangements > General Overview

## **HN8** Price Fixing & Restraints of Trade, Tying Arrangements

Tying is defined as selling one good (the tying product) on the condition that the buyer also purchase another, separate good (the tied product). The antitrust concern over tying arrangements is limited to those situations in which the seller can exploit its power in the market for the tying product to force buyers to purchase the tied product when they otherwise would not. Tying requires "appreciable economic power" in the tying product market.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Evidence > Burdens of Proof > General Overview

## **HN9** Private Actions, Remedies

In Brunswick, the United States Supreme Court held that the antitrust laws protect consumers, not competitors, and that antitrust plaintiffs must show a causal connection between the defendant's anti-competitive conduct and injury to consumers. Injury to competitors does not suffice.

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**Judges:** Before: SCIRICA, Chief Judge, ROTH and BECKER, Circuit Judges.

**Opinion by:** SCIRICA

## Opinion

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### [\*377] OPINION OF THE COURT

SCIRICA, *Chief Judge*.

In this antitrust action, we address allegations of unlawful monopolization and tying in the aftermarket for replacement hot air balloon fabric. The District Court granted defendants' motion for summary judgment, finding no triable issue of monopoly power in the relevant product market. We will affirm.

I.

Harrison Aire, a hot air balloon ride operator, alleges antitrust violations by Raven Industries and its balloon-manufacturing subsidiary, Aerostar International. Consistent with our standard [\*\*2] of review on summary judgment, we recount the facts in the light most favorable to the non-moving party, appellant Harrison Aire.

Terry Harrison, the sole owner and proprietor of Harrison Aire, is an FAA-licensed pilot and aircraft mechanic. After a twenty-three year career at Eastern Airlines, he retired in 1973 to launch the Harrison Aire enterprise from an airstrip in central New Jersey. The company owns and operates several hot air balloons which it charters for recreational day trips over the New Jersey countryside. Since the mid 1990s, the business has suffered cash-flow problems. Harrison Aire blames its losses, in part, on the prohibitive expense of replacement balloon fabric, which it contends is a result of Raven/Aerostar's monopolization of the relevant balloon fabric aftermarket.

Raven Industries is a diversified manufacturing company based in Sioux Falls, South Dakota. From the 1970s through 1986, it manufactured hot air balloons and replacement balloon fabric. In 1986, Raven [\*378] formed Aerostar International as a wholly-owned subsidiary to take over its balloon business. Aerostar International manufactures and sells hot air balloons in a market of at least five competitors [\*\*3] and also produces and sells replacement balloon fabric.

Hot air balloons are regulated from cradle to grave by the Federal Aviation Administration. The FAA certifies balloon design and manufacturing standards, [14 C.F.R. § 21.11-53](#), requires the manufacturer to provide a maintenance manual along with its aircraft, *id.* [§ 21.50](#), reviews the content of the manual, *id.* [§ 31.82](#), and certifies replacement part designs for airworthiness, *id.* 21.303. The FAA's "maintenance manual" and "replacement part" regulations bear on this appeal.

Balloon manufacturers are required to provide their customers with a balloon maintenance manual, known as an "ICA" (Instructions for Continued Airworthiness), which sets forth recommended and required maintenance procedures. The manual is in two parts. The first, known as the "FAA accepted" section, establishes manufacturer-recommended but not FAA-required protocols. The second, known as the "Airworthiness Limitation Section," establishes FAA requirements affecting flight safety.

Regulations also govern the manufacture and sale of replacement balloon parts, including replacement fabric. All replacement parts must be "of such a quality" that [\*\*4] the repaired balloon is "at least equal to its original or properly altered condition." [14 C.F.R. § 43.13\(b\)](#). The FAA authorizes third-party manufacturers to sell aftermarket parts, including replacement fabric, provided they first obtain FAA certification that the product is equal to or better than the original. *Id.* [§ 21.303](#).

Replacement fabric extends the service life of a hot air balloon. The top half of the balloon "envelope"--the material encapsulating the hot air--tends to deteriorate more rapidly than the bottom half. By replacing top-half fabric after 300 to 500 hours of use, balloon owners are able to extend the aircraft's service life for an additional 200 to 300 hours. Generally, it is more economical to replace fabric in this manner than to purchase an entirely new envelope. Harrison Aire followed this practice in maintaining its fleet of Raven/Aerostar balloons.

Harrison Aire purchased its first Raven balloon in 1978. The parties' dispute over fabric replacement began shortly thereafter. According to Terry Harrison, Raven advised him that he could not purchase replacement fabric from other manufacturers because installation of third-party [\*\*5] fabric would render the balloon unairworthy. In 1982, Raven revised its balloon maintenance manuals to make this policy explicit, warning Raven balloon owners that "only fabric which has been tested and approved according to Raven factory standards may be used for repair of Raven envelopes. Failure to comply with this requirement constitutes a departure from type design and renders the balloon unairworthy." This language appeared in the FAA-approved, rather than the FAA-required, section of Raven maintenance manuals. Reading the manual in the light most favorable to Harrison Aire, it warned that only Raven-brand fabric should be used in Raven balloons.

Terry Harrison repeatedly complained to Raven, believing its insertion of the "warning" into the balloon manual transformed the fabric policy into an FAA requirement that legally barred him from obtaining cheaper fabric elsewhere. On several occasions between 1982 and 1986, Harrison confronted Raven representatives [\*379]

about the manual language, but was told that no other aftermarket product was equal to or better than Raven fabric, and that only Raven fabric was consistent with airworthiness standards. Harrison understood this as a representation [\*\*6] that he was required to purchase Raven fabric in order to comply with the FAA's "equal to or better" standard for replacement parts. Harrison Aire contends that from 1978 to 1986, Raven misled the company into believing the purchase of Raven fabric was mandated by law, when in fact it was merely recommended by the manufacturer.

In February 1986, Raven Industries formed Aerostar International to take over its hot air balloon business. Aerostar continued Raven's balloon operation essentially uninterrupted, and became the new focus of Harrison Aire's campaign to purchase fabric from third-party sources. Shortly after Aerostar was incorporated, Harrison registered several complaints with Aerostar about "being forced" to use Raven/Aerostar fabric. Nevertheless, despite its understanding that Aerostar balloons required Aerostar replacement fabric, Harrison Aire purchased a "big ride" Aerostar balloon in 1986 that is the subject of this litigation.

By 1995, Harrison Aire's "big ride" Aerostar balloon required a major fabric replacement. By this time, two other manufacturers had received FAA approval to produce aftermarket fabric for Aerostar balloons. See [14 C.F.R. § 21.303](#) [\*\*7] (authorizing the manufacture of replacement balloon parts upon receipt of a "Parts Manufacturer Approval" from the FAA). Harrison investigated one of the approved sellers, Custom Nine Designs, but decided against purchasing their fabric because of concerns that it lacked quality. Harrison never contacted the other approved supplier, Head Balloons. Viewing Aerostar-brand fabric as its only option and as prohibitively expensive, Harrison Aire retired the "big ride" balloon in 1996 rather than repairing it.

Harrison eventually realized that installation of third-party fabric was legally permissible. In July 2000, following an administrative proceeding between the FAA and a third-party balloon repair service, an Administrative Law Judge concluded the fabric "warning" found in Aerostar's maintenance manual was not legally binding. *In re Braden's Balloons Aloft, Inc.*, FAA No. CP99SWO037 (July 26, 2000). Harrison contends the Braden's decision provided him notice, for the first time, that his company was not required to purchase Aerostar-brand fabric.

In March 2002, Harrison Aire filed suit in federal court, alleging, *inter alia*, antitrust injury arising from Raven/Aerostar's [\*\*8] monopolization of the aftermarket for replacement Aerostar balloon fabric and from the unlawful tying of Aerostar-brand fabric to Aerostar balloons. But for Raven/Aerostar's allegedly misleading and exclusionary aftermarket fabric policy, Harrison Aire contends that its "big ride" balloon would have been repaired in 1996 and still operational. The District Court granted summary judgment to defendants, holding they lacked sufficient market power in the relevant product market. [Harrison Aire, Inc. v. Aerostar Int'l, Inc.](#), 316 F. Supp. 2d 186 (E.D. Pa. 2004).<sup>1</sup>

## [\*\*9] [\*380] II.

The District Court had jurisdiction under the federal antitrust laws, [15 U.S.C. § 15](#) (providing cause of action and treble damage remedy), and [28 U.S.C. § 1331](#). We have jurisdiction under [28 U.S.C. § 1291](#). [HN1](#)<sup>↑</sup> Our summary judgment standard of review is plenary. [In re Flat Glass Antitrust Litig.](#), 385 F.3d 350, 357 (3d Cir. 2004) (drawing all reasonable inferences in favor of the non-moving party).

Significantly, however, [HN2](#)<sup>↑</sup> "**antitrust law**" limits the range of permissible inferences" that can be drawn "from ambiguous evidence." [Matsushita Elec. Indus. Co. v. Zenith Radio Corp.](#), 475 U.S. 574, 588, 89 L. Ed. 2d 538, 106 S. Ct. 1348 (1986); see also [Monsanto Co. v. Spray-Rite Serv. Corp.](#), 465 U.S. 752, 764, 79 L. Ed. 2d 775, 104 S.

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<sup>1</sup> Harrison Aire's complaint included both federal antitrust counts and supplemental claims under state law. On May 3, 2004, the District Court granted Raven/Aerostar's motion for summary judgment in part, dismissing the antitrust counts and ordering trial on the state law counts. The parties then stipulated to final judgment with prejudice against Harrison Aire on the surviving claims, in order to facilitate an immediate appeal on the antitrust issues. Accordingly, the state law claims are not at issue and our analysis is confined to the federal antitrust claims.

Ct. 1464 (1984). To avoid deterring pro-competitive behavior, "certain inferences may not be drawn from circumstantial evidence in an antitrust case." In re Flat Glass Antitrust Litig., 385 F.3d at 357 (quoting Intervest, Inc. v. Bloomberg, L.P., 340 F.3d 144, 160 (3d Cir. 2003)).

To survive a motion for summary judgment, an antitrust **[\*\*10]** plaintiff must produce economically plausible evidence supporting the elements of its claim. See Matsushita, 475 U.S. at 588; Ideal Dairy Farms v. John Labatt, Ltd., 90 F.3d 737, 748-50 (3d Cir. 1996) (applying Matsushita in section 2 action); Zenith Radio Corp. v. Matsushita Elec. Indus. Co., 513 F. Supp. 1100, 1140 (E.D. Pa. 1981) ("It is now settled that summary judgment is appropriate in those antitrust cases where plaintiffs, after having engaged in extensive discovery, fail to produce 'significant probative evidence' in support of the allegations in their complaint.") (citations omitted). "If the plaintiff's theory is economically senseless, no reasonable jury could find in its favor, and summary judgment should be granted." Eastman Kodak Co. v. Image Tech. Servs., Inc., 504 U.S. 451, 468-69, 119 L. Ed. 2d 265, 112 S. Ct. 2072 (1992).

### III.

We begin with Harrison Aire's monopolization claim. **HN3** [↑] Under section 2 of the Sherman Act, monopolization consists of: "(1) the possession of monopoly power in the relevant market and (2) the willful acquisition or maintenance of that power as distinguished from growth or development **[\*\*11]** as a consequence of a superior product, business acumen, or historic accident." United States v. Grinnell Corp., 384 U.S. 563, 570-71, 16 L. Ed. 2d 778, 86 S. Ct. 1698 (1966); see also 15 U.S.C. § 2; LePage's, Inc. v. 3M, 324 F.3d 141 (3d Cir. 2003) (en banc) (reviewing section 2 case law and explaining the "willful acquisition or maintenance" element).

Monopoly power is defined as "the power to control prices or exclude competition." United States v. E.I. du Pont de Nemours & Co., 351 U.S. 377, 391, 100 L. Ed. 1264, 76 S. Ct. 994 (1956). More precisely, it is "the power to charge a price higher than the competitive price without inducing so rapid and great an expansion of output from competing firms as to make the supracompetitive price untenable." Am. Academic Suppliers, Inc. v. Beckley-Cardy, Inc., 922 F.2d 1317, 1319 (7th Cir. 1991); see also United States v. Dentsply Int'l Inc., 399 F.3d 181, 189 (3d Cir. 2005) (emphasizing a monopolist's power "to maintain market share") (emphasis in original) (quoting United States v. Syufy Enters., 903 F.2d 659, 665-66 (9th Cir. 1990)).

**[\*381]** Monopoly **[\*\*12]** power can be demonstrated with either direct evidence of supracompetitive pricing and high barriers to entry, see Rebel Oil Co. v. Atl. Richfield Co., 51 F.3d 1421, 1434 (9th Cir. 1995), or with structural evidence of a monopolized market. Because "direct proof is only rarely available, courts more typically examine market structure in search of circumstantial evidence of monopoly power." United States v. Microsoft, 346 U.S. App. D.C. 330, 253 F.3d 34, 51 (D.C. Cir. 2001) (en banc) (citations omitted).

#### A.

Harrison Aire contends Aerostar charged supracompetitive prices for its fabric, based on the uncontested fact that Aerostar's fabric is more expensive than that of its aftermarket competitors. But this alone does not support a reasonable inference of monopoly power. **HN4** [↑] Competitive markets are characterized by both price and quality competition, and a firm's comparatively high price may simply reflect a superior product. Blue Cross & Blue Shield United v. Marshfield Clinic, 65 F.3d 1406, 1412 (7th Cir. 1995) ("Generally you must pay more for higher quality."). Therefore, "when dealing with a heterogeneous product or service . **[\*\*13]** . . . a reasonable finder of fact cannot infer monopoly power just from higher prices." Id. at 1411-12.

Here, the record is clear that balloon fabric is a heterogeneous product. Fabric is sold in various weaves and grades, of differing strength and durability. The record demonstrates that Aerostar fabric is of comparatively high quality. Although Harrison considered purchasing fabric from one of Aerostar's aftermarket competitors, Custom Nine Designs, he rejected the product because Custom Nine "didn't prove to me that it wasn't a bogus part." Furthermore, Custom Nine's president acknowledged that Aerostar's "diamond weave" fabric was a superior

aftermarket product to his own. Because it is undisputed that balloon fabric, and particularly Aerostar fabric, is differentiated by composition and quality, Aerostar's comparatively high price does not, by itself, support a reasonable inference of monopoly power.

## B.

Turning to Harrison Aire's circumstantial evidence of monopoly power, we note the structural indicators of a monopolized market. [HNS ↑](#) In a typical [section 2](#) case, monopoly power is "inferred from a firm's possession of a dominant share of a relevant market that [\\*\\*14](#) is protected by entry barriers." [Microsoft, 253 F.3d at 51](#); see also *Fineman v. Armstrong World Indus.*, 980 F.2d 171, 201-03 (3d Cir. 1992) (explaining market share analysis). Plaintiffs relying on market share as a proxy for monopoly power must plead and produce evidence of a relevant product market, of the alleged monopolist's dominant share of that market, and of high barriers to entry. [Queen City Pizza, Inc. v. Domino's Pizza, Inc., 124 F.3d 430, 436 \(3d Cir. 1997\)](#) (market definition); *Fineman*, 980 F.2d at 201-03 (3d Cir. 1992) (market share); [Microsoft, 253 F.3d at 82](#) (barriers to entry).

Additional factors are relevant in the aftermarket context. Aftermarket monopolization cases require a more comprehensive analysis, because market share data standing alone is not necessarily a reliable proxy for monopoly power. [SMS Syst. Maint. Servs. Inc. v. Digital Equip. Corp., 188 F.3d 11, 16 \(1st Cir. 1999\)](#). Many firms supply unique and/or proprietary aftermarket parts and services for their primary market products. As a result, they "can be expected to have a very high percentage" [\\*\\*15](#) share of the relevant aftermarket. *Id.* But high aftermarket share is not necessarily indicative of monopoly [\[\\*382\]](#) power--i.e., the power to charge and maintain a supracompetitive price--because aftermarket behavior generally is disciplined by competition in the primary product market. If the primary market is competitive, a firm exploiting its aftermarket customers ordinarily is engaged in a short-run game--for when buyers evaluate the "lifecycle" cost of the product, the cost of the product over its full service life, they will shop elsewhere. Eventually, the aftermarket "monopolist" lacks customers to exploit. See *Parts & Elec. Motors, Inc. v. Sterling Elec., Inc.*, 866 F.2d 228, 236 (7th Cir. 1988) (Posner, J., dissenting) (describing the exploitation of aftermarket customers as a "suicidal" business practice); [SMS, 188 F.3d at 16](#) ("firms concerned with the long term cannot afford to bite the hands that feed them").

This portrayal is conventional antitrust theory. See 2A Philip E. Areeda & Herbert Hovenkamp, [Antitrust Law](#) P 564b, at 322-28 (2d ed. 2002). But as explained in *Kodak*, it "may not accurately explain the behavior of the primary [\\*\\*16](#) and derivative markets for complex durable goods" where "significant information and switching costs" sever the usual link between the primary market and the aftermarket. [504 U.S. at 473](#). Information costs are barriers that prevent primary market consumers from evaluating the lifecycle costs of a product. [Id. at 473-74](#). For primary market competition to discipline aftermarket behavior, consumers require information on, among other things, the expected cost, quality and availability of aftermarket products such as parts and service. Perfect information is not required for the primary market to check the aftermarket. See [Jefferson Parish Hosp. Dist. No. 2 v. Hyde, 466 U.S. 2, 27, 80 L. Ed. 2d 2, 104 S. Ct. 1551 \(1984\)](#) (holding, in tying case, that imperfect information does not necessarily "generate the kind of monopoly power that justifies condemnation"); [SMS, 188 F.3d at 19 n.3](#) ("perfect information about the aftermarket is not required"). But sometimes lifecycle pricing information is particularly difficult or impossible for primary market customers to acquire, as in the case of a unilateral change in aftermarket policy targeting "locked [\\*\\*17](#) in" customers. *Kodak* involved this type of market failure. See [Queen City Pizza, 124 F.3d at 440](#) ("The *Kodak* case arose out of concerns about unilateral changes in *Kodak*'s parts and repairs policies.")

*Kodak* involved a primary market for photocopiers and an aftermarket for *Kodak* parts and service. The primary market was competitive. But *Kodak* controlled nearly 100% of the parts aftermarket, and 80% to 95% of the service market. [504 U.S. at 480](#). Historically, *Kodak*'s customers had been able to obtain copier repair service from independent service organizations that charged "substantially" less than *Kodak*. [504 U.S. at 457](#). Later, however, after customers were locked in to *Kodak* copiers, *Kodak* changed its aftermarket policy to sell replacement parts only to those customers who also purchased *Kodak* service or who repaired their own machines. [Id. at 458](#). This policy change led to higher aftermarket prices. [Id. at 465](#). In other words, *Kodak* used its power in the replacement

parts market to "squeeze the independent service providers out of the repair market and to force copier purchasers to obtain service [\*\*18] directly from Kodak, at higher cost." [Queen City Pizza, 124 F.3d at 440](#).

The Supreme Court held the independent service organizations' tying and monopolization claims against Kodak could not be dismissed on summary judgment following truncated discovery. [Kodak, 1\\*3831 504 U.S. at 486](#). On the key question of monopoly power in the parts and services aftermarket, the Court cited evidence of (1) supracompetitive pricing, *id. at 469*; (2) Kodak's dominant share of the relevant aftermarket, *id. at 480*; (3) significant information costs that prevented lifecycle pricing by primary market customers, *id. at 475*; and (4) high "switching costs" that served to "lock in" Kodak's aftermarket customers, *id. at 477*. Together, this evidence supported a reasonable inference of monopoly power in the relevant aftermarket, precluding summary judgment.

**HN6** In broad terms, *Kodak* stands for the proposition that market reality is the touchstone of antitrust analysis. Where the plaintiff comes forward with concrete evidence of a monopolized market, the defendant "bears a substantial burden in showing that it is entitled [\*\*19] to summary judgment." [504 U.S. at 469](#). On the more specific issue of aftermarket monopolization, *Kodak* held that primary market competition does not necessarily preclude monopoly power in the relevant aftermarket where a unilateral policy change targets "locked-in" customers.

But *Kodak* does not transform every firm with a dominant share of the relevant aftermarket into a monopolist. To create a triable question of aftermarket monopoly power, the plaintiff must produce "hard evidence dissociating the competitive situation in the aftermarket from activities occurring in the primary market." [SMS, 188 F.3d at 17 \(1st Cir. 1999\)](#).

**HN7** In considering the effect of primary market competition on aftermarket behavior, we address at the outset the relevant market definition. Some courts have viewed the primary and aftermarket as comprising a single relevant product market. See *id.*; [PSI Repair Servs., Inc. v. Honeywell, Inc., 104 F.3d 811, 820 \(6th Cir. 1997\)](#). But this may not always be the case. Relevant market definition is a function of reasonably available product substitutes. [Du Pont, 351 U.S. at 395 \(1956\)](#). Products [\*\*20] are included in a single relevant market when they "have the ability--actual or potential--to take significant amounts of business away from each other." [Allen-Myland, Inc. v. IBM Corp., 33 F.3d 194, 206 \(3d Cir. 1994\)](#) (quoting [SmithKline Corp. v. Eli Lilly & Co., 575 F.2d 1056, 1063 \(3d Cir. 1978\)](#)); see also [Rothery Storage & Van Co. v. Atlas Van Lines, Inc., 253 U.S. App. D.C. 142, 792 F.2d 210, 218 \(D.C. Cir. 1986\)](#). Under this framework, we believe the relevant market here is that for replacement fabric for Aerostar balloons. The primary balloon market is distinct from the fabric aftermarket because fabric is a complement to, not a substitute for, the primary good. Nevertheless, these complementary products are linked by consumer demand such that competition in the foremarket may discipline behavior in the aftermarket. The proper inquiry, then, focuses on the existence of monopoly power, i.e., "whether competition in the equipment market will significantly restrain power in the service and parts market." [Kodak, 504 U.S. at 470 n.15](#).

One important consideration is whether a unilateral change in aftermarket policy [\*\*21] exploits locked-in customers. [Queen City Pizza, 124 F.3d at 440 \(3d Cir. 1997\)](#); [SMS, 188 F.3d at 19 \(1st Cir. 1999\)](#); [Alcatel USA, Inc. v. DGI Techs., Inc., 166 F.3d 772, 783 \(5th Cir. 1999\)](#); [PSI, 104 F.3d at 820 \(6th Cir. 1997\)](#). As the Court of Appeals for the Seventh Circuit has explained: "The Court did not doubt in *Kodak* that if spare parts had been bundled with Kodak's copiers from the outset, or Kodak had informed customers about its policies before they [\*384] bought its machines, purchasers could have shopped around for competitive lifecycle prices. The material dispute that called for a trial was whether the change in policy enabled Kodak to extract supra-competitive prices from customers who had already purchased its machines." [Digital Equip. Corp. v. Uniq Digital Tech., Inc., 73 F.3d 756, 763 \(7th Cir. 1996\)](#); accord [SMS, 188 F.3d at 17-19 \(1st Cir. 1999\)](#); [PSI, 104 F.3d at 820 \(6th Cir. 1997\)](#).

We emphasize, however, that an "aftermarket policy change" is not the *sine qua non* of a *Kodak* claim. An aftermarket policy change is an important consideration, [\*\*22] but only one of several relevant factors. As noted, the *Kodak* plaintiffs came forward with evidence of (1) supracompetitive pricing, (2) Kodak's dominant share of the relevant aftermarket, (3) significant information costs that prevented lifecycle pricing, and (4) high "switching costs" that served to "lock in" Kodak's aftermarket customers.

Here, in contrast, Harrison Aire has failed to meet its burden of dissociating competition in the primary market from conditions in the aftermarket. It is undisputed that the primary balloon market is competitive. And unlike the plaintiffs in *Kodak*, Harrison Aire has failed to produce evidence of supracompetitive pricing, of dominant aftermarket share, of information costs preventing lifecycle pricing, or of a change in aftermarket policy targeting locked-in customers. Together, these evidentiary failures compel summary judgment for the defendant.

Harrison Aire purchased its first Raven balloon in 1978. From that time on, Terry Harrison believed that Raven required him to use Raven-brand replacement fabric. Harrison repeatedly complained about this policy. From 1982, when Raven first published its allegedly exclusionary "warning" about [\\*\\*23](#) third-party replacement fabric, and continuing through 1986, when Raven formed Aerostar, Terry Harrison on several occasions confronted Raven representatives about their restrictive fabric policy. Similarly, immediately after Aerostar's incorporation in February, 1986, Harrison registered several complaints about "being forced" to buy Aerostar fabric. Yet knowing Raven/Aerostar's restrictive fabric policy, Harrison Aire entered the competitive primary market in 1986 to purchase the "big ride" Aerostar balloon that is the subject of this lawsuit.

The transparency of Raven/Aerostar's aftermarket fabric policy, and Harrison Aire's undisputed knowledge of it, cuts strongly against an inference of monopoly power. SMS is instructive on this point. Like Harrison Aire, the plaintiffs in SMS produced some evidence of switching costs, [188 F.3d at 20](#), but failed to come forward with sufficient evidence of supracompetitive pricing, [id. at 24](#), and significant information barriers to lifecycle pricing, [id. at 18-19](#), to survive summary judgment on the issue of monopoly power. In affirming summary judgment for the defendant, the court in SMS [\[\\*\\*24\]](#) engaged in a comprehensive analysis under the relevant *Kodak* factors. In particular, SMS emphasized the transparency of the defendant's aftermarket policy, explaining that readily available aftermarket information allows reasonably diligent primary market customers to engage in lifecycle pricing. [Id. at 18-19](#). This, in turn, checks aftermarket monopolization. See [id. at 19](#) ("The transparency of [defendant's] allegedly monopolistic policy represents a salient departure from the *Kodak* scenario.").

Raven/Aerostar's aftermarket policy was transparent and known to Harrison Aire at all relevant times. Neither information costs nor a unilateral change in aftermarket policy prevented Harrison Aire from shopping for competitive lifecycle balloon [\[\\*385\]](#) prices when it purchased the "big ride" balloon at issue in 1986. Furthermore, after full discovery, Harrison Aire has not produced other evidence dissociating competitive conditions in the primary balloon market from conditions in the aftermarket for replacement fabric. The record here is clear that Harrison Aire got precisely the balloon and the aftermarket fabric that it bargained for in the competitive [\[\\*\\*25\]](#) primary market.

Lacking any evidence of significant information barriers to lifecycle pricing, or any other evidence dissociating competitive conditions in the primary market and the aftermarket, summary judgment is proper on Harrison Aire's monopolization claim.

#### IV.

Harrison Aire also alleges unlawful tying under [section 1](#). The claim lacks merit. [HN8](#) "Tying is defined as selling one good (the tying product) on the condition that the buyer also purchase another, separate good (the tied product)." [Town Sound & Custom Tops, Inc. v. Chrysler Motors Corp., 959 F.2d 468, 475 \(3d Cir. 1992\)](#) (en banc). "The antitrust concern over tying arrangements is limited to those situations in which the seller can exploit its power in the market for the tying product to force buyers to purchase the tied product when they otherwise would not." [Queen City Pizza, 124 F.3d at 442-43](#) (quoting [Town Sound, 959 F.2d at 475](#)); see also [Microsoft, 253 F.3d at 84](#). Tying requires "appreciable economic power" in the tying product market. [Kodak, 504 U.S. at 464](#); [Brokerage Concepts v. U.S. Healthcare, Inc., 140 F.3d 494, 516-17 \(3d Cir. 1998\)](#). [\[\\*\\*26\]](#)

Harrison Aire contends Raven/Aerostar unlawfully tied its hot air balloons (the tying product) to its replacement fabric (the tied product), but fails to produce any evidence of appreciable market power in the tying product market. As noted, it is undisputed that the primary market for hot air balloons is competitive. Absent this essential element, we will affirm summary judgment on the tying claim.

**V.**

As an alternative holding, the District Court concluded Harrison Aire failed to properly allege antitrust injury under *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 50 L. Ed. 2d 701, 97 S. Ct. 690 (1977). This was error. **HN9** [↑] *Brunswick* held the antitrust laws protect consumers, not competitors, and that antitrust plaintiffs must show a causal connection between the defendant's anti-competitive conduct and injury to consumers. *Id. at 488-89*. Injury to competitors does not suffice. Here, Harrison Aire is a consumer of balloon fabric, and it claims antitrust injury in the form of business losses caused by high fabric prices, which in turn allegedly were caused by Raven/Aerostar's exclusionary conduct in the relevant fabric market. This type of injury--prohibitively [\*\*27] high consumer prices resulting from allegedly monopolistic behavior--is the type the antitrust laws are designed to redress. See *Town Sound*, 959 F.2d at 486 (3d Cir. 1992) (en banc) (explaining antitrust injury); *U.S. Gypsum Co. v. Ind. Gas Co.*, 350 F.3d 623, 626-28 (7th Cir. 2003) (same).

The District Court concluded that "any injuries that Plaintiff suffered would have come from Defendants' misrepresentations, not from any market power, abuse of market power or other anti-competitive conduct." *316 F. Supp. 2d at 224*. But these purported misrepresentations are alleged to have had an anticompetitive effect in the aftermarket--namely the exclusion of more efficient competitors. Harrison Aire alleges that Aerostar used misleading [\*386] manual language, and the imprimatur of FAA acceptance, to consolidate its position in the fabric aftermarket. This, in turn, allegedly prevented Harrison and consumers like him from purchasing lower-cost fabric from Aerostar's competitors. These allegations satisfy the antitrust injury requirement.

The District Court found antitrust injury lacking because the manual "did not forbid Plaintiff from purchasing other [\*\*28] manufacturers' fabric and that a reasonable investigation on this point by Plaintiff would have disclosed . . . that Plaintiff could buy replacement fabric from anyone who manufactured [it] to the FAA standards." *Id. at 217*. In other words, the District Court held that no injury to consumers could be shown because no jury could find that Harrison Aire reasonably relied on the manual.

It is true that further investigation by Harrison Aire *might* have revealed that Aerostar's replacement-fabric instructions were not legally binding. But the record is not clear that Harrison Aire's reliance on the manual was unreasonable. Indeed, it appears that the FAA, like Harrison Aire, viewed Aerostar's manual as restricting the use of non-Aerostar fabric in Aerostar balloons. Not until the *Braden*'s decision in 2000 did the FAA recognize the Aerostar manual as non-binding. Since the FAA itself interpreted Aerostar's manual as restricting the use of third-party fabric, the reasonableness of Harrison Aire's reliance on that manual presents a jury question. A jury could have found that Harrison reasonably believed that Aerostar's manuals prevented him from buying lower-priced [\*\*29] fabric from competitors. Because this alleged exclusion of competitors, to the detriment of consumers, is the sort of harm the antitrust laws are intended to prevent, summary judgment was improper on the issue of antitrust injury. While we hold Harrison Aire's antitrust claims ultimately fail for lack of monopoly/market power in the relevant market, they are not defective for failure to allege antitrust injury.

**CONCLUSION**

For the reasons set forth, we will affirm the judgment of the District Court.

## Pelfresne v. Village of Lindenhurst

United States District Court for the Northern District of Illinois, Eastern Division

September 16, 2005, Decided ; September 16, 2005, Filed

No. 03 C 6905

### **Reporter**

2005 U.S. Dist. LEXIS 23094 \*; 2005-2 Trade Cas. (CCH) P74,945

C. PELFRESNE, Trustee Under Illinois Land Trust No. 25, Dated May 29, 1998, Plaintiff, v. VILLAGE OF LINDENHURST, an Illinois municipal corporation, et al., Defendants.

**Subsequent History:** Sanctions disallowed by [Pelfresne v. Vill. of Lindenhurst, 2007 U.S. Dist. LEXIS 46586 \(N.D. Ill., June 26, 2007\)](#)

**Prior History:** [Pelfresne v. Vill. of Lindenhurst, 2004 U.S. Dist. LEXIS 14176 \(N.D. Ill., July 23, 2004\)](#)

## **Core Terms**

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relocation, Defendants', immunity, motion to dismiss, Sherman Act, third party, annexation, property right, Municipal, LaSalle, removal, plaintiff's claim, unjust enrichment, tortious interference, declaratory, consumers, malicious, ordinance, frontage, alleges, vacate, restraint of trade, malicious injury, anticompetitive, authorization, entities, cable, civil conspiracy, cause of action, real estate

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN1[ Motions to Dismiss, Failure to State Claim]**

The purpose of a motion to dismiss is to test the sufficiency of the plaintiff's complaint, not to decide its merits. A motion to dismiss will be granted only if it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which entitles him to relief. In reviewing a motion to dismiss for failure to state a claim, the court accepts as true all factual allegations in the plaintiff's complaint and draws all reasonable inferences in his favor.

Civil Procedure > Judgments > Declaratory Judgments > General Overview

### **HN2[ Judgments, Declaratory Judgments]**

The purposes of declaratory judgments are to clarify and settle the legal relations at issue and to terminate and afford relief from uncertainty, insecurity, and controversy giving rise to the proceeding. Where the substantive suit would resolve the issues raised by the declaratory judgment action, the declaratory judgment action serves no useful purpose because the controversy has ripened and the anticipation and uncertainty of litigation are alleviated.

Antitrust & Trade Law > Sherman Act > Remedies > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Conspiracy to Monopolize > Sherman Act

Antitrust & Trade Law > Sherman Act > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Per Se Rule & Rule of Reason > Per Se Violations

### **HN3** Sherman Act, Remedies

To state a claim for relief under § 1 of the Sherman Act, plaintiff must allege either that the contract, combination, or conspiracy resulted in a per se violation of the Sherman Act or that it unreasonably restrained competition in a relevant market.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Right to Petition Immunity

Labor & Employment Law > Collective Bargaining & Labor Relations > Unfair Labor Practices > General Overview

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > General Overview

### **HN4** Noerr-Pennington Doctrine, Right to Petition Immunity

Under the Noerr-Pennington doctrine, parties may petition the government for official action favorable to their interests without fear of suit, even if the result of the petition, if granted, might harm the interests of others.

Governments > Local Governments > Claims By & Against

### **HN5** Local Governments, Claims By & Against

Parker immunity would not protect local governments directly, but recognized that such immunity does apply where a municipality's restriction of competition is an authorized implementation of state policy. For the immunity to apply, however, there must be a clear articulation of a state policy to authorize anticompetitive conduct by the municipality. This requirement is satisfied if suppression of competition is the foreseeable result of what the state authorizes.

Administrative Law > Agency Rulemaking > State Proceedings

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Transportation Law > Bridges & Roads > Billboards

### **HN6** Agency Rulemaking, State Proceedings

To be sure, state law authorizes only agency decisions that are substantively and procedurally correct. Errors of fact, law, or judgment by the agency are not authorized. In order to prevent Parker from undermining the very interests of federalism it is designed to protect, it is necessary to adopt a concept of authority broader than what is applied to determine the legality of the municipality's action under state law.

Business & Corporate Compliance > ... > Real Property Law > Zoning > Annexation

Governments > Local Governments > Boundaries

Governments > Local Governments > Ordinances & Regulations

#### **HN7** **Zoning, Annexation**

See [65 Ill. Comp. Stat. 5/11-15.1-1.](#)

Governments > Local Governments > Ordinances & Regulations

Transportation Law > Bridges & Roads > Abandonment & Vacation

#### **HN8** **Local Governments, Ordinances & Regulations**

See [65 Ill. Comp. Stat. 5/11-91-1.](#)

Governments > Local Governments > Claims By & Against

Healthcare Law > Healthcare Litigation > Antitrust Actions > Facilities

Healthcare Law > Business Administration & Organization > Covenants not to Compete > General Overview

#### **HN9** **Local Governments, Claims By & Against**

To be sure, a municipality is not automatically beyond the reach of antitrust laws merely by virtue of a state delegation of authority. As with other zoning ordinances, however, the Illinois statute authorizing the removal and relocation of roads has the foreseeable result of placing landowners at an economic disadvantage in connection with the development of their property.

Contracts Law > Remedies > Equitable Relief > General Overview

#### **HN10** **Remedies, Equitable Relief**

To establish that the retention of a benefit conferred upon defendants by a third-party constitutes an unjust enrichment, a plaintiff must show that (1) the benefit should have been given to the plaintiff, but the third party mistakenly gave it to the defendant instead; (2) the defendant procured the benefit from the third party through some type of wrongful conduct, or (3) the plaintiff for some other reason had a better claim to the benefit than the defendant.

Torts > ... > Commercial Interference > Prospective Advantage > General Overview

Torts > Business Torts > General Overview

Torts > Business Torts > Commercial Interference > General Overview

## **HN11** [blue download icon] **Commercial Interference, Prospective Advantage**

To state a tortious interference claim, a plaintiff must allege (1) a reasonable expectation of entering into a valid business relationship; (2) defendants' knowledge of that expectancy; (3) purposeful or intentional interference by defendants that prevents the plaintiff's legitimate expectancy from ripening into a valid business relationship; and (4) damages to the plaintiff resulting from the interference. Numerous Illinois cases have stated that a plaintiff states a cause of action only if he alleges a business expectancy with a specific third party as well as action by the defendant directed towards that third party.

Civil Procedure > ... > Pleadings > Complaints > Requirements for Complaint

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

## **HN12** [blue download icon] **Complaints, Requirements for Complaint**

Under the federal rule of notice pleading, all the rules require is a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests.

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

## **HN13** [blue download icon] **Pleadings, Rule Application & Interpretation**

The Federal Rules do not require that a complaint allege the specific third party or class of third parties with whom the plaintiff claims to have had a valid business expectancy. As the court explained, a [Fed. R. Civ. P. 12\(b\)\(6\)](#) motion cannot be used to dismiss a complaint on the ground that it does not include information that [Fed. R. Civ. P. 8](#) does not require it to contain.

Torts > Premises & Property Liability > General Overview

## **HN14** [blue download icon] **Torts, Premises & Property Liability**

Pendleton does not affirmatively recognize a claim for malicious injury to property. It recognizes the general principle of law that every man has the right to dispose of his own labor or capital according to his own will.

Governments > State & Territorial Governments > Claims By & Against

Torts > Public Entity Liability > Immunities > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > General Overview

Torts > ... > Concerted Action > Civil Conspiracy > Defenses

Torts > Public Entity Liability > Liability > General Overview

## [HN15](#) [blue] State & Territorial Governments, Claims By & Against

The Tort Immunity Act is designed to protect local public entities from liability arising out of the operations of government. Under the Act, a public entity is not liable for an injury caused by adopting or failing to adopt an enactment or by failing to enforce any law. [745 Ill. Comp. Stat. 10/2-103](#). In addition, a public entity is not liable for an injury caused by the issuance, denial, suspension or revocation of, or by the failure or refusal to issue, deny, suspend or revoke, any permit, license, certificate, approval, order or similar authorization where the entity or its employee is authorized by enactment to determine whether or not such authorization should be issued, denied, suspended or revoked. Public employees are similarly immune from liability for such actions under §§ 2-205 and 2-206. [745 Ill. Comp. Stat. 10/2-205](#), 2-206.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Affirmative Defenses > Immunity

Torts > Public Entity Liability > Immunities > General Overview

Civil Procedure > ... > Defenses, Demurrsers & Objections > Affirmative Defenses > General Overview

## [HN16](#) [blue] Affirmative Defenses, Immunity

Immunity under the Tort Immunity Act constitutes an affirmative defense that cannot be disposed of on a motion to dismiss. Though this is generally true, the exception occurs where the allegations of the complaint itself set forth everything necessary to satisfy the affirmative defense.

Governments > Local Governments > Boundaries

Torts > Public Entity Liability > Immunities > General Overview

## [HN17](#) [blue] Local Governments, Boundaries

The Tort Immunity Act expressly extends immunity to injuries caused by the refusal to deny any approval or other similar authorization. [745 Ill. Comp. Stat. 10/2-104](#).

**Counsel:** [\*1] For Charles Pelfresne, Trustee under Illinois Land Trust No. 25, dated May 29, 1998, Plaintiff: Bradley Paul Nelson, William Butler Berndt, Schopf & Weiss, Chicago, IL.

For Vlg of Lindenhurst, an Illinois municipal corporation, Ken Czyzewicz, an individual, Mark Federman, an individual, Mary McCarthy, an individual, Fred Messmer, an individual, Carl Norlin, an individual, Barbara Stout, an individual, Pam Dunham, an individual, Carol Zerba, James B Stevens, an individual, Defendants: Paul P. Phillips, Soffietti, Johnson, Teegen, Phillips & Schwartz, Ltd., Fox Lake, IL; William W. Kurnik, Basileios John Foutris, Knight, Hoppe, Kurnik & Knight, LLC, Des Plaines, IL.

For Zale Equities, Inc., an Illinois corporation, Zale Equities, LLC, an Illinois limited liability company, Zale Group, Inc., an Illinois corporation, Defendants: Martin Stuart Korey, Stone, Pogrund, Korey & Spagat, Chicago, IL.

For Nature's Ridge-Lindenhurst, LLC, an Illinois limited liability company, Leon Joffe, an individual, Defendants: Martin Stuart Korey, James P. Ziegler, Stone, Pogrund, Korey & Spagat, Chicago, IL.

For Paul Baumunk, an individual, Defendant: William W. Kurnik, Basileios John Foutris, [\*2] Knight, Hoppe, Kurnik & Knight, LLC, Des Plaines, IL.

For KB Home, a Delaware corporation, KB Home Illinois, Inc., a Delaware corporation, Gordon White, an individual, Defendants: Martin Stuart Korey, Dean J Lurie, Stone, Pogrund, Korey & Spagat, Chicago, IL.

**Judges:** Judge Rebecca R. Pallmeyer.

**Opinion by:** REBECCA R. PALLMEYER

## **Opinion**

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### **MEMORANDUM OPINION AND ORDER**

This dispute arises from the removal and relocation of a 1,000-foot portion of road that was situated along the edge of property owned by Plaintiff C. Pelfresne in the Village of Lindenhurst, Illinois. The Village approved a petition by other local property owners to remove and relocate the road in connection with a plan to create a single-family development and an adjacent 3.45-acre commercial development. As a result, Plaintiff lost access to the road and filed this lawsuit on September 30, 2003 seeking declaratory and injunctive relief and compensation for the loss of his property value. Plaintiff initially asserted claims of restraint of trade, trespass, private nuisance, and civil conspiracy against the following Defendants: real estate developers Nature's Ridge-Lindenhurst, LLC, Zale Equities, Inc., Zale Equities, [\*3] LLC, Zale Group, Inc., and Leon Joffe (collectively, the "Zale Defendants"); LaSalle Bank National Association ("LaSalle"); and the Village, Village Trustees Ken Czyzewicz, Mark Federman, Mary McCarthy, Fred Messmer, Carl Norlin, Barbara Stout, Pat Dunham, and Carol Zerba, Village President Paul Baumunk, and Village Administrator James Stevens (collectively, the "Village Defendants").

The Zale Defendants and the Village Defendants filed separate motions to dismiss the complaint, which the court granted in part and denied in part on July 23, 2004. [Pelfresne v. Village of Lindenhurst, 2004 U.S. Dist. LEXIS 14176, No. 03 C 6905, 2004 WL 1660812 \(N.D. Ill. July 23, 2004\)](#). On September 7, 2004, Plaintiff filed an Amended Complaint seeking to remedy the deficiencies in the original complaint, and adding real estate development companies KB Home and KB Home Illinois, Inc. (collectively, the "KB Defendants"), and Gordon White as Defendants. The Zale and KB Defendants and the Village Defendants again move for dismissal of the Amended Complaint on a number of grounds. For the reasons set forth below, the Zale and KB Defendants' motion is granted in part and denied in part, and the Village Defendants' motion [\*4] is granted.

### **BACKGROUND**

The facts of this case as set forth in the court's July 23, 2004 Memorandum Opinion and Order are largely repeated in the Amended Complaint. See [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812, at \\*1-5](#). This opinion assumes the reader's familiarity with the earlier decision and recites the relevant facts here only briefly.

### **A. The Parties**

Plaintiff is a Michigan-based real estate developer who owns a Trust holding approximately 100 acres of land located on what was formerly the northeast corner of Savage Road and Grass Lake Road in unincorporated Lake County, Illinois. (Cmplt. PP 1,2.)<sup>1</sup> Prior to its removal, Savage Road ran east-west and intersected Grass Lake Road, which runs northwest-southeast, at approximately a 45-degree angle. (Ex. A to Cmplt.)

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<sup>1</sup> The Amended Complaint is cited as "Cmplt. P \_\_\_. As noted earlier, the court is uncertain of the relationship, if any, among Plaintiff "C. Pelfresne" and other Pelfresnes who have filed similar complaints involving other Illinois municipalities.

[\*5] The Village is an Illinois municipal corporation located in Lake County, Illinois. Defendant Paul Baumunk is a citizen and resident of Illinois who served as President of the Village from April 1999 through April 2003. (Cmplt. PP 3, 12.) Defendants Ken Czyzewicz, Mark Federman, Mary McCarthy, Fred Messmer, Carl Norlin, Barbara Stout, Pat Dunham, and Carol Zerba (collectively, the "Village Trustees") are current or former Trustees of the Village. All are residents and citizens of Illinois. (*Id.* P 13.) Defendant James B. Stevens is also a resident and citizen of Illinois who serves as Village Administrator. (*Id.* P 14.)

Defendant Zale Equities, LLC ("Zale LLC") conducted real estate development and related activities as an Illinois limited liability company until it was involuntarily dissolved on October 31, 2002. Prior to its dissolution, Zale LLC's principal place of business was in Lake County, Illinois, and its former members - Edward Zale, Roberta Zale, Amy Joffe, Melissa Norris, and Leon Joffe - are all citizens of Illinois.<sup>2</sup> (*Id.* P 5.) Defendants Zale Equities, Inc. and Zale Group, Inc. were Illinois real estate development corporations with principal places of [\*6] business in Lake County, Illinois. Zale Equities was involuntarily dissolved on September 2, 2003, and Zale Group was involuntarily dissolved on November 1, 2000.<sup>3</sup> (*Id.* PP 4, 6.) Defendant Zale Enterprises, Inc., an Illinois corporation with its principal place of business in Lake County, Illinois, conducts real estate development and related activities in Lake and Cook Counties in Illinois. (*Id.* P 7.)

Defendant Nature's Ridge-Lindenhurst, LLC ("NRL") is in the business of owning, developing, and marketing real estate in Lindenhurst, Illinois. NRL is an Illinois limited liability company with its principal place of business in Lake County, and its members - Edward Zale, Roberta Zale, Amy Joffe, Melissa Norris, and Leon Joffe - are all citizens of Illinois. (*Id.* P 8.) Defendant LaSalle Bank [\*7] National Association is a national banking association with its principal place of business in Chicago, Illinois. (*Id.* P 9.) Defendant Leon Joffe, a resident and citizen of Illinois, is in the business of developing and marketing real estate in Lake and Cook Counties "through Zale Equities, Zale LLC, Zale Group, Zale Enterprises, NRL, [LaSalle], and other entities." (*Id.* P 10.)

Defendants KB Home and KB Home Illinois, Inc. are Delaware corporations with their principal places of business in Los Angeles, California. The KB Defendants conduct real estate and related activities in, among other places, Lake County, Illinois. (*Id.* P 15, 16.) On or about September 5, 2003, the KB Defendants acquired the assets of the Zale Defendants. (*Id.* P 36.) Gordon White is in the business of developing and marketing real estate in Lake and Cook Counties "through Zale Equities, Zale LLC, Zale Group, Zale Enterprises, NRL, [LaSalle], KB Home, KB Illinois, and other entities." He is a citizen and resident of Illinois. (*Id.* P 11.)

## B. The Savage Road Dispute

At some point prior to April 19, 2000, either the Zale Defendants or LaSalle purchased or contracted to purchase [\*8] approximately 80 acres of land then located at the southeast corner of Savage Road and Grass Lake Road in unincorporated Lake County, Illinois. On an unspecified date, LaSalle became owner in fee simple title of that property, "with one or more of the . . . Zale Defendants owning the beneficial interest." (*Id.* PP 9, 19.) LaSalle and the Zale Defendants intended to develop the property as a single-family development to be known as "Nature's Ridge," with a 3.45-acre commercial development in the northeast corner of the property (collectively, "Nature's Ridge"). To that end, "one or more of the [LaSalle or the] Zale Defendants had filed petitions and other documents with the Village . . . to annex the Nature's Ridge property under the terms of a proposed annexation agreement." The proposed agreement required the Village to rezone the Nature's Ridge property for the planned residential and commercial purposes. (*Id.* PP 21, 22.) It also called for the removal of Savage Road from its 45-degree intersection with Grass Lake Road to a point at least 1,000 feet east of that intersection, and replacing it with a section of road that curved south to form a 90-degree T-shaped intersection [\*9] with Grass Lake Road. (*Id.* P 27.) (See Map, attached as Exhibit A.) See also [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812, at \\*1.](#)

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<sup>2</sup> The Complaint does not provide an explanation for the involuntary dissolution.

<sup>3</sup> Again, the Complaint does not explain why these companies were voluntarily dissolved or who initiated those proceedings.

On April 19, 2000, the Village Plan Commission held a hearing regarding the proposed development plan. (*Id.* P 23.) Sometime thereafter, over objection from an attorney for the Trust (owned by Plaintiff), the Village and the Village Trustees approved both the rezoning and the relocation of Savage Road. (*Id.* PP 25, 27.) In late 2002, "one or more of [the LaSalle or] Zale Defendants" effected the plan described above, and Plaintiff, whose property abutted Savage Road prior to its relocation, lost all access to that road. (*Id.* P 29.) Plaintiff claims that Defendants sought unsuccessfully to purchase his property sometime "in the past," and that they removed the road to "drive down the value of Plaintiff's property in the hope that they can some day purchase the property for less and in retaliation for Plaintiff's refusal to sell to these defendants." (*Id.* PP 31, 32.)

### C. The Complaint

On September 30, 2003, Plaintiff filed suit against the Zale Defendants, LaSalle, and the Village Defendants. Count I alleged that all Defendants [\*10] failed to take any of the steps required by § 11-91-1 of the Illinois Municipal Code, [65 ILCS 5/11-91-1](#), including public notice, a public hearing, passage of a Village ordinance by three-fourths vote of the Village Board of Trustees, or payment of just compensation to landowners who lost frontage onto Savage Road. [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812, at \\*2](#). Plaintiff sought a declaration pursuant to [28 U.S.C. § 2201](#) that the Village did not properly vacate Savage Road, that Plaintiff has a right of access to Savage Road in its original location, that the Village Defendants improperly consented to the unlawful removal of Savage Road, that the Zale Defendants were without authority to remove Savage Road, and that the Village Defendants were without authority to vacate Savage Road. *Id.* Plaintiff also sought a preliminary and permanent injunction under [FED. R. CIV. P. 65](#) requiring Defendants to restore Savage Road to its previous condition and location, and prohibiting further development along the relocated portion of Savage Road. *Id.*

Count II, titled "Inverse Condemnation," asserted that by closing the road, the Village Defendants damaged Plaintiff's [\*11] property for public use without just compensation as required by [Article I, § 15 of the Illinois Constitution](#). According to Plaintiff, "the value of his property has substantially depreciated in fair cash market value" in an amount greater than \$ 75,000 as a result of the roadway's removal. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*3](#). In Count III, asserted only against the Village, Plaintiff sought reimbursement under [65 ILCS 5/11-9-1](#) for the depreciation in the fair market value of his property, and for the deprivation of his access to and frontage on Savage Road. *Id.*

In Count IV, Plaintiff alleged that all Defendants violated § 1 of the Sherman Act, [15 U.S.C. § 1](#), as they "agreed, combined, and conspired" to annex the Nature's Ridge property and to relocate Savage Road in restraint of trade and commerce in the Lindenhurst area real estate market beginning in early 2000. Count V alleged that all Defendants willfully, wantonly, and knowingly entered into an agreement to remove and relocate Savage Road without following the procedures set forth in [65 ILCS 5/11-91-1, et seq.](#), and that each Defendant "committed one or more tortious acts in furtherance of the conspiracy, including but [\*12] not limited to trespass, private nuisance, and restraint of trade and commerce." *Id.* Count VI asserted that Defendants' "improper removal of Savage Road interfered with [Plaintiff's] property right in and use of the access to Savage Road and constitutes an unlawful trespass," resulting in substantial loss in the property's value. Finally, Plaintiff alleged in Count VII that Defendants' "improper removal of Savage Road has eliminated [Plaintiff's] right of access to and frontage on Savage Road and has therefore caused an unreasonable interference with the use and enjoyment of [Plaintiff's] property." *Id.* Notably, Plaintiff did not allege a claim for the taking of his property without just compensation, perhaps because Plaintiff has not yet exhausted his state procedural remedies. See [Sprint Spectrum L.P. v. City of Carmel, 361 F.3d 998, 1003-04 \(7th Cir. 2004\)](#) ("a property owner must exhaust all available state remedies for compensation prior to bringing a taking claim to federal court.")<sup>4</sup>

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<sup>4</sup>The court understands that at least some Defendants may be willing to compensate Plaintiff for the diminution in value of his property as a result of the relocation of Savage Road. Yet Plaintiff has been puzzlingly reluctant to disclose the results of an appraisal to ascertain the amount of that loss.

#### [\*13] D. The July 23, 2004 Opinion

The Zale Defendants and the Village Defendants separately moved to dismiss the complaint for lack of standing and failure to state a claim. In its July 23, 2004 Memorandum Opinion and Order, the court first determined that Plaintiff has standing to sue for relief based on his allegation that his property value has declined. The court noted, however, that "if during the discovery process Defendants can demonstrate that the fair market value of Plaintiff's property has not decreased, . . . the court will entertain motions to dismiss pursuant to [Rule 12\(b\)\(1\)](#), as well as for sanctions against Plaintiff." [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*6](#).

The court next upheld Plaintiff's claim for declaratory relief in Count I, but dismissed his claim for injunctive relief due to his failure to satisfy the court that his alleged injuries could not be compensated with money damages. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*7-9](#). With respect to Count II alleging "Inverse Condemnation," the court held that Plaintiff stated a valid claim for damage under [Article I, § 15 of the Illinois Constitution](#), again based on his allegation that his property value has substantially depreciated. Plaintiff could not, however, [\*14] assert that claim against any of the individual Village Defendants. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*10-11](#).

The court rejected the Village Defendants' argument for dismissing Count III on the grounds that Plaintiff has an easement for "ingress and egress of farm implement vehicles and supporting vehicles." In the court's view, there was a question of fact as to whether the easement provided Plaintiff with adequate substitute access to Savage Road. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*12](#). The court, however, dismissed Plaintiff's Sherman Act claim without prejudice: Plaintiff's assertions that his own property value had decreased but that the Lemont real estate market generally had increased were inconsistent and, in the court's view, defeated the allegation that Defendants' actions had anticompetitive effects. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*14](#). The court also dismissed Counts VI and VII for failure to allege any physical invasion of property as required to state claims for trespass and private nuisance. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*14-16](#). Having dismissed Plaintiff's underlying tort claims (trespass, private nuisance, and restraint of trade and commerce), the court dismissed Plaintiff's civil conspiracy claim (Count V) as well. [2004 U.S. Dist. LEXIS 14176, \[WL\] at \\*16](#) (citing [Fritz v. Johnston, 209 Ill. 2d 302, 317, 807 N.E.2d 461, 470, 282 Ill. Dec. 837 \(2004\)](#) [\*15] (requiring that conspirators commit a tortious or unlawful act in furtherance of the conspiracy)).

#### E. The Amended Complaint

On September 3, 2004, Plaintiff filed an Amended Complaint seeking to remedy the deficiencies identified in the original complaint, and adding the KB Defendants and Gordon White as Defendants. Once again, Plaintiff's most logical claim - unlawful taking - appears nowhere in the Complaint. Nor has he provided any information as to the amount by which his property has been devalued by the relocation of Savage Road. Plaintiff instead advances the following theories of relief.

Count I seeks declaratory relief for Defendants' failure to take any of the steps required by § 11-91-1 of the Illinois Municipal Code, [65 ILCS 5/11-91-1](#), including public notice, a public hearing, passage of a Village ordinance by three-fourths vote of the Village Board of Trustees, or payment of just compensation to landowners who lost frontage onto Savage Road. (Cmplt. PP 35, 40.) Count II charges the Village with violating [Article I, § 15 of the Illinois Constitution](#) by taking Plaintiff's property without just compensation. (*Id.* P 42.) In Count III, Plaintiff seeks damages [\*16] from the Village under [65 ILCS 5/11-9-1](#) for the depreciation in the fair market value of his property, and for the deprivation of his access to and frontage on Savage Road. (*Id.* PP 48-52.)

Count IV asserts that Defendants violated [§ 1](#) of the Sherman Act by conspiring to "unreasonably restrain[] competition for the sale and development of real estate" in the Lemont area and to preclude Plaintiff and other developers "from fully competing with the Zale Defendants and the KB Defendants for the sale and development of medium to high-density mixed-use property." (*Id.* P 59, 62.) These actions, Plaintiff claims, have restricted competition and limited consumer choice in the Lemont area, and have "caused or reasonably will cause

increased prices for purchasers and consumers of both residential and commercial real estate in the relevant market." (*Id.* PP 64, 65.)

In Count V. Plaintiff alleges that the Zale and KB Defendants have been unjustly enriched by the relocation of Savage Road. (*Id.* PP 70-72.) Count VI charges the Zale Defendants, the KB Defendants, Joffe, and White with tortious interference with Plaintiff's prospective economic advantage "from the eventual [\*17] development and sale of [his] property." (*Id.* P 74.) Count VII alleges that the Zale Defendants, Joffe, and White "willfully, maliciously, intentionally, and unlawfully interfered with and impaired Plaintiff's property right by unlawfully removing Savage Road and relocating it onto the Zale Defendants' property." (*Id.* P 81.) Count VII further alleges that the KB Defendants "willfully, maliciously, and intentionally aided, abetted, and assisted with the interference with and impairment of Plaintiff's property rights by acting to cement and retaining the Zale Defendants' and KB Defendants' exclusive access to and control over the relocated portion of Savage Road and its frontage." (*Id.* P 82.) Finally, Count VIII charges all Defendants with civil conspiracy. (*Id.* PP 86-89.)

The Zale and KB Defendants have moved to dismiss all claims against them, and the Village Defendants seek dismissal of Counts I, IV, and VIII. The court has diversity jurisdiction over this matter pursuant to [28 U.S.C. § 1332](#) and considers each motion below.

## DISCUSSION

**HN1** [↑] The purpose of a motion to dismiss is to test the sufficiency of the plaintiff's complaint, not [\*18] to decide its merits. *Gibson v. City of chicago*, [910 F.2d 1510, 1520 \(7th Cir. 1990\)](#). A motion to dismiss will be granted only "if it appears beyond doubt that the plaintiff can prove no set of facts 'in support of his claim which entitles him to relief.' *Conley v. Gibson*, [355 U.S. 41, 45-46, 2 L. Ed. 2d 80, 78 S. Ct. 99 \(1957\)](#). In reviewing a motion to dismiss for failure to state a claim, the court accepts as true all factual allegations in the plaintiff's complaint and draws all reasonable inferences in his favor. *Franzoni v. Hartmarx Corp.*, [300 F.3d 767, 770 \(7th Cir. 2002\)](#).

The Zale, KB, and Village Defendants all move to dismiss Count I as duplicative of Count III. The Village Defendants also claim that they are immune from liability under the Sherman Act (Count IV) pursuant to *Parker v. Brown*, [317 U.S. 341, 352, 87 L. Ed. 315, 63 S. Ct. 307 \(1943\)](#), and that they are absolutely immune from liability for civil conspiracy (Count VIII) under the Illinois Tort Immunity Act, [745 ILCS 10/1-101 et seq.](#) The Zale and KB Defendants insist that there is no public injury to support Plaintiff's Sherman Act claim, and that Plaintiff has not properly alleged claims for unjust enrichment, [\*19] tortious interference, malicious injury to property, or civil conspiracy.

### I. Count I

In Count I of the Amended Complaint, Plaintiff seeks a declaration pursuant to [28 U.S.C. § 2201](#) that the Village did not properly vacate Savage Road, that Plaintiff has a right of access to Savage Road in its original location, that the Village Defendants improperly consented to the unlawful removal of Savage Road, that the Zale and KB Defendants were without authority to remove Savage Road, and that the Village Defendants were without authority to vacate Savage Road. (Cmplt. P 40.) The Zale, KB, and Village Defendants all insist that this claim is duplicative of Count III, which seeks money damages from the Village under [65 ILCS 5/11-91-1](#) for the property damage caused by the relocation of Savage Road. (Zale/KB Mem., at 2; Village Mem., at 7 <sup>5</sup> (citing *Green Bay Packaging, Inc. v. Hoganson & Assocs., Inc.*, [362 F. Supp. 78, 82 \(N.D. Ill. 1973\)](#) (striking as duplicative two counterclaims alleging breach of an oral contract where the complaint sought declaratory relief as to the contractual rights of the parties).)

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<sup>5</sup> The Zale Defendants' and KB Defendants' Motion to Dismiss Plaintiff's Amended Complaint is cited as "Zale/KB Mem., at \_\_\_\_\_. The Memorandum of Village of Lindenhurst Defendants in Support of their Motion to Dismiss Counts I, IV, and VIII of the Amended Complaint is cited as "Village Mem., at \_\_\_\_\_. "

[\*20] [HN2](#) "The purposes of declaratory judgments are to 'clarify[] and settle the legal relations at issue' and to 'terminate and afford relief from uncertainty, insecurity, and controversy giving rise to the proceeding.'" [Amari v. Radio Spirits, Inc.](#), 219 F. Supp. 2d 942, 944 (N.D. Ill. 2002) (quoting [Tempco Elec. Heater Corp. v. Omega Eng'g, Inc.](#), 819 F.2d 746, 749 (7th Cir. 1987)). "Where the substantive suit would resolve the issues raised by the declaratory judgment action, the declaratory judgment action 'serve[s] no useful purpose' because the controversy has 'ripened' and the anticipation and uncertainty of litigation are alleviated." *Id.* In this case, Plaintiff has filed a lawsuit seeking damages caused by Defendants' unlawful relocation of a portion of Savage Road. Plaintiff thus has no need for a declaratory judgment establishing the same unlawful conduct. See [Dixie Gas & Food, Inc. v. Shell Oil Co.](#), 2005 U.S. Dist. LEXIS 12010, No. 03 C 8210, 2005 WL 1273273, at \*7 (N.D. Ill. May 25, 2005) ("the process for determination on the merits is underway in this suit, and the additional declaratory judgment action requested by plaintiffs is redundant.")

Plaintiff [\*21] disagrees that the relief requested in Count I is "entirely duplicative" of the relief requested in other counts, noting that he seeks "a declaration that he has a right of access to 650 feet of frontage on Savage Road in its original location, and that the Village Defendants are without authority to vacate Savage Road." (Pl. Resp., at 13-14.)<sup>6</sup> As Defendants note, however, the court already rejected Plaintiff's claim for injunctive relief requiring the relocation of Savage Road to its original location. (Zale/KB Reply, at 6.)<sup>7</sup> [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812](#), at \*8-9. Defendants' motion to dismiss Count I as duplicative is granted.<sup>8</sup>

## [\*22] II. Count IV

Defendants next argue that Plaintiff's Sherman Act claim once again fails because he has alleged neither a personal nor a public injury. The Village Defendants also claim immunity from liability under [Parker v. Brown](#), 317 U.S. 341, 87 L. Ed. 315, 63 S. Ct. 307 (1943).

### A. The Zale and KB Defendants

[HN3](#) To state a claim for relief under § 1, Plaintiff must allege "either that the contract, combination, or conspiracy resulted in a *per se* violation of the Sherman Act or that it unreasonably restrained competition in a relevant market." [MCM Partners, Inc. v. Andrews-Bartlett & ASSOCS., Inc.](#), 62 F.3d 967, 976 (7th Cir. 1995) (citations omitted). As noted, the court previously dismissed Plaintiff's Sherman Act claim for failure to sufficiently allege anticompetitive effects. Specifically, Plaintiff's repeated assertion that his property value had decreased was inconsistent with his claim in Count IV that consumers were being injured by the fact that prices in the Lindenhurst real estate market had increased. [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812](#), at \*14. Plaintiff contends that the Amended Complaint now alleges at least three types of injury to [\*23] competition: (1) a reduction in supply or output; (2) increased prices; and (3) a reduction in the quality and quantity of consumer choice. (Pl. Resp., at 3.) Plaintiff's theory is as follows: The Lindenhurst market "is characterized by a small and continually shrinking supply of remaining undeveloped properties with the potential for development as medium to high-density mixed-use developments, and a relatively strong and growing demand for such property." (Cmplt. P 55.) The relocation of Savage Road has "removed" Plaintiff's property from the market for medium to high-density mixed-use development because the property is no longer at an intersection and no longer has any frontage on, or

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<sup>6</sup> Plaintiff C. Pelfresne's Response to Defendants' Motions to Dismiss is cited as "Pl. Resp., at \_\_\_\_."

<sup>7</sup> The Zale and KB Defendants' Reply in Support of the Zale and KB Defendants' Motion to Dismiss the Plaintiff's Amended Complaint is cited as "Zale/KB Reply, at \_\_\_\_."

<sup>8</sup> Plaintiff notes that this court previously upheld his claim for declaratory judgment. (Pl. Resp., at 13.) See [Pelfresne, 2004 U.S. Dist. LEXIS 14176, 2004 WL 1660812](#), at \*7-8. In addressing the previous motions to dismiss, however, the court was asked to consider only whether Plaintiff had sufficiently alleged a violation of state law and an injury in fact, and not whether the declaratory judgment and the damages claims were duplicative.

useful access to, Savage Road. (Pl. Resp., at 4.) In Plaintiff's view, this has resulted in an output restriction - i.e., a reduction in the supply of property in the relevant market. "Output restrictions are classic per se violations which personify the law of supply because product scarcity causes consumers to pay inflated prices to satisfy demand. Unlike pure supply and demand, competitors use output restrictions to inflate profit by thwarting competition by intentionally limiting product availability. [\*24] " [United States v. Andreas, 39 F. Supp. 2d 1048, 1059 \(N.D. Ill. 1998\)](#).

With the reduction in supply of property that may be developed as medium to high-density mixed-use developments, Plaintiff argues, the price to consumers for such property will increase, and the quality and quantity of their property choices will decrease. (Pl. Resp., at 5-6 (citing [MCM Partners, 62 F.3d at 972](#) (antitrust claim stated where defendants' conduct allegedly eliminated plaintiff from the market, securing defendants a "virtual monopoly" and allowing them to charge higher rates for rental equipment); *Davis v. First Nat'l Bank of Westville*, 868 F.2d 206, 208 (7th Cir. 1989).) Under this theory, Plaintiff insists, the allegations that the value of his property, which cannot be used for medium to high-density mixed-use developments, has decreased while the price for properties that may be used for medium to high-density mixed-use developments has increased are entirely consistent. (Pl. Resp., at 5.)

The Zale and KB Defendants do not specifically respond to any of these arguments, claiming instead that Plaintiff's theory is flawed because he does not allege any personal [\*25] injury from the Sherman Act violation. According to Defendants, "the alleged injured class are consumer/developers wishing to develop property in the Lindenhurst area," and Plaintiff does not claim to be one of those consumer/developers. (Zale/KB Reply, at 2 (citing [Metro Cable Co. v. CATV of Rockford, Inc., 516 F.2d 220 \(7th Cir. 1975\)](#).) In *Metro Cable*, the plaintiff applied for but did not receive a franchise from the City of Rockford, Illinois to construct and operate a cable television transmission system. [516 F.2d at 222](#). The plaintiff sued the company that did obtain the franchise (CATV), its affiliate, and four individuals associated with those companies, alleging that they organized CATV in part to induce the city's mayor and an alderman to oppose the plaintiff's current and future franchise applications. [Id. at 222-24](#). The plaintiff argued that this violated the Sherman Act because the defendants formed a plan to block any cable television in Rockford that would compete with their station (WCEE-TV), and organized CATV to secure what was in effect an exclusive franchise "to delay building cable facilities in order to postpone [\*26] the day when WCEE-TV would have competition from cable television." [Id. at 232-33](#).

The court found that the part of the plan consisting of inducing the city council to grant CATV a franchise and deny one to the plaintiff did not fall within the Sherman Act, noting that the *Noerr-Pennington* doctrine protects concerted efforts to induce government to take lawful action. [Id. at 227, 233](#) (citing [United Mine Workers of America v. Pennington, 381 U.S. 657, 670, 14 L. Ed. 2d 626, 85 S. Ct. 1585 \(1965\)](#) (noting that [Eastern Railroad Presidents Conference v. Noerr Motor Freight, Inc., 365 U.S. 127, 5 L. Ed. 2d 464, 81 S. Ct. 523 \(1961\)](#), "shields from the Sherman Act a concerted effort to influence public officials regardless of intent of purpose.")) The only injured parties in *Metro Cable* were those "who suffered injury by reason of the delay in establishing a cable television system in Rockford, for example, a distant television station which could only reach Rockford consumers through cable television facilities." [Id. at 233](#).

The Zale and KB Defendants appear to be arguing, somewhat obliquely, that they cannot be liable under § 1 of the Sherman Act by virtue of the *Noerr-Pennington* [\*27] doctrine. [HN4](#) Under that doctrine, "parties may petition the government for official action favorable to their interests without fear of suit, even if the result of the petition, if granted, might harm the interests of others." [Tarpley v. Keistler, 188 F.3d 788, 794 \(7th Cir. 1999\)](#). See also [Greater Rockford Energy and Tech. Corp. v. Shell Oil Co., 998 F.2d 391, 397 \(7th Cir. 1993\)](#) ("lobbying that would arguably restrain trade is protected political activity and does not violate the antitrust laws.") That is precisely what Plaintiff has alleged here.

Plaintiff claims that the Zale Defendants conspired with the Village Defendants "to annex the Nature's Ridge property and to remove and relocate Savage Road in restraint of trade and commerce in the market for the sale and development of prime medium to high-density mixed use real estate." (Cmplt. P 57.) Plaintiff also claims that after acquiring the assets of the Zale Defendants, the KB Defendants

induced and agreed with the Village Defendants to have the Village approve an ordinance purporting to vacate the removed section of Savage Road and took other affirmative steps to ensure the KB Defendants' [\*28] continual improper and unlawful access to that frontage, to the exclusion of Plaintiff and other landowners.

(*Id. P 58.*) The Zale and KB Defendants had a right to petition the Village to annex Nature's Ridge and to relocate Savage Road, even though those actions ultimately harmed Plaintiff's interests. *Tarpley, 188 F.3d at 794; In re Brand Name Prescription Drugs Antitrust Litig., 186 F.3d 781, 788-89 (7th Cir. 1999)* (the Noerr-Pennington doctrine "exempts from antitrust law collusive efforts to obtain governmental protection against the winds of competition.") Notably, there is nothing to suggest that the Zale and KB Defendants' "activities [were] not genuinely aimed at procuring favorable government action." *City of Columbia v. Omni Outdoor Advertising, Inc., 499 U.S. 365, 380, 113 L. Ed. 2d 382, 111 S. Ct. 1344 (1991)* ("A classic example [of the sham exception] is the filing of frivolous objections to the license application of a competitor, with no expectation of achieving denial of the license but simply in order to impose expense and delay.") The Zale and KB Defendants' motion to dismiss Count IV is granted.

## B. The Village Defendants

[\*29] The Village Defendants argue that they are immune from liability under the Sherman Act because their actions in annexing Nature's Ridge and approving the relocation of Savage Road are "authorized implementation[s] of state policy." (Village Mem., at 3 (quoting *City of Columbia, 499 U.S. at 371*.)) In *City of Columbia*, the plaintiff objected to a Columbia, South Carolina ordinance restricting the size, location, and spacing of billboards within the city. The ordinance "obviously benefitted" a favored local company, Columbia Outdoor Advertising, Inc. ("COA"), which "already had its billboards in place," and "severely hindered" the plaintiff's ability to compete. *499 U.S. at 368*. The plaintiff filed suit against the City and COA alleging, in part, that the ordinance was the result of "an anticompetitive conspiracy between city officials and COA" in violation of § 1 of the Sherman Act. *Id. at 369*. Reversing a judgment in favor of the plaintiff, the Supreme Court first noted its decision in *Parker v. Brown, 317 U.S. 341, 87 L. Ed. 315, 63 S. Ct. 307 (1943)* that the Sherman Act does "not apply to anticompetitive restraints imposed by the States 'as [\*30] an act of government.'" *Id. at 370* (quoting *Parker, 317 U.S. at 352*). The Court confirmed that *HNS* [↑] Parker immunity would not protect local governments directly, but recognized that such immunity does apply where "a municipality's restriction of competition [is] an authorized implementation of state policy." *Id.* (citing *Town of Hallie v. City of Eau Claire, 471 U.S. 34, 38, 85 L. Ed. 2d 24, 105 S. Ct. 1713 (1985)*). For the immunity to apply, however, there must be a "clear articulation of a state policy to authorize anticompetitive conduct' by the municipality." *Id. at 372* (quoting *Hallie, 471 U.S. at 40*). This requirement is satisfied "if suppression of competition is the 'foreseeable result' of what the state authorizes." *Id.* (quoting *Hallie, 471 U.S. at 42*).

Applying these principles to the Columbia ordinance, the Court held that "no more is needed to establish, for *Parker* purposes, the city's authority to regulate than its unquestioned zoning power over the size, location, and spacing of billboards." *Id.* The Court further determined that

the very purpose of zoning regulation is to displace unfettered [\*31] business freedom in a manner that regularly has the effect of preventing normal acts of competition, particularly on the part of new entrants. A municipal ordinance restricting the size, location, and spacing of billboards (surely a common form of zoning) necessarily protects existing billboards against some competition from newcomers.

*Id. at 373.* As for the plaintiff's invocation of a "conspiracy exception" to *Parker* immunity, the Court reaffirmed its "rejection of any interpretation of the Sherman Act that would allow plaintiffs to look behind the actions of state sovereigns to base their claims on 'perceived conspiracies to restrain trade.'" *Id. at 379* (quoting *Hoover v. Ronwin, 466 U.S. 558, 580, 80 L. Ed. 2d 590, 104 S. Ct. 1989 (1984)*). The Court therefore found the City immune from liability.

The Village Defendants argue that the Village's authority to enter into annexation agreements (such as the annexation of Nature's Ridge) and to regulate land use, lot size, roads, and other matters necessary for the public health, safety, and welfare (such as the relocation of Savage Road) is established by state law as set forth in the

Illinois Municipal Code, [65 ILCS 5/11-15.1-1](#), [5/11-15.1-2\(b\)](#), [\[\\*32\] \(f\), 5/11-91-1](#).<sup>9</sup> (Village Mem., at 4.) Plaintiff insists that the Village's actions were not authorized by state policy because the Village allowed the Zale and KB Defendants to "remove and relocate Savage Road for Zale's benefit, without following the requirements of state law mandating prior notice and a prior hearing before a road is vacated." (Pl. Resp., at 6.) As the Village Defendants point out, however, the Supreme Court rejected just such an argument in *City of Columbia*, where it stated:

**HN6** "To be sure, state law 'authorizes' only agency decisions that are substantively and procedurally correct. Errors of fact, law, or judgment by the agency are not 'authorized.' .... We ... believe, [however], that in order to prevent *Parker* from undermining the very interests of federalism it is designed to protect, it is necessary to adopt a concept of authority broader than what is applied to determine the legality of the municipality's action under state law. .... It suffices for the present to conclude that here no more is needed to establish, for *Parker* purposes, the city's authority to regulate than its unquestioned zoning power over the size, location, and spacing [\[\\*33\]](#) of billboards.

[499 U.S. at 371-72](#) (quoting P. Areeda & H. Hovenkamp, *Antitrust Law* P 212.3b, at 145 (Supp. 1989)). As in *City of Columbia*, the Village has unquestioned authority to annex property and relocate roads, which suffices as authority for purposes of *Parker* immunity.

[\[\\*34\]](#) Plaintiff argues that *Parker* immunity nonetheless does not apply here because [§ 11-91-1](#) "has nothing to do with displacing competition in favor of regulation." (Pl. Resp., at 7.) Noting the statute's language that "the relief to the public from further burden and responsibility of maintaining any street or alley, or part thereof, constitutes a public use or public interest authorizing the vacation," Plaintiff contends that [65 ILCS 5/11-91-1](#) simply grants authority to municipalities to vacate roads . . . to relieve the burden on a municipality to maintain the road" and "is not aimed at replacing competition with regulation." (*Id.* at 8.) The problem with this argument is that an anticompetitive effect need only be the "foreseeable result," and not the stated aim or purpose of the statute. As the Supreme Court explained in *City of Columbia*,

We have rejected the contention that this requirement [authorization of anticompetitive conduct] can be met only if the delegating statute explicitly permits the displacement of competition . . . It is enough, we have held, if suppression of competition is the "foreseeable result" of what the statute authorizes.

[\[\\*35\] 499 U.S. at 372-73](#) (quoting *Hallie, 471 U.S. at 41-42*).

**HN9** To be sure, a municipality is not automatically beyond the reach of antitrust laws merely by virtue of a state delegation of authority. (Pl. Resp., at 8 (citing *Lancaster Community Hosp. v. Antelope Valley Hosp. Dist.*, [940 F.2d 397, 400 \(9th Cir. 1991\)](#)) ("The courts must assure themselves that the subordinate [entity] acts in accord with the state's wishes when it contravenes the federal antitrust laws."): *Surgical Care Ctr. of Hammond, L.C. v. Hospital Serv. Dist. No. 1 of Tangipahoa Parish*, [171 F.3d 231, 235 \(5th Cir. 1999\)](#) (finding that "it is not the foreseeable

<sup>9</sup> [Section 11-15.1-1](#) provides that "the corporate authorities of any municipality may enter into an annexation agreement with one or more of the owners of record of land in unincorporated territory." [65 ILCS 5/11-15.1-1](#). [Section 11-15.1-2](#) states that an annexation agreement may [HN7](#) provide for:

(b) The continuation in effect, or amendment, or continuation in effect as amended, of any ordinance relating to subdivision controls, zoning, official plan, and building, housing and related restrictions ....

\* \* \*

(f) Any other matter not inconsistent with the provisions of this Code, nor forbidden by law.

[65 ILCS 5/11-15.1-2\(b\), \(f\). Section 11-91-1 HN8](#) provides:

Whenever the corporate authorities of any municipality, whether incorporated by special act or under any general law, determine that the public interest will be subserved by vacating any street or alley, or part thereof, within their jurisdiction in any incorporated area, they may vacate that street or alley, or part thereof, by an ordinance.

result of allowing a hospital service district to form joint ventures that it will engage in anticompetitive conduct.".) As with other zoning ordinances, however, the Illinois statute authorizing the removal and relocation of roads has the foreseeable result of placing landowners at an economic disadvantage in connection with the development of their property. The Village Defendants are immune from liability under the Sherman Act and their motion to dismiss Count IV is granted.

### III. Count V

[\*36] The Zale and KB Defendants argue that Plaintiff cannot maintain his unjust enrichment claim because he fails to allege that he performed any services for Defendants. Citing *Oncology Therapeutics Network Joint Venture, L.P. v. Olympia Fields Internal Medicine Assocs., S.C., 2003 U.S. Dist. LEXIS 8073, No. 01 C 2079, 2003 WL 21087954 (N.D. Ill. May 13, 2003)*, Defendants contend that the elements of an unjust enrichment claim include: (1) Plaintiff performed services; (2) the benefit of those services was conferred upon Defendants; and (3) it is unjust for Defendants to retain the benefit without compensating Plaintiff. *2003 U.S. Dist. LEXIS 8073, [WL] at \*5*. Plaintiff insists that an unjust enrichment claim requires only a showing that (1) Defendants have unjustly retained a benefit to Plaintiff's detriment; and (2) Defendants' retention of the benefit violates the fundamental principles of justice, equity, and good conscience. (Pl. Resp., at 9 (citing *HPI Health Care Servs., Inc. v. Mt. Vernon Hosp., Inc., 131 Ill. 2d 145, 160, 545 N.E.2d 672, 679, 137 Ill. Dec. 19 (1989)*.)

The court agrees that Plaintiff need not have performed any services for Defendants in order to state a claim for unjust enrichment. The *Oncology* [\*37] *Therapeutics* court suggests such a requirement, but the case it relied on, *First Nat'l Bank of Springfield v. Malpractice Research, Inc., 179 Ill. 2d 353, 688 N.E.2d 1179, 228 Ill. Dec. 202 (1997)*, addressed the elements of a claim for quantum meruit, not unjust enrichment. *Id. at 365, 688 N.E.2d at 1185*. What is clear is that Plaintiff must establish that he furnished some benefit to Defendants "under circumstances which would make it unjust for [Defendants] to retain the benefit without paying." *Hayes Mechanical, Inc. v. First Indus., L.P., 351 Ill. App. 3d 1, 9, 812 N.E.2d 419, 285 Ill. Dec. 599, 351 Ill. App. 3d 1, 812 N.E.2d 419, 426, 285 Ill. Dec. 599 (1st Dist. 2004)*. Plaintiff may seek to recover a benefit that he gave directly to Defendants, or one which was transferred to Defendants by a third party. *State Farm General Ins. Co. v. Stewart, 288 Ill. App. 3d 678, 691, 681 N.E.2d 625, 633, 224 Ill. Dec. 310 (1st Dist. 1997)*. HN10 [↑] To establish that the retention of a benefit conferred upon Defendants by a third-party constitutes an unjust enrichment, Plaintiff must show that "(1) the benefit should have been given to the plaintiff, but the third party mistakenly gave it to the defendant instead; (2) the defendant [\*38] procured the benefit from the third party through some type of wrongful conduct, or (3) the plaintiff for some other reason had a better claim to the benefit than the defendant." *Id., 681 N.E.2d at 633-34*. See also *HPI Health Care Servs., Inc., 131 Ill. 2d at 161-62, 545 N.E.2d at 679*.

In this case, Plaintiff does not allege that he directly gave Defendants the benefit of the use of Savage Road. Rather, he suggests that the Zale and KB Defendants received that benefit from the Village, "as the relocation of Savage Road increased the value of the Zale Defendants' and the KB Defendants' property." (Cmplt. P 70.) Plaintiff does not, however, indicate which of the three *State Farm* elements supports his unjust enrichment claim. Plaintiff certainly cannot claim that the benefit "should have been given" to him, as he already had the use of Savage Road prior to its removal and relocation. Nor is there any evidence that the relocation was a "mistake." See *National Am. Ins. Co. v. Indiana Lumbermens Mut. Ins. Co., 221 F.3d 1339 (Table) (7th Cir. 2000)* (to establish a "mistake," "a plaintiff must point to some unintentional act arising from [\*39] ignorance, surprise, or misplaced confidence.") To the contrary, the Village both knew about and approved of the relocation, which resulted in Savage Road's meeting Grass Lake Road at a right (and safer) angle.

Plaintiff does allege that the Zale and KB Defendants procured the relocation from the Village "through some type of wrongful conduct" -- namely, they conspired to relocate Savage Road to reduce competition and "intentionally drive down the value of Plaintiff's property." (*Id.* PP 32-34.) To the extent the court has dismissed Plaintiff's Sherman Act claims, however, he has not sufficiently alleged that the Zale and KB Defendants engaged in wrongful conduct in order to secure the relocation of Savage Road from the Village. That leaves the theory that Plaintiff had a better claim to the road than the Zale or KB Defendants. Aside from arguing that the value of his property decreased and that Defendants did not follow proper procedures in relocating Savage Road, however, Plaintiff

offers nothing to suggest that his claim to the use of Savage Road was somehow superior to that of Defendants, or that the Village had a duty to maintain the road in its original location. Absent such [\*40] a showing, Plaintiff cannot maintain a claim for unjust enrichment.

## V. Count VI

The Zale and KB Defendants next contend that Plaintiff's claim for tortious interference with prospective economic advantage fails because he does not identify any third party with which he had a reasonable business expectancy. (Zale/KB Mem., at 5.) [HN11](#)[] To state a tortious interference claim, Plaintiff must allege (1) a reasonable expectation of entering into a valid business relationship; (2) Defendants' knowledge of that expectancy; (3) purposeful or intentional interference by Defendants that prevents Plaintiff's legitimate expectancy from ripening into a valid business relationship; and (4) damages to Plaintiff resulting from the interference. [\*Associated Underwriters of Am. Agency, Inc. v. McCarthy\*, 356 Ill. App. 3d 1010, 1020, 826 N.E.2d 1160, 1169, 292 Ill. Dec. 724 \(1st Dist. 2005\)](#). Numerous Illinois cases have stated that "[a] plaintiff states a cause of action only if he alleges a business expectancy with a specific third party as well as action by the defendant directed towards that third party." *Id.* See also [\*Solaia Technology, LLC v. Specialty Pub. Co.\*, 357 Ill. App. 3d 1, 826 N.E.2d 1208, 292 Ill. Dec. 772 \(1st Dist. 2005\)](#)[\*41] (collecting cases) (affirming dismissal of tortious interference claim where the plaintiffs failed to allege that "specific third parties actually contemplated entering into a business relationship with plaintiffs.") (emphasis in original).

Plaintiff argues that such specificity is not required to state a claim in federal court, which follows a liberal notice pleading standard. See [\*Kyle v. Morton High Sch.\*, 144 F.3d 448, 454 \(7th Cir. 1998\)](#) [HN12](#)[] ("Under the federal rule of notice pleading, 'all the Rules require is a short and plain statement of the claim that will give the defendant fair notice of what the plaintiff's claim is and the grounds upon which it rests.') (internal quotations omitted). In [\*Cook v. Winfrey\*, 141 F.3d 322 \(7th Cir. 1998\)](#), for example, the plaintiff wanted to sell the tabloid press his story about how national celebrity Oprah Winfrey had used cocaine while they were involved in a romantic relationship. *Id. at 324*. When Winfrey preempted him by revealing the drug abuse herself on her nationally syndicated television program, the plaintiff charged Winfrey with, among other things, tortiously interfering with his [\*42] "ability to enter into contracts or business relationships with third parties interested in purchasing the rights to publication of his experiences." *Id. at 324, 328*.

The district court dismissed the claim because the plaintiff "did not name any particular third party with whom he had a reasonable expectation of a business relationship, or toward whom Winfrey directed her interfering actions." *Id. at 327-28*. The Seventh Circuit reversed, however, holding that [HN13](#)[] "the Federal Rules do not require that [a] complaint allege the specific third party or class of third parties with whom [the plaintiff] claims to have had a valid business expectancy." *Id. at 328*. As the court explained, "[a] [Rule 12\(b\)\(6\)](#) motion cannot be used to dismiss a complaint on the ground that it does not include information that [Rule 8](#) does not require it to contain." *Id.* See also [\*Kim v. Kim\*, 360 F. Supp. 2d 897, 905 \(N.D. Ill. 2005\)](#).

In this case, Plaintiff alleges that he "had a reasonable expectation of entering into a valid business relationship for the development [and sale] of [his] property." (Cmplt. P 74.) The Zale and KB Defendants [\*43] argue that this does not suffice to allege that Defendants "acted toward a third party," perhaps because Plaintiff incorrectly identifies the Village Defendants as those third parties. (Zale/KB Reply, at 5; Pl. Resp., at 10.) In fact, Plaintiff's claimed expectation of entering into a business relationship with persons interested in purchasing and developing his property is adequate to allege a claim for tortious interference with prospective economic advantage. (Cmplt. PP 74, 76 (alleging that Defendants "purposely and intentionally interfered with Plaintiff's business expectancy).) The Zale and KB Defendants' motion to dismiss Count VI is denied.

## V. Count VII

In Count VII, Plaintiff alleges that the Zale and KB Defendants aided and abetted the "impairment of Plaintiff's property rights." The Zale and KB Defendants urge the court to dismiss Count VII on the grounds that Illinois does not recognize a claim for malicious injury to property rights. (Zale/KB Mem., at 6 (citing *Shields Enterprises, Inc. v. First Chicago Corp.*, 1987 U.S. Dist. LEXIS 9378, No. 86 C 10213, 1987 WL 18356 (N.D. Ill. Oct. 7, 1987).) The plaintiff in *Shields Enterprises* sought to pursue a malicious injury [\*44] to property rights action, relying on two cases that only vaguely referred to such a tort: *Doremus v. Hennessy*, 176 Ill. 608, 52 N.E. 924 (1898), and *Robinson v. Lull*, 145 F. Supp. 134 (N.D. Ill. 1956). In *Doremus*, defendants, who performed services for the plaintiff's laundry business, conspired to put her out of business unless she raised her prices. Recognizing a cause of action in these circumstances, the court stated, in dicta, the following general principle of law:

Every man has a right, under the law, as between himself and others, to full freedom in disposing of his own labor or capital according to his own will, and any one who invades that right without lawful cause or justification commits a legal wrong; and, if followed by an injury caused in consequence thereof, the one whose right is thus invaded has a legal ground of action for such wrong.

176 Ill. at 615, 52 N.E. at 926.

In *Robinson*, defendants expelled plaintiff, a physician, from a local medical society on false charges, thereby destroying his practice. The court described the plaintiff's resulting complaint as "stating a cause of action in tort, [\*45] alleging an intentional and wrongful invasion of plaintiff's right to establish and conduct a lawful business." 145 F. Supp. at 138. The *Robinson* court noted, however, that the complaint was inartfully drafted and that the action was actually based on an alleged violation of the medical society's by-laws. *Id.* After reviewing these two cases, the *Shields Enterprises* court (which did not describe the facts of the cases before it) dismissed the plaintiff's malicious injury to property claim, explaining that "this Court cannot say with any certainty that the Illinois Supreme Court would find that a cause of action existed here based on an unclear 1956 federal district court case and on dicta expounded in 1898." 1987 U.S. Dist. LEXIS 9378, 1987 WL 18356, at \*4.

Plaintiff maintains that a number of other Illinois Appellate Courts have in fact recognized a cause of action for malicious injury to property. In Pendleton v. Time, Inc., 339 Ill. App. 188, 89 N.E.2d 435 (1st Dist. 1949), the plaintiff was an artist who painted the first portrait of Harry S. Truman before he became the President of the United States. After Truman became President, Time published a portrait [\*46] of Truman painted by artist Jay Wesley Jacobs, falsely characterizing the painting as the first portrait for which Truman had ever sat. Id. at 190-93. 89 N.E.2d at 436-37. The plaintiff sued Time, alleging that he "lost all benefit and advantage accruing to him by reason of his having made and executed the first portrait of said Harry S. Truman," and that he "was further made to appear as stating an untruth in his prior statements of and concerning his having made the first portrait of the said Harry S. Truman." Id. at 193, 89 N.E.2d at 437. The court found that the plaintiff had alleged a property right in the value attained in painting the "first" portrait of Truman, and that there must be a remedy afforded for the willful, malicious, and intentional injury to that property right. Id. at 194-95, 89 N.E.2d at 438.

Contrary to Plaintiff's suggestion, HN14[] Pendleton does not affirmatively recognize a claim for malicious injury to property. As with Doremus, Pendleton recognizes the general principle of law that every man has the right to dispose of his own labor or capital according to his own will. Nor is Plaintiff's [\*47] reliance on Renard v. Columbia Broad. Sys., Inc., 126 Ill. App. 3d 563, 467 N.E.2d 1090, 82 Ill. Dec. 17 (1st Dist. 1984), helpful; that case merely noted that the trial court had dismissed the plaintiff's cause of action for malicious injury to property rights, and on appeal addressed only the plaintiff's claim for libel. Id. at 566, 467 N.E.2d at 1093. In Nemanich v. Long Grove Country Club Estates, Inc., 119 Ill. App. 2d 169, 255 N.E.2d 466 (2d Dist. 1970), the court noted the case of Ammons v. Jet Credit Sales, Inc., 34 Ill. App. 2d 456, 181 N.E. 2d 601 (1st Dist. 1962), in which the court "expressed favor with a count based on malicious and wrongful impairment of property in that the plaintiff's employment was jeopardized and credit impaired as a result of the defendant's action [making a garnishment demand on the plaintiff's employer] but affirmed the trial court on the basis that the demand was void on its face and not actionable." Id. at 175-76, 255 N.E.2d at 469. The *Nemanich* court stated that "the tort of malicious and wrongful impairment of property, like any other tort, must be based on the commission of a civil [\*48] wrong," but dismissed the claim for failure to allege that the defendants had committed any such wrong. Id. at 176, 255 N.E.2d at 469.

The court does not believe that any of these cases supports Plaintiff's claim for malicious impairment of property rights, and has serious doubts as to the validity of any such claim under Illinois law. As the *Shields Enterprises* court noted, "one must go back over thirty years to find even the briefest mention of the issue in Illinois . . ." [1987 U.S. Dist. LEXIS 9378, 1987 WL 18356, at \\*4](#). Even assuming such a tort did exist, moreover, there is nothing to suggest that Defendants committed a civil wrong necessary to support the claim. The Zale and KB Defendants' motion to dismiss Count VII is granted.

## VI. Count VIII

The Zale and KB Defendants finally contend that Plaintiff has no cause of action for civil conspiracy because he cannot maintain any of his three underlying tort claims (restraint of trade under the Sherman Act, tortious interference with prospective economic advantage, or malicious injury to property rights). (Zale/KB Mem., at 6.) In light of the court's determination that Plaintiff has in fact stated a claim for tortious interference [[\\*49](#)] with prospective economic advantage, the Zale and KB Defendants' motion to dismiss Count VIII on this basis is denied.

The Village Defendants insist that the civil conspiracy claim against them must nonetheless be dismissed because they are immune from suit under the Illinois Tort Immunity Act, [745 ILCS 10/1-101 et seq. HN15](#)<sup>10</sup> The Tort Immunity Act is designed to "protect local public entities from liability arising out of the operations of government." [Mazin v. Chicago White Sox, Ltd., 358 Ill. App. 3d 856, 832 N.E.2d 827, 832, 295 Ill. Dec. 377 \(1st Dist. 2005\)](#). Under the Act, a public entity is not liable "for an injury caused by adopting or failing to adopt an enactment or by failing to enforce any law." [745 ILCS 10/2-103](#). In addition, a public entity

is not liable for an injury caused by the issuance, denial, suspension or revocation of, or by the failure or refusal to issue, deny, suspend or revoke, any permit, license, certificate, approval, order or similar authorization where the entity or its employee is authorized by enactment to determine whether or not such authorization should be issued, denied, suspended or revoked.

[745 ILCS 10/2-104](#). Public employees are similarly immune from [[\\*50](#)] liability for such actions under [§§ 2-205](#) and [2-206](#). [745 ILCS 10/2-205, 2-206](#).

The Village Defendants argue that Plaintiff's damages "are all an integral part of and arise out of the annexation of the Zale property," including the relocation of Savage Road. (Village Mem., at 6.) According to the Village Defendants, those acts "arise out of the issuance of an 'approval' within the meaning of [Section 2-104](#) and [Section 2-206](#) of the Act" -- i.e., the Village's approval of the annexation plan. (*Id.*; Village Reply, at 6.)<sup>10</sup> Plaintiff first responds that [HN16](#)<sup>10</sup> immunity under the Act constitutes an affirmative defense that cannot be disposed of on a motion to dismiss. (Pl. Resp., at 12.) Though this is generally true, "the exception occurs where . . . the allegations of the complaint itself set forth everything necessary to satisfy the affirmative defense . . ." [United States v. Lewis, 411 F.3d 838, 842 \(7th Cir. 2005\)](#).

[[\\*51](#)] Plaintiff next argues that nothing in the Tort Immunity Act covers the conduct or damages occasioned when "the Village Defendants agreed to allow a private developer, Zale, to unlawfully remove Savage Road." (Pl. Resp., at 12.) In Plaintiff's view, such an allegation does not amount to a claim of injury either by the "issuance" of any "permit, license, certificate, approval, order or similar authorization," or by "the adoption of, or failure to adopt, an enactment." (*Id.*) The Illinois Supreme Court rejected a similar argument in [Village of Bloomingdale v. CDG Enterprises, Inc., 196 Ill. 2d 484, 752 N.E.2d 1090, 256 Ill. Dec. 848 \(2001\)](#). In that case, CDG Enterprises petitioned the Village of Bloomingdale to rezone property CDG had contracted to purchase. The Village denied the petition, allegedly to further its own plan to develop an adjacent parcel as a golf course. When the Village sued to recover for the services it rendered in reviewing CDG's petition, CDG counterclaimed, alleging tortious interference with business expectancy. [Id. at 485-86, 752 N.E.2d at 1093-94](#). Reversing dismissal of that claim, the appellate court characterized it as a challenge to the [[\\*52](#)] "corrupt misuse of the Village's power to steal away the expected

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<sup>10</sup> The Reply Memorandum of Village of Lindenhurst Defendants in Support of their Motion to Dismiss the Plaintiff's Amended Complaint is cited as "Village Reply, at \_\_\_. "

benefits of [CDG's] plans to develop the property." *Id.*, 752 N.E.2d at 1099. In other words, the "gravamen" of CDG's claim was the "Village's theft of [CDG's] opportunity." *Id.* The Illinois Supreme Court reversed that determination, however, noting that "the Village's denial of CDG's rezoning petition is precisely what the legislature intended to immunize such entities from." *Id.* The court was not persuaded by CDG's argument that "it really challenges the process by which the Village denied its petition, not the mere fact that it was denied." *Id.* As the court explained,

whether the Village denied the petition through an "abuse of official process and power," through "corrupt and malicious misuse of power," or for "corrupt or malicious motives," as CDG claims, is wholly immaterial to CDG's claim in tort . . . because [section 2-104](#) contains no reference to intent whatsoever and . . . it certainly does not contain an exception for "willful and wanton misconduct" or "corrupt or malicious motives."

[\*Id.\* at 495-96, 752 N.E.2d at 1099.](#)

In this case, the Village's [\*53] decision to approve the annexation agreement, including the relocation of Savage Road, is exactly the type of action the Tort Immunity Act is designed to protect. Plaintiff offers nothing to suggest that approving an annexation agreement is a ministerial, as opposed to discretionary task. Indeed, [HN17](#)[] the Act expressly extends immunity to injuries caused by the refusal to deny any approval or other similar authorization. [745 ILCS 10/2-104](#). See [Village of Bloomingdale, 196 Ill. 2d at 497, 752 N.E.2d at 1100](#) ("[section 2-104](#) plainly grants immunity for injury caused by the 'denial [of] any permit' and is, therefore, controlling.") (emphasis in original). See also [Kevin's Towing, Inc. v. Thomas, 351 Ill. App. 3d 540, 545, 814 N.E.2d 1003, 1008, 286 Ill. Dec. 777 \(2d Dist. 2004\)](#) (immunity does not require showing that the public authority acted in good faith). The Village Defendants' motion to dismiss Count VIII is granted.<sup>11</sup>

#### **[\*54] CONCLUSION**

For the reasons stated above, the Zale and KB Defendants' motion to dismiss (Docket No. 38) is granted with respect to Counts I, IV, V, and VII, but denied with respect to Counts VI and VIII. The Village Defendants' motion to dismiss Counts I, IV, and VIII (Docket No. 34) is granted.

ENTER:

REBECCA R. PALLMEYER

United States District Judge

Dated: September 16, 2005

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<sup>11</sup> Having determined that the Village Defendants are immune from liability under the Tort Immunity Act, the court need not address whether they are also entitled to legislative immunity. (Village Mem., at 7.) See [Biblia Abierta v. Banks, 129 F.3d 899, 903 \(7th Cir. 1997\)](#) ("The doctrine of absolute legislative immunity recognizes that when acting collectively to pursue a view of the public good through legislation, legislators must be free to represent their constituents 'without fear of outside interference' that would result in private lawsuits.")



## **Strawflower Elecs., Inc. v. Radioshack Corp.**

United States District Court for the Northern District of California

September 20, 2005, Decided ; September 20, 2005, Filed

No. C-05-0747 MMC

### **Reporter**

2005 U.S. Dist. LEXIS 45205 \*; 2005 WL 2290314

STRAWFLOWER ELECTRONICS, INC., Plaintiff, v. RADIOSHACK CORPORATION, Defendant.

**Prior History:** [\*1] (Docket No. 40).

[Strawflower Elecs., Inc. v. RadioShack Corp., 2005 U.S. Dist. LEXIS 49444 \(N.D. Cal., June 3, 2005\)](#)

## **Core Terms**

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products, alleges, motion to dismiss, antitrust claim, non-RadioShack-branded, trademark, fiduciary duty, parties, market power, tied product, argues, Sherman Act, buy, confidential relationship, declaratory judgment, claim for relief, antitrust, quotation, seller, anti trust law, termination, franchise, claim for breach, joint venture, Clayton Act, losses, buyer, fiduciary relationship, tying arrangement, cause of action

**Counsel:** For Strawflower Electronics Inc., Plaintiff: Jeffrey L. Fillerup, LEAD ATTORNEY, Luce Forward Hamilton & Scripps LLP, San Francisco, CA.

For RadioShack Corporation, Defendant: Paul D. Nelson, LEAD ATTORNEY, Duane Morris, LLP, San Francisco, CA, Ray L. Wong, LEAD ATTORNEY, Duane Morris LLP, San Francisco, Ca.

For RadioShack Corporation, Counter-claimant: Paul D. Nelson, LEAD ATTORNEY, Duane Morris, LLP, San Francisco, CA, Ray L. Wong, LEAD ATTORNEY, Duane Morris LLP, San Francisco, Ca.

For Strawflower Electronics Inc., Counter-defendant: Jeffrey L. Fillerup, LEAD ATTORNEY, Luce Forward Hamilton & Scripps LLP, San Francisco, CA.

**Judges:** MAXINE M. CHESNEY, United States District Judge.

**Opinion by:** MAXINE M. CHESNEY

## **Opinion**

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### **ORDER GRANTING IN PART AND DENYING IN PART DEFENDANT'S MOTION TO DISMISS; VACATING HEARING.**

Before the Court is defendant RadioShack Corporation's ("RadioShack") motion, filed August 18, 2005, to dismiss the second through sixth causes of action asserted against it in plaintiff Strawflower Electronics, Inc.'s ("Strawflower") Second Amended Complaint. Strawflower has filed opposition to the motion, to which RadioShack has replied. Having [\*2] considered the papers filed in support of and in opposition to the motion, the Court finds

the motion appropriate for resolution without oral argument, see [Civil L.R. 7-1\(b\)](#), and hereby VACATES the September 23, 2005 hearing on the matter. For the reasons set forth below, RadioShack's motion to dismiss is GRANTED in part and DENIED in part.

## BACKGROUND

Strawflower alleges that, in December 1979, it entered into a contract with RadioShack ("Contract"), by which RadioShack authorized Strawflower to sell RadioShack products and to use the RadioShack name in the operation of a retail store in Half Moon Bay, California. (See Second Amended Complaint ("SAC") 16.) According to Strawflower, it opened the Half Moon Bay store in December 1979, and used the RadioShack name and sold RadioShack products for approximately 25 years. (See *id.* 18.) Strawflower alleges that, pursuant to the Contract terms, RadioShack was permitted to terminate the Contract only if "(1) [Strawflower] fail[ed] to purchase from [RadioShack] a minimum of \$ 10,000 worth of merchandise, at [Strawflower]'s cost ... in any one year ... OR (2) [Strawflower] fail[ed] to reasonably serve [its] [\*3] market area with products reasonably expected to be carried by RADIO SHACK Authorized Sales Centers in locations of similar market size." ( See *id.* P 9.)

According to Strawflower, RadioShack, prior to and during 2004, sought to terminate the Contract by invoking both grounds for termination set forth in the Contract; Strawflower opposed termination, contending that it purchased in excess of \$ 10,000 worth of merchandise every year, and that it had "reasonably served" its market area. ( See *id.* P 10.) Strawflower alleges that when it asked RadioShack to explain the factual basis for its claim that cause existed to terminate the Contract, RadioShack refused to respond, provided inconsistent grounds for termination of the Contract, or provided grounds for termination that are not set forth in the Contract; thereafter, on or about January 17, 2005, RadioShack sent Strawflower a letter stating that RadioShack was terminating the Contract "for cause," effective February 17, 2005. ( See *id.* P 11.)

Strawflower further alleges that, within the past four years, RadioShack implemented a new policy that required Strawflower to buy non-RadioShack-branded products directly from RadioShack, [\*4] rather than from independent distributors. ( See *id.* P 40.) According to Strawflower, the policy required Strawflower to buy a certain percentage of both non-RadioShack-branded products and RadioShack-branded products from RadioShack, or face termination of the Contract. ( See *id.*) In implementing this policy, RadioShack, according to Strawflower, conditioned Strawflower's ability to buy and sell RadioShack-branded products, and Strawflower's right to use the RadioShack name, on Strawflower's buying non-RadioShack-branded products from RadioShack, instead of from independent distributors who sold the same products at lower cost. ( See *id.* P 46.) Strawflower contends this policy is harmful to competition and harmful to consumers because it precluded Strawflower from buying the non-RadioShack-branded products at the lowest price, and forced Strawflower to sell at higher prices to consumers. ( See *id.* P 48.)

Strawflower asserts seven causes of action against RadioShack: (1) breach of contract; (2) a claim for a declaratory judgment that RadioShack breached the Contract and that Strawflower did not breach the Contract; (3) a claim for a declaratory judgment that the Contract [\*5] created a franchise relationship between Strawflower and RadioShack, pursuant to the California Franchise Relations Act ("CFRA") ([California Business and Professions Act § 20000 et seq.](#)) and California Franchise Investment Law ("CFIL") ([California Corporations Code § 31000 et seq.](#)); (4) breach of fiduciary duty; (5) illegal tying in violation of § 3 of the Clayton Act ([15 U.S.C. § 14](#)) and § 1 of the Sherman Act ([15 U.S.C. § 1](#)); (6) illegal tying in violation of the Cartwright Act ([California Business and Professions Code § 16727 et seq.](#)); and (7) unfair competition in violation of [California Business and Professions Code § 17200](#).

RadioShack now moves to dismiss the second through sixth causes of action for failure to state a claim, pursuant to [Rule 12\(b\)\(6\) of the Federal Rules of Civil Procedure](#). RadioShack does not move to dismiss the first cause of action, for breach of contract, or the seventh cause of action, for unfair competition in violation of [§ 17200](#).

## LEGAL STANDARD

A motion to dismiss under [Rule 12\(b\)\(6\)](#) cannot be granted unless "it appears beyond doubt that the plaintiff can prove no set [\*6] of facts in support of his claim which would entitle him to relief." See [Conley v. Gibson, 355 U.S. 41, 45-46, 78 S. Ct. 99, 2 L. Ed. 2d 80 \(1957\)](#). Dismissal can be based on the lack of a cognizable legal theory or the absence of sufficient facts alleged under a cognizable legal theory. See [Balistreri v. Pacifica Police Dept., 901 F.2d 696, 699 \(9th Cir. 1990\)](#).

Generally, a district court, in ruling on a [Rule 12\(b\)\(6\)](#) motion, may not consider any material beyond the pleadings. See [Hal Roach Studios, Inc. v. Richard Feiner And Co., Inc., 896 F.2d 1542, 1555 n. 19 \(9th Cir. 1990\)](#). Material that is properly submitted as part of the complaint, however, may be considered. See *id.* Documents whose contents are alleged in the complaint, and whose authenticity no party questions, but which are not physically attached to the pleading, also may be considered. See [Branch v. Tunnell, 14 F.3d 449, 454 \(9th Cir. 1994\)](#). In addition, the Court may consider any document "the authenticity of which is not contested, and upon which the plaintiffs complaint necessarily relies," regardless of whether the document is referred to in the complaint. [\*7] See [Parrino v. FHP, Inc., 146 F.3d 699, 706 \(9th Cir. 1998\)](#). Finally, the Court may consider matters that are subject to judicial notice. See [Mack v. South Bay Beer Distributors, Inc., 798 F.2d 1279, 1282 \(9th Cir. 1986\)](#).

In analyzing a motion to dismiss, the Court must accept as true all material allegations in the complaint, and construe them in the light most favorable to the nonmoving party. See [NL Industries, Inc. v. Kaplan, 792 F.2d 896, 898 \(9th Cir. 1986\)](#). The Court may disregard factual allegations if such allegations are contradicted by the facts established by reference to exhibits attached to the complaint. See [Durning v. First Boston Corp., 815 F.2d 1265, 1267 \(9th Cir. 1987\)](#). Conclusory allegations, unsupported by the facts alleged, need not be accepted as true. See [Holden v. Hagopian, 978 F.2d 1115, 1121 \(9th Cir. 1992\)](#).

## DISCUSSION

### A. Breach of Fiduciary Duty

RadioShack argues that Strawflower's claim for breach of fiduciary duty is subject to dismissal because that there is no fiduciary relationship between the parties as a matter of law. Strawflower alleges that a [\*8] fiduciary relationship existed between it and RadioShack because they were "business partners and/or joint venturers," ( see SAC P 30), and because "RadioShack insisted, demanded and required that Strawflower provide RadioShack with confidential business information, which RadioShack claimed it would then use for the joint benefit of Strawflower and RadioShack." ( See *id.* P 31.)

#### 1. Business Partners

By statute, a fiduciary relationship exists among partners in a business partnership. See [Cal. Corp. Code § 16404](#). "A partnership is defined by statute ... as an association of two or more persons to carry on as co-owners a business for profit." See [Persson v. Smart Inventions, Inc., 125 Cal. App. 4th 1141, 1157, 23 Cal. Rptr. 3d 335 \(2005\)](#) (citing [Cal. Corp. Code § 16202\(a\)](#)) (emphasis added).

Defendants argue that the lack of a partnership is clear from the face of the Contract, which states that the RadioShack store at issue is owned and operated solely by Strawflower. As defendants note, the Contract expressly provides: "The management, operation and ownership of the store are acknowledged to be solely under the control of [Strawflower]." ( See Fillerup [\*9] Decl. in Support of Plaintiffs Motion For Leave to File Second Amended Complaint, Ex. A-1 ("Contract") § III.)<sup>1</sup> The Contract also identifies the store as "owned" by Strawflower,

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<sup>1</sup> Although the Second Amended Complaint states that the Contract is attached thereto, it is not attached to the copy of the Second Amended Complaint that was filed with the Court. It was, however, attached to the copy of the Second Amended

see *id.* § I.A), and further provides that Strawflower may not use the RadioShack trademark "unless it is clearly indicated that the store is owned and operated by [Strawflower]." ( See *id.* § I.D). Strawflower also agreed "not to do anything that would imply or indicate" that RadioShack "in any manner, either directly or indirectly owns, controls, [or] operates" Strawflower or its store. ( See *id.*) Although Strawflower correctly notes that the existence of a partnership is a question of fact, see, e.g., *Persson, 125 Cal. App. 4th at 1157*, Strawflower fails to allege or argue any facts that would support a finding that RadioShack is a co-owner of Strawflower's RadioShack store.

**[\*10]** Accordingly, the Court will GRANT defendants' motion to dismiss Strawflower's claim for breach of fiduciary duty to the extent it is based on fiduciary duties created by a partnership.

## 2. Joint Venture

A fiduciary relationship exists among parties to a joint venture. See *Oakland Raiders v. National Football League, 131 Cal. App. 4th 621, 632, 32 Cal. Rptr. 3d 266 (2005)*. "A joint venture, of necessity, 'requires an agreement under which the parties have (1) a joint interest in a common business, (2) an understanding that profits and losses will be shared, and (3) a right to joint control.'" See *id. at 637-38* (citing *Ramirez v. Long Beach Unified School Dist., 105 Cal. App. 4th 182, 193, 129 Cal. Rptr. 2d 128 (2002)*).

Defendants argue that Strawflower's claim for breach of fiduciary duty is subject to dismissal, to the extent it is based on duties created by a joint venture, because there is no allegation that the parties intended to share in the profits and losses incurred in the operation of Strawflower's RadioShack store, and no allegation that the parties intended to share control of the operation of the store. The Court need not reach the issue of control, as the **[\*11]** Contract does not provide for the sharing of profits and losses, and Strawflower neither alleges nor argues that the parties otherwise agreed to share profits and losses incurred in the operation of Strawflower's store. Rather, Strawflower argues that an agreement to share profits and losses is not a prerequisite to finding the existence of a joint venture. As noted above, however, the California Court of Appeal has held that "an understanding that profits and losses will be shared" is a requirement of a joint venture. See *id.*

Accordingly, the Court will GRANT defendants' motion to dismiss Strawflower's claim for breach of fiduciary duty to the extent it is based on fiduciary duties created by a joint venture.<sup>2</sup>

## **[\*12] 3. Confidential Relationship**

As noted, Strawflower also alleges that a fiduciary relationship was created between it and RadioShack because "RadioShack insisted, demanded and required that Strawflower provide RadioShack with confidential business information, which RadioShack claimed it would then use for the joint benefit of Strawflower and RadioShack." (See SAC 131.) Strawflower alleges that said confidential information included "customer information, sales information, and marketing information," which Strawflower states it would not have provided to RadioShack "but for the fiduciary duty that existed." (See *id.*) Strawflower alleges that RadioShack "used such confidential information for its

Complaint Strawflower submitted to the Court in connection with its motion for leave to file the Second Amended Complaint. In any event, the Court may consider the Contract in ruling on the instant motion to dismiss, regardless of whether it is attached to the Complaint. See *Branch v. Tunnell, 14 F.3d at 454*.

<sup>2</sup> Although Strawflower does not allege in its complaint that a fiduciary relationship arose as a result of a franchisor-franchisee relationship between RadioShack and Strawflower, the Court notes that Strawflower does suggest in its opposition that such a duty exists. (See Opp. at 22-23.) The Ninth Circuit repeatedly has held, however, that a fiduciary relationship is not created by a franchisor-franchisee relationship. See, e.g., *Boat & Motor Mart v. Sea Ray Boats, Inc., 825 F.2d 1285, 1292 (9th Cir. 1987)* (holding "[t]he relation between a franchisor and a franchisee is not that of a fiduciary to a beneficiary" and that "[t]he California Franchise Relations Act has not imposed additional fiduciary duties on the franchisor"); *Walker v. KFC Corp., 728 F.2d 1215, 1221 n.5 (9th Cir. 1984)* (holding California legislature, in enacting Franchise Investment Law, did not intend to impose fiduciary duty on franchisors).

own benefit and not for the joint benefit of RadioShack and Strawflower." (See *id.* P 32.) RadioShack argues that Strawflower's breach of fiduciary duty claim is subject to dismissal, to the extent it is based on a confidential relationship between the parties, because Strawflower has not alleged a relationship of the type that gives rise to a fiduciary duty.

"[O]ne standing in a confidential or fiduciary relationship with another is subject to liability to the other [\*13] for harm resulting from a breach of duty imposed by the relation." See *Richelle L. v. Roman Catholic Archbishop, 106 Cal. App. 4th 257, 273, 130 Cal. Rptr. 2d 601 (2003)* (internal quotation and citation omitted). The term "confidential relationship" refers to "an unequal partnership between parties in which one surrenders to the other some degree of control because of the trust and confidence he reposes in the other." See *id. at 272 n.6*. "A confidential relationship cannot be imposed on an individual, but must be voluntarily accepted" and "is not created simply by the receipt of confidential information." See *id.* The "essential elements" of a "confidential relation that gives rise to a fiduciary duty" are: "1) [t]he vulnerability of one party to the other which 2) results in the empowerment of the stronger party by the weaker which 3) empowerment has been solicited or accepted by the stronger party and 4) prevents the weaker party from effectively protecting itself." See *id. at 272* (internal quotation and citation omitted). "The vulnerability that is the necessary predicate of a confidential relation, and which the law treats as absolutely essential, [\*14] usually arises from advanced age, youth, lack of education, weakness of mind, grief, sickness or some other incapacity." *Id. at 273* (internal quotation and citation omitted).

In *Persson v. Smart Inventions, Inc.*, a case involving negotiations over the buyout of one 50% shareholder in a corporation by the other 50% shareholder, in which the selling party contended key information was withheld by the other party, the California Court of Appeal held that a confidential relationship giving rise to a fiduciary duty was not created "during arms-length business negotiations between the parties," finding the requisite "vulnerability" lacking in such relationship. See *Persson, 125 Cal. App. 4th at 1146, 1162*. Defendants argue that the instant transaction likewise was an arms-length business transaction in which no "confidential relationship" arose.

Strawflower does not allege any facts in its Second Amended Complaint to suggest that it suffered from the requisite "vulnerability." Moreover, in its opposition, Strawflower does not argue that it could amend the complaint to do so.

Accordingly, the Court will GRANT defendants' motion to dismiss Strawflower's [\*15] claim for breach of fiduciary duty to the extent it is based on fiduciary duties created by a confidential relationship. As Strawflower has failed to adequately allege any basis for a fiduciary relationship between the parties, Strawflower's claim for breach of fiduciary duty will be dismissed in its entirety.

## B. Antitrust Claims

RadioShack moves to dismiss Strawflower's claims for unlawful tying, brought under the Clayton Act, Sherman Act, and Cartwright Act (collectively, "antitrust claims"), on two separate grounds. First, RadioShack argues that the Court has already dismissed these claims with prejudice. Second, RadioShack argues that the antitrust claims, on their merits, fail to state a claim.

### 1. Prior Dismissal

In Strawflower's First Amended Complaint, it asserted causes of action under the Clayton Act, Sherman Act, and Cartwright Act, for unlawful tying. Although the claims were not clearly pleaded, Strawflower, in opposition to RadioShack's motion to dismiss the antitrust claims asserted in the First Amended Complaint, clarified that its antitrust claims were based on "an illegal tying arrangement in which RadioShack's sale of RadioShack branded products [\*16] is tied to Strawflower's continued use of the RadioShack name." (See Order Granting in Part and Denying in Part Motion to Dismiss, filed June 3, 2005, at 5.) The Court granted RadioShack's motion to dismiss the antitrust claims, with prejudice, holding that, under the facts alleged, the RadioShack trademark could not be considered a separate product for purposes of a tying claim. (See *id.* at 6-7.)

In its Second Amended Complaint, Strawflower asserts a new theory in support of its antitrust claims.<sup>3</sup> Rather than contending that RadioShack violated the antitrust laws by tying the sale of RadioShack-branded products to the use of the RadioShack name, Strawflower now contends that RadioShack violated the antitrust laws by (1) tying Strawflower's purchase of RadioShack-branded products to Strawflower's purchase of non-RadioShack-branded products; and (2) tying Strawflower's use of the RadioShack name to the sale of non-RadioShack-branded products. (See SAC PP 49-50.)

[\*17] The Court previously dismissed Strawflower's antitrust claims, with prejudice, based on the theory then asserted. As Strawflower now asserts a new theory in support of its antitrust claims, the Court's prior dismissal does not preclude Strawflower from asserting its antitrust claims, as currently pleaded.

## 2. Tying - Legal Standard

The Supreme Court has held, with respect to the definition of tying, that "the standards used by the [Sherman Act and Clayton Act] are the same." See [\*Jefferson Parish Hospital District No. 2 v. Hyde\*, 466 U.S. 2, 23 n.39, 104 S. Ct. 1551, 80 L. Ed. 2d 2 \(1984\)](#). Federal decisions interpreting the Sherman Act and Clayton Act with respect to tying likewise are applicable to tying claims brought under the California Cartwright Act, as the sections of the Cartwright Act addressing tying were modeled after the Sherman and Clayton Acts. See [\*Hamro v. Shell Oil Co.\*, 674 F.2d 784, 786 \(9th Cir. 1982\)](#). Accordingly, and because the parties treat the antitrust claims interchangeably, the Court will analyze together all three antitrust claims asserted by Strawflower.

"A tying arrangement is an agreement by a party to sell one product but only [\*18] on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any other supplier." [\*Eastman Kodak Co. v. Image Technical Services, Inc.\*, 504 U.S. 451, 461, 112 S. Ct. 2072, 119 L. Ed. 2d 265 \(1992\)](#) (internal quotation and citation omitted). The Supreme Court has held that "[s]uch an arrangement violates [§ 1 of the Sherman Act](#) if the seller has appreciable economic power in the tying market and if the arrangement affects a substantial volume of commerce in the tied market." See *id.* "The essential characteristic of an invalid tying arrangement lies in the seller's exploitation of its control over the tying product to force the buyer into the purchase of a tied product that the buyer either did not want at all, or might have preferred to purchase elsewhere on different terms." [\*Id. at 464 n.9\*](#) (internal quotation and citation omitted). "When such 'forcing' is present, competition on the merits in the market for the tied item is restrained and the Sherman Act is violated." *Id.*; see also [\*Paladin Associates, Inc. v. Montana Power Co.\*, 328 F.3d 1145, 1159 \(9th Cir. 2003\)](#) (holding [\*19] elements of tying claim are: "(1) that there exist two distinct products or services in different markets whose sales are tied together; (2) that the seller possesses appreciable economic power in the tying product market sufficient to coerce acceptance of the tied market; and (3) that the tying arrangement affects a not insubstantial volume of commerce in the tied product market") (internal quotation and citation omitted).

## 3. Separate Products

As noted, Strawflower alleges that RadioShack engaged in unlawful tying by conditioning Strawflower's ability to purchase RadioShack-branded products and to use the RadioShack trademark (the tying products) on its purchase of non-RadioShack-branded products from RadioShack (the tied products).<sup>4</sup> (See SAC PP 49-50.)

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<sup>3</sup>Contrary to RadioShack's argument, the doctrine of res judicata is inapplicable, particularly in light of the Court's order of July 26, 2005, granting Strawflower leave to amend.

<sup>4</sup>Strawflower defines the term "RadioShack-branded product" to mean "a product with a label and packaging bearing the name 'RadioShack.'" (See SAC P 37.) By contrast, a "non-RadioShack-branded product" is "a product not produced by RadioShack and bearing some name other than RadioShack on the label and packaging, for instance, Hewlett-Packard, Lexmark, or Eveready." (See *id.*)

[\*20] RadioShack's first argument in support of dismissal is that Strawflower's new allegations, as a legal matter, fare no better than those previously dismissed by the Court. Strawflower previously argued that RadioShack unlawfully tied the use of its trademark to Strawflower's sale of RadioShack-branded products; in other words, that RadioShack permitted Strawflower to use the RadioShack name only if Strawflower sold certain RadioShack products. The Court dismissed Strawflower's antitrust claims, as based on that theory, because the Ninth Circuit has held that, under such circumstances, a trademark may not be considered a separate product for purposes of a tying claim.

As discussed in this Court's previous order of dismissal, the Ninth Circuit, in *Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348 (9th Cir. 1982)*, rejected the plaintiff's argument therein that Baskin-Robbins' policy of conditioning the grant of a franchise upon the purchase of ice cream exclusively from Baskin-Robbins constituted an unlawful tying of the Baskin-Robbins trademark to the ice cream products the plaintiff was compelled to purchase, in violation of the Sherman Act. See *id. at 1352-54*. [\*21] The Ninth Circuit held that in "a distribution type" franchise, such as that employed by Baskin-Robbins, "the franchised outlets serve merely as conduits through which the trademarked goods of the franchisor flow to the ultimate consumer" and the trademark in a distribution franchise "serves merely as a representation of the end product marketed by the system." See *id. at 1353-54*. As the Ninth Circuit observed, "[b]ecause the prohibition of tying arrangements is designed to strike solely at the use of a dominant desired product to compel the purchase of a second undesired commodity," there can be no claim for unlawful tying "where the trademark serves only to identify the allegedly tied product." See *id. at 1354*; see also *Hamro v. Shell Oil Co., 674 F.2d at 786-87* (rejecting plaintiffs claim that Shell engaged in unlawful tying in violation of Cartwright Act by authorizing plaintiff to use Shell's trademark at his service station only if he purchased Shell gasoline; holding "as a matter of law the Shell trademark and Shell gasoline are not separate and distinct products"). Consequently, this Court found that any requirement that [\*22] Strawflower purchase RadioShack-branded products in order to use the RadioShack trademark fell squarely within the holdings of *Krehl* and *Hamro* and did not state a claim for unlawful tying in violation of the antitrust laws. (See Order Granting in Part and Denying in Part Motion to Dismiss, filed June 3, 2005, at 5-8.)

In the instant complaint, Strawflower alleges that RadioShack is tying Strawflower's ability to sell RadioShack-branded products and its use of the RadioShack trademark to the purchase of non-RadioShack-branded products from RadioShack. (See SAC PP 49-50.) Contrary to RadioShack's argument, these allegations differ materially from the allegations in the First Amended Complaint. First, Strawflower's current allegation that RadioShack conditioned Strawflower's access to RadioShack-branded products on its purchase of non-RadioShack-branded products raises a classic tying claim. See *Eastman Kodak, 504 U.S. at 461* (defining "tying arrangement" as "an agreement by one party to sell one product only on the condition that the buyer also purchases a different (or tied) product, or at least agrees that he will not purchase that product from any [\*23] other supplier"). Additionally, as currently pleaded, the RadioShack trademark is not being used to identify the allegedly tied product and, consequently, the trademark may be considered to be a separate product for purposes of a tying claim. See *Krehl, 664 F.2d at 1352* (noting that "under certain circumstances, a trademark may be sufficiently unrelated to the alleged tied product to warrant treatment as a separate item"); see also *Siegel v. Chicken Delight, Inc., 448 F.2d 43 (9th Cir. 1971)* (finding unlawful tying in violation of Sherman Act where chicken franchise conditioned use of trademark on purchase of cooking equipment, packaging supplies, and mixes that were not manufactured by franchisor).<sup>5</sup>

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<sup>5</sup> Because the RadioShack trademark cannot be said to identify products sold in RadioShack stores "bearing some name other than RadioShack on the label and packaging, for instance, Hewlett-Packard, Lexmark, or Eveready," ( see *id.*), the instant case is distinguishable from cases cited by RadioShack in which the product at issue was manufactured by a third party, but sold under the defendant's trademark, not under the trademark of the manufacturer. See, e.g., *Krehl, 664 F.2d at 1354 n.14* (ice cream sold under Baskin-Robbins trademark but not manufactured by Baskin-Robbins); *Power Test Petroleum Distributors, Inc. v. Calcu Gas, 754 F.2d 91, 98 (2nd Cir. 1985)* (gasoline sold under PowerTest trademark but not manufactured by PowerTest); *Jack Walters & Sons Corp. v. Morton Building, Inc., 737 F.2d 698, 704 (7th Cir. 1984)* (prefabricated building sold under Morton trademark although all components not manufactured by Morton).

[\*24] Accordingly, the Court rejects RadioShack's argument that the legal issues presented by Strawflower's current allegations are indistinguishable as a legal matter from those presented by the allegations in its prior complaint.

#### 4. Purchase of Allegedly Tied Products

RadioShack further argues that the antitrust claims are subject to dismissal because Strawflower fails to allege that it purchased any of the allegedly tied products. Strawflower alleges that during the first twenty years after the Contract was executed, it purchased non-RadioShack-branded products only from independent distributors. (See SAC 139.) Thereafter, Strawflower alleges, RadioShack implemented a policy requiring Strawflower to buy non-RadioShack-branded products only from RadioShack. (See *id.* P 40.) Strawflower alleges that RadioShack terminated the Contract "based upon RadioShack's claim that Strawflower has not complied with the policy." (See *id.* P 47.) As RadioShack points out, Strawflower does not allege that it, in fact, purchased any non-RadioShack-branded products from RadioShack.

The Ninth Circuit has stated that an "essential" element of a tying claim is "proof that the seller [\*25] coerced a buyer to purchase the tied product." See *Paladin Associates v. Montana Power Co.*, 328 F.3d at 1159 (emphasis in original). In *Paladin*, the Ninth Circuit further noted that "mere sales pressure" does not constitute evidence of the requisite coercion. See *id. at 1160*. Because *Paladin* did not involve a plaintiff who refused to purchase the tied product, the Ninth Circuit did not address whether evidence of acts that could be described as attempted coercion were sufficient to state a tying claim. Other circuits, however, have held that no tying claim can be stated where the plaintiff refused to purchase the tied product. See, e.g., *Famous Brands, Inc. v. David Sherman Corp.*, 814 F.2d 517, 523 (8th Cir. 1987) (citing *Unijax, Inc. v. Champion Int'l, Inc.*, 683 F.2d 678, 685 (2nd Cir. 1982)) ("Actual coercion by the seller that in fact forces the buyer to purchase the tied product is an indispensable element of a tying violation.")). Additionally, a leading antitrust treatise concurs that "an express tying contract that is proposed to buyers but rejected by them does not constitute a tie" and that "the [\*26] mere termination or rejection of a dealer or customer who refuses to comply with a tie" is not unlawful tying. See Areeda, Elhauge, and Hovenkamp, *Antitrust Law*, §§ 1753a, 1753f (2d ed. 2004).

In its opposition, Strawflower states that it did purchase non-RadioShack-brand products from RadioShack, although it did not purchase enough of the products to satisfy RadioShack. (See Opp. at 11; see also Fillerup Decl. Ex. A (Mackintosh Decl. P 11.) In reply, RadioShack argues that Strawflower's purchase of some non-RadioShack products from RadioShack is not sufficient to support an antitrust claim if Strawflower did not purchase the percentage of such products required by RadioShack. This argument was not addressed in RadioShack's opening brief, however, and Strawflower has not had an opportunity to respond to it.

Accordingly, the Court will GRANT RadioShack's motion to dismiss Strawflower's antitrust claims, for failure to allege actual purchase, but will afford Strawflower leave to amend its antitrust claims to allege that it purchased non-RadioShack-branded products from RadioShack. Thereafter, if RadioShack still wishes to move to dismiss based on the argument raised [\*27] in its reply, it may do so.

#### 5. Market Power

As an additional ground for dismissal of the antitrust claims, RadioShack argues that Strawflower has failed to adequately allege that RadioShack possesses the requisite market power with respect to any of the alleged tying products. As noted, Strawflower alleges the tying products are RadioShack-branded products and the RadioShack trademark. (See SAC PP 49-50.)

The Ninth Circuit has held that an essential element of a tying claim is "that the seller possesses appreciable economic power in the tying product market sufficient to coerce acceptance of the tied market." See *Paladin Associates, Inc. v. Montana Power Co.*, 328 F.3d at 1159. "Market power is the power to force a purchaser to do something that he would not do in a competitive market." See *Eastman Kodak*, 504 U.S. at 464 (internal quotation

and citation omitted). "The existence of such power ordinarily is inferred from the seller's possession of a predominant share of the market." See *id.*

Strawflower does not allege that RadioShack has a predominant share of the market for any of the products alleged to be RadioShack-branded products, [\*28] including "batteries, ionizers, power supplies, toys, and massagers." See SAC P 49.) Rather, Strawflower alleges it "spent the past 25 years and substantial time and money in developing the RadioShack name and the market for RadioShack products," that this investment "locked Strawflower into a relationship with RadioShack," and that "RadioShack took advantage of Strawflower's locked-in position" by initiating a new policy requiring Strawflower to purchase non-RadioShack-branded products only from RadioShack. ( See SAC P 51.)

Plaintiffs rely on *Eastman Kodak*, in which the Supreme Court addressed this "lock-in" theory of market power. In *Eastman Kodak*, the issue was whether Eastman Kodak had unlawfully tied the sale of service for Kodak copying machines to the sale of parts for such machines. See [\*id. at 459\*](#). Eastman Kodak argued that because it lacked market power in the market for the machines themselves, it could not be found to have market power in the "aftermarket" for service and parts for the machines, as a matter of law. See [\*id. at 456\*](#). The Supreme Court rejected the argument. The Supreme Court first noted that plaintiffs had submitted [\*29] evidence that Kodak did in fact have market power in the parts market. See [\*id. at 464-65\*](#). Consequently, the Supreme Court held, Kodak could not demonstrate it was entitled to summary judgment unless it showed that despite such evidence, "an inference of market power [was] unreasonable." See [\*id. at 469\*](#). The Supreme Court observed that Kodak's theory, "that lack of power in the equipment market necessarily precludes power in the aftermarket," rested on the assumption that if Kodak raised its prices for parts and service above competitive levels, customers would stop buying Kodak equipment. See [\*id. at 469-70\*](#). The Supreme Court found, however, that "[i]f the cost of switching is high, consumers who already have purchased the equipment, and thus are 'locked in,' will tolerate some level of service-price increases before changing equipment brands" and, consequently, "a seller profitably could maintain supracompetitive prices in the aftermarket if the switching costs were high relative to the increase in service prices, and the number of locked-in customers were high relative to the number of new purchasers." See [\*id. at 475\*](#). [\*30] Because the plaintiffs presented evidence that switching costs for Kodak equipment owners were very high, the Supreme Court concluded "a question of fact" existed as to "whether information costs and switching costs foil the simple assumption that the equipment and service markets act as pure complements to each other." See [\*id. at 477\*](#). *Eastman Kodak* thus suggests that a plaintiff may prove market power by showing such plaintiff was economically "locked in" to a business relationship with the defendant. See also *Subsolutions, Inc. v. Doctor's Associates, Inc.*, [\*62 F. Supp. 2d 616, 625-26 \(D. Conn. 1999\)\*](#) (holding plaintiff adequately alleged market power by reference to *Eastman Kodak* lock-in theory).

In relying on the *Eastman Kodak* "lock-in" theory to prove the defendant has the requisite market power, a plaintiff still must allege, however, that the challenged activity affected a substantial portion of the relevant market. See *Universal Avionics Systems Corp. v. Rockwell Int'l Corp.*, [\*184 F. Supp. 2d 947, 955 \(D. Ariz. 2001\)\*](#) (holding challenged conduct must affect "substantial number of customers"); see also Areeda, [\*31] Elhauge and Hovenkamp, *Antitrust Law*, § 1740a (2d ed. 2004) (same). In *Eastman Kodak*, the challenged conduct affected all customers who owned Kodak photocopiers and all independent servicing organizations who serviced Kodak photocopiers; in *Subsolutions*, the challenged conduct affected all Subway franchisees. See *Eastman Kodak*, [\*504 U.S. at 458, 477\*](#); see *Subsolutions*, [\*62 F. Supp. 2d at 620\*](#). Here, by contrast, Strawflower does not allege that the challenged RadioShack policy applied to all RadioShack stores, but, rather, alleges that "RadioShack implemented a policy that required Strawflower to buy non-RadioShack-branded products directly from RadioShack." (See SAC 140 (emphasis added).)

Accordingly, the Court will GRANT RadioShack's motion to dismiss Strawflower's antitrust claims, for failure to adequately allege market power. The Court will, however, afford Strawflower leave to amend.

## 6. Antitrust Injury

RadioShack's final argument in support of dismissal of the antitrust claims is that Strawflower lacks standing to assert such claims because it has failed to allege that it suffered antitrust injury.

A suit for violation [**\*32**] of the Clayton Act or the Sherman Act may be brought by "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws[]." See [15 U.S.C. § 15](#).<sup>6</sup> A plaintiff, however, "must prove the existence of *antitrust* injury, which is to say injury of the type the antitrust laws were intended to prevent and that flows from that which makes defendants' acts unlawful." See [Atlantic Richfield Co. v. USA Petroleum Co., 495 U.S. 328, 334, 110 S. Ct. 1884, 109 L. Ed. 2d 333 \(1990\)](#) (internal quotation and citation omitted; emphasis in original). "[I]njury, although causally related to an antitrust violation, nevertheless will not qualify as 'antitrust injury' unless it is attributable to an anti-competitive aspect of the practice under scrutiny, since it is inimical to the antitrust laws to award damages for losses stemming from continued competition." *Id.* (internal quotations and citations omitted). "Where the defendant's conduct harms the plaintiff without adversely affecting competition generally, there is no antitrust injury." See [Paladin, 328 F.3d at 1158](#).

[**\*33**] Here, Strawflower expressly alleges that RadioShack's requirement that Strawflower purchase non-RadioShack-branded products only from RadioShack harmed competition because, according to Strawflower, "it precluded Strawflower from buying non-RadioShack-branded products at lower prices and on better terms from sellers other than RadioShack, and it forced Strawflower to sell at higher prices to consumers." (See SAC P 48.) RadioShack argues that Strawflower nonetheless cannot show it suffered antitrust injury because it has not alleged that it was coerced into buying undesired products from RadioShack. As noted above, Strawflower states in its opposition that it did purchase such products from RadioShack, and the Court will afford Strawflower leave to amend the complaint to so allege.

Accordingly, the Court will GRANT RadioShack's motion to dismiss Strawflower's antitrust claims, for failure to allege antitrust injury, with leave to amend.

### C. Declaratory Relief Claims

RadioShack moves to dismiss or strike both of Strawflower's claims for declaratory relief on the ground that such claims are duplicative of Strawflower's other claims.

By statute, the Court "may," but is [**\*34**] not required to, "declare the rights and other legal relations of any interested party seeking such declaration, whether or not further relief is or could be sought." See [28 U.S.C. § 2201\(a\)](#); see also [Wilton v. Seven Falls Co., 515 U.S. 277, 282, 115 S. Ct. 2137, 132 L. Ed. 2d 214 \(1995\)](#) (noting courts' discretion to entertain claim for declaratory judgment). [Rule 57 of the Federal Rules of Civil Procedure](#) provides that "[t]he existence of another adequate remedy does not preclude a judgment for declaratory relief in cases where it is appropriate." See [Fed. R. Civ. Proc. 57](#). The Supreme Court has held, however, that a court has the discretion to dismiss a claim for declaratory relief if "a declaratory judgment would serve no useful purpose." See [Wilton, 515 U.S. at 288](#).

#### 1. Second Claim For Relief

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<sup>6</sup>The Cartwright Act similarly confers standing on "any person who is injured in his or her business or property by reason of anything forbidden or declared unlawful by [the Cartwright Act], regardless whether such injured person deals directly or indirectly with the defendant." See [In re Napster, Inc. Copyright Litigation, 354 F. Supp. 2d 1113, 1125 \(N.D. Cal. 2005\)](#) (citing, [Cal. Bus. & Prof. Code § 16750\(a\)](#).) As Strawflower correctly notes, the definition of "antitrust injury" under California law is less restrictive than the federal standard, in that California law expressly confers antitrust standing on persons who are injured indirectly by the defendant's anticompetitive conduct. See *id.* As Strawflower alleges that it was injured directly by RadioShack, however, the difference appears immaterial for purposes of the instant motion, and no party argues to the contrary.

Strawflower seeks, in its second claim for relief, a judgment declaring that RadioShack breached the Contract, declaring that Strawflower did not breach the Contract, and declaring any further relief arising out of the Contract that is "necessary, just and/or proper." (See SAC P 18.) This claim, as defendants correctly note, [\*35] is entirely duplicative of Strawflower's cause of action for breach of contract. As a separate claim for a declaratory judgment on the issue serves "no useful purpose" in the instant litigation, the Court will GRANT defendants' motion to dismiss the second claim for relief.

## **2. Third Claim For Relief**

Strawflower seeks, in its third claim for relief, a declaratory judgment that the parties had a franchisor-franchisee relationship within the meaning of the CFIL and CFRA and that, consequently, RadioShack was subject to all the duties and obligations of a franchisor under those statutes. (See SAC P 27.) Strawflower further alleges that RadioShack "failed to comply with a franchisor's obligations in connection with termination of a franchise." (See *id.* P 25.)

RadioShack argues that the third claim for relief should be dismissed as duplicative of Strawflower's claim for unfair competition in violation of [§ 17200](#). Strawflower alleges that RadioShack engaged in unfair competition in violation of [§ 17200](#) by violating the CFIL and CFRA, as well as by violating the Clayton Act, Sherman Act, and the Cartwright Act. (See *id.* PP 58-59.) Because Strawflower has alleged multiple [\*36] bases for liability under [§ 17200](#), it is conceivable the Court could find that RadioShack engaged in unfair competition without reaching the merits of Strawflower's claim under the CFIL and CFRA. Consequently, Strawflower's claim for a declaratory judgment that the parties had a franchisor-franchisee relationship within the meaning of the CFIL and CFRA and that, consequently, RadioShack was subject to all the duties and obligations of a franchisor under those statutes, ( see SAC P 27), is not necessarily duplicative of Strawflower's [§ 17200](#) claim.

Accordingly, the Court will DENY RadioShack's motion to dismiss the third claim for relief.

## **CONCLUSION**

For the reasons set forth above, RadioShack's motion to dismiss is hereby GRANTED in part and DENIED in part, as follows:

1. The motion to dismiss Strawflower's claim for breach of fiduciary duty is GRANTED, and said claim is DISMISSED with prejudice.
2. The motion to dismiss Strawflower's antitrust claims is GRANTED, with leave to amend.
3. The motion to dismiss Strawflower's second claim for relief, for a declaratory judgment, is GRANTED.
4. The motion to dismiss Strawflower's third claim for relief, for a declaratory [\*37] judgment, is DENIED.
5. Strawflower may file a Third Amended Complaint within 21 days of the date of this order. If Strawflower fails to timely file a Third Amended Complaint, all claims that have been dismissed with leave to amend will be dismissed with prejudice.

This order terminates Docket No. 40.

## **IT IS SO ORDERED.**

Dated: September 20, 2005

MAXINE M. CHESNEY

United States District Judge

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## **Flying Eagle Espresso, Inc. v. Host Int'l, Inc.**

United States District Court for the Western District of Washington

September 21, 2005, Decided ; September 22, 2005, Filed

NO. C04-1551P

### **Reporter**

2005 U.S. Dist. LEXIS 37679 \*; 2005 WL 2318827

FLYING EAGLE ESPRESSO, INC., Plaintiff(s), v. HOST INTERNATIONAL INC., et al., Defendant(s).

**Prior History:** [Flying Eagle Espresso, Inc. v. Host Int'l Inc., 2005 U.S. Dist. LEXIS 54837 \(W.D. Wash., Jan. 19, 2005\)](#)

## **Core Terms**

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summary judgment, cause of action, unionization, lease, concessionaires, airport, violations, renewal, allegations, anti-trust, Harmony, material fact, negotiating, state actor, conspiracy, employees, sublease, parties, courts, civil conspiracy, produce evidence, exemption, accomplish, regulated, coercion, rights, solicitation, sublessees, disputed, communications

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

### **HN1** [] **Entitlement as Matter of Law, Appropriateness**

Summary judgment is not warranted if a material issue of fact exists for trial.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

### **HN2** [] **Entitlement as Matter of Law, Appropriateness**

On a motion for summary judgment, the underlying facts are viewed in the light most favorable to the party opposing the motion.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > Appropriateness

### **HN3** [] **Entitlement as Matter of Law, Appropriateness**

Summary judgment will not lie if the evidence is such that a reasonable jury could return a verdict for the nonmoving party.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Absence of Essential Element

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Movant Persuasion & Proof

#### **HN4** **Burdens of Proof, Absence of Essential Element**

A party moving for summary judgment has the burden to show initially the absence of a genuine issue concerning any material fact. This can be done by either producing evidence negating an essential element of plaintiff's claim or by showing that plaintiff does not have enough evidence of an essential element to carry its ultimate burden at trial.

Civil Procedure > ... > Summary Judgment > Burdens of Proof > Nonmovant Persuasion & Proof

#### **HN5** **Burdens of Proof, Nonmovant Persuasion & Proof**

On a motion for summary judgment, once the moving party has met its initial burden, the burden shifts to the nonmoving party to establish the existence of an issue of fact regarding an element essential to that party's case, and on which that party will bear the burden of proof at trial. To discharge this burden, the nonmoving party cannot rely on its pleadings, but instead must have evidence showing that there is a genuine issue for trial.

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

#### **HN6** **Summary Judgment, Entitlement as Matter of Law**

At the summary judgment stage, the judge's function is not to weigh the evidence but to determine whether there is a genuine issue for trial.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

Governments > Legislation > Interpretation

#### **HN7** **Deceptive & Unfair Trade Practices, State Regulation**

In interpreting the Washington Consumer Protection Act, state courts are to look to federal precedent for guidance, but it is not controlling.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

Governments > Legislation > Interpretation

#### **HN8** **Deceptive & Unfair Trade Practices, State Regulation**

The directive to be "guided by" federal law in interpreting the Washington Consumer Protection Act does not mean that state courts are bound to follow it. But neither are state courts free to ignore it, and indeed in practice Washington courts have uniformly followed federal precedent in matters described under the Consumer Protection

Act. Any departure from federal law must be for a reason rooted in Washington statutes or case law and not in the general policy arguments a court would weigh if the issue came before it as a matter of first impression.

Civil Procedure > Preliminary Considerations > Federal & State Interrelationships > Erie Doctrine

#### **HN9** **Federal & State Interrelationships, Erie Doctrine**

When interpreting state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Governments > Legislation > Interpretation

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

#### **HN10** **Exemptions & Immunities, Parker State Action Doctrine**

The Washington Consumer Protection Act is patterned after federal law, and [Wash. Rev. Code § 19.86.920](#) anticipates that state courts will be guided by federal court interpretation of federal [antitrust law](#). [Section 19.86.920](#) also commands that the regulatory scheme be liberally construed that its beneficial purposes may be served. However, this admonition does not mean that state courts are bound to follow federal law. A departure from following the federal precedent of the state actor immunity doctrine must have a firm foundation in state authority.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > General Overview

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

#### **HN11** **Exemptions & Immunities, Parker State Action Doctrine**

[Wash. Rev. Code § 19.86.170](#) states that the provisions of the Washington Consumer Protection Act, including its anti-trust provisions, do not apply to actions or transactions permitted by any other regulatory body or officer acting under statutory authority of the state.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

Governments > Legislation > Interpretation

#### **HN12** **Exemptions & Immunities, Parker State Action Doctrine**

In delineating the application of [Wash. Rev. Code § 19.86.170](#), Washington courts have taken the approach that "liberal construction" is a command that the coverage of an act's provisions in fact be liberally construed and that its exceptions be narrowly confined. As a result, Washington courts have carefully scrutinized both the "action or transaction" involved and the permission required to qualify for exemption under in [§ 19.86.170](#).

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

### [\*\*HN13\*\*](#) [blue icon] Exemptions & Immunities, Parker State Action Doctrine

The Washington Supreme Court has articulated a narrow interpretation of the phrase "action or transaction" in [Wash. Rev. Code § 19.86.170](#) such that a generally regulated practice does not automatically receive exemption from claims under the Washington Consumer Protection Act. If a particular practice found to be unfair or deceptive is not regulated, even though the business is regulated generally, it would appear to be the legislative intent that the provisions of the act should apply.

Antitrust & Trade Law > Exemptions & Immunities > Parker State Action Doctrine > Scope

### [\*\*HN14\*\*](#) [blue icon] Exemptions & Immunities, Parker State Action Doctrine

Washington courts making an "exemption" analysis under [Wash. Rev. Code § 19.86.170](#) have closely analyzed the activity at issue for specific permission and narrowly construed that permission in order to avoid conflict with the "liberal construction" intent of the Washington legislature. As a result, "permission" necessitates overt affirmative action to permit the activity by the entity involved in the complaint. Washington takes a very limited approach to its application of the exemption for activities permitted by most agencies.

Transportation Law > Air & Space Transportation > Airports > General Overview

### [\*\*HN15\*\*](#) [blue icon] Air & Space Transportation, Airports

[Wash. Rev. Code § 14.08.120](#) permits a municipality to confer the privileges of concession of supplying upon its airports goods, commodities, things, services and facilities, [§ 14.08.120\(4\)](#), and to sell or lease any property, real or personal, acquired for airport purposes and belonging to the municipality, which, in the judgment of its governing body, may not be required for aircraft landings, aircraft takeoffs, or related aeronautic purposes, in accordance with the laws of the state, [§ 14.08.120\(5\)](#).

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > Monopoly Power

### [\*\*HN16\*\*](#) [blue icon] Actual Monopolization, Monopoly Power

An anti-trust plaintiff has the burden to prove possession of monopoly power in a relevant market.

Antitrust & Trade Law > Regulated Practices > Private Actions > Sherman Act

### [\*\*HN17\*\*](#) [blue icon] Private Actions, Sherman Act

To establish an anti-trust claim, it is not enough to claim that the plaintiff's own operations were injured; the antitrust laws were enacted for the protection of competition, not competitors.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

### [\*\*HN18\*\*](#) [blue icon] Deceptive & Unfair Trade Practices, State Regulation

To prevail in a private action under the Washington Consumer Protection Act, a plaintiff must establish five distinct elements: (1) an unfair or deceptive act or practice; (2) occurring in trade or commerce; (3) public interest impact; (4) injury to plaintiff in his or her business or property; and (5) causation. The plaintiff must satisfy all five elements in order to prevail; in the summary judgment context, a plaintiff has the burden to establish, at a minimum, the existence of disputed issues of material fact regarding each of the elements of its cause of action.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

#### **HN19** [L] **Deceptive & Unfair Trade Practices, State Regulation**

Ordinarily, a breach of a private contract affecting no one but the parties to the contract is not an act or practice affecting the public interest for purposes of the Washington Consumer Protection Act. A complainant can refashion a private dispute into one with an impact on the public by: (1) a "per se" showing of the violation of a statute with a specific legislative declaration of public interest; or (2) a showing that additional plaintiffs have been or will be impacted in a similar manner. The factors that need to be proven in this regard include: (1) were the alleged acts committed in the course of defendant's business? (2) did defendant advertise to the public in general? (3) did defendant actively solicit the plaintiff, indicating potential solicitation of others? and (4) did plaintiff and defendant occupy unequal bargaining positions? While no one factor is dispositive and it is not necessary that all of them be established, the plaintiff is required to establish sufficient indicia of effect on public interest from which a trier of fact could reasonably find public interest impact.

Torts > ... > Concerted Action > Civil Conspiracy > Elements

#### **HN20** [L] **Civil Conspiracy, Elements**

The establishment of a civil conspiracy requires a plaintiff to demonstrate two elements: (1) that two or more parties combined to accomplish an unlawful purpose or combined to accomplish a lawful purpose by unlawful means, and (2) the conspirators entered into an agreement to accomplish the conspiracy.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

#### **HN21** [L] **Exemptions & Immunities, Noerr-Pennington Doctrine**

The Noerr-Pennington doctrine provides First Amendment protection to lobbying and legislative activities regardless of the party's subjective goal or interest.

Antitrust & Trade Law > Exemptions & Immunities > Noerr-Pennington Doctrine > Scope

#### **HN22** [L] **Exemptions & Immunities, Noerr-Pennington Doctrine**

The protection of the Noerr-Pennington doctrine has been extended to unions.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### **HN23** [L] **Union Violations, Secondary Activities**

A "hot cargo agreement" is an agreement between a union and a secondary (union) employer to boycott the goods or services of a primary (non-union) business.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### [HN24](#) [↓] **Union Violations, Secondary Activities**

The two-part test for a lawful work-preservation clause requires proof that: (1) the object of the clause is preservation of work traditionally performed by the union, and (2) the contracting employer has the power to give the employees the work at issue (the "right of control" test).

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### [HN25](#) [↓] **Union Violations, Secondary Activities**

29 U.S.C.S. § 158(b)(4)(B) bars unions from forcing or requiring any person to cease doing business with any other person.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### [HN26](#) [↓] **Union Violations, Secondary Activities**

29 U.S.C.S. § 158(e) defines as an unfair labor practice any contract or agreement, express or implied between a union and an employer to cease doing business with any other person.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### [HN27](#) [↓] **Union Violations, Secondary Activities**

Both 29 U.S.C.S. § 159(b)(4)(B) and 29 U.S.C.S. § 158(e) are aimed at the practice of "secondary boycotts," whereby a union can apply pressure on one (non-union) employer through the union's relationship with another (union) employer. Violations of § 158(b)(4) cover a wide range of actions but require some proof of coercion, while § 158(e) is aimed at "hot cargo agreements" wherein a union and employer enter into an agreement that the employer will not do business with a second employer whom the union considers to be unfair to organized labor.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

#### [HN28](#) [↓] **Union Violations, Secondary Activities**

The term "coerce" extends to any form of economic pressure of a compelling or restraining nature.

Torts > ... > Business Relationships > Intentional Interference > Elements

#### [HN29](#) [↓] **Intentional Interference, Elements**

There are five elements to establishing a cause of action for tortious interference with a business expectancy: (1) a valid contract or business expectancy; (2) of which the defendant had knowledge; (3) an intentional interference inducing or causing a breach of the contract or expectancy; (4) existence of an improper motive or use of an improper means in the interference; (5) resulting in damages.

Torts > ... > Business Relationships > Intentional Interference > Elements

### [\*\*HN30\*\*](#) [L] **Intentional Interference, Elements**

A valid business expectancy includes any prospective contractual or business relationship that would be of pecuniary value.

Civil Rights Law > ... > Section 1983 Actions > Elements > General Overview

### [\*\*HN31\*\*](#) [L] **Section 1983 Actions, Elements**

The elements of a [42 U.S.C.S. § 1983](#) claim are: (1) the conduct complained of was committed by a person acting under color of state law; and (2) the conduct deprived a person of rights, privileges, or immunities secured by the Constitution or laws of the United States.

Civil Rights Law > ... > Elements > Color of State Law > Joint Ventures

### [\*\*HN32\*\*](#) [L] **Color of State Law, Joint Ventures**

The "state actor" component of a [42 U.S.C.S. § 1983](#) claim can be established by showing that a private person conspired with a local governmental official.

Civil Rights Law > ... > Elements > Color of State Law > Joint Ventures

### [\*\*HN33\*\*](#) [L] **Color of State Law, Joint Ventures**

A defendant's knowledge of and participation in a conspiracy may be inferred from circumstantial evidence from evidence of the defendant's actions.

Labor & Employment Law > ... > Unfair Labor Practices > Union Violations > Secondary Activities

### [\*\*HN34\*\*](#) [L] **Union Violations, Secondary Activities**

Congress has given parties with allegations of violations of [29 U.S.C.S. § 158\(b\)\(4\)](#) the right to sue a union for damages in any district court of the United States. [29 U.S.C.S. § 187\(b\)](#).

Business & Corporate Compliance > ... > Unfair Labor Practices > Employer Violations > Interference With Protected Activities

Civil Rights Law > ... > Section 1983 Actions > Scope > Government Actions

## [HN35](#) [blue icon] Employer Violations, Interference With Protected Activities

The National Labor Relations Act does not preclude a [42 U.S.C.S. § 1983](#) action arising from government interference with federally-protected labor rights.

Civil Rights Law > ... > Elements > Color of State Law > Joint Ventures

## [HN36](#) [blue icon] Color of State Law, Joint Ventures

Private parties may be liable under [42 U.S.C.S. § 1983](#) when they join with government entities to interfere with federally-protected rights.

Civil Rights Law > ... > Section 1983 Actions > Elements > Protected Rights

## [HN37](#) [blue icon] Elements, Protected Rights

In a [42 U.S.C.S. § 1983](#) suit, the burden is on the defendant to establish that [§ 1983](#) protection has been withdrawn for violation of a particular federal right.

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For Unite Here Local 8, formerly known as, Hotel Employees And Restaurant, Employees Union Local No 8, Defendant: J Thomas Bowen, Kristin L Martin, Michael T Anderson, Richard G McCracken, DAVIS COWELL & BOWE, SAN FRANCISCO, CA; Terrance M Costello, Dmitri Iglitzin, SCHWERIN CAMPBELL BARNARD, LLP, SEATTLE, WA.

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For Host International Inc, Counter Claimant: Molly A Terwilliger, HELLER EHRMAN LLP (WA), SEATTLE, WA.

**Judges:** Marsha J. Pechman, United States District Judge.

**Opinion by:** Marsha J. Pechman

## **Opinion**

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### ORDER ON MOTIONS FOR SUMMARY JUDGMENT

The above-entitled Court, having received and reviewed the motions of all three Defendants for summary judgment in this matter, all the pleadings filed in response to said motions, and all exhibits and declarations attached thereto, and having heard oral argument thereon, makes the following ruling:

[\*2] IT IS HEREBY ORDERED that summary judgment will be GRANTED to all Defendants on the following causes of action:

1. Violations of the Washington anti-trust statutes ([RCW 19.86.030](#), [19.86.040](#))
2. Violations of the Washington Consumer Protection Act ([RCW 19.86.020](#))

IT IS FURTHER ORDERED that summary judgment will be DENIED on the following causes of action:

1. Civil conspiracy under Washington state law (as to all Defendants)
2. Violations of [42 U.S.C. § 1983](#) (as to all Defendants)
3. Violations of the National Labor Relations Act, [29 U.S.C. §§ 158\(b\)\(4\)](#) and [\(e\)](#) (as to Defendant Hotel Employees and Restaurant Employees Union Local No. 8 only)
4. Allegations of tortious interference with a business [\*3] expectancy (as to Defendants the Port of Seattle and Hotel Employees and Restaurant Employees Union Local No. 8 only).

IT IS FURTHER ORDERED that summary judgment as to the cause of action against Defendant the Port of Seattle for contempt of court will be DENIED; however, Plaintiff is ordered to move the Court for an order of referral of the civil contempt cause of action to the Honorable Barbara J. Rothstein of this district for a determination of whether she wishes to retain jurisdiction over such claim.

## **Background**

By virtue of a long-term lease and concession agreement with the Defendant Port of Seattle ("the Port"), Defendant Host International ("Host") had the right to sublease concession space within the Seatac Airport. The Port was obligated by law to make a certain percentage of concession space available for "disadvantaged business enterprises" ("DBEs") and in 1994 Plaintiff Flying Eagle Espresso ("FEE") won out over several hundred other DBE applicants to open a retail coffee kiosk in the baggage claim area of the airport. Like the rest of the DBEs at the time, FEE employed non-union labor (although the business offered no benefit plan, FEE paid a higher [\*4] per-hour wage than the union rate). Elmer Decl., P 9.

Host's lease was set to expire at the end of 2004. The collective bargaining agreement ("CBA") that Defendant Hotel Employees and Restaurant Employees Union Local No. 8 ("HERE") was negotiating with Host prior to the expiration of Host's lease with the Port contained a provision (Article 2.01) with language aimed at non-union shops within the facility:

No work customarily performed by employees covered by this Agreement shall be performed under any sublease, subcontract, or other agreement unless the terms of any lease, contract or other agreement specifically state that (a) all such work shall be performed only by members of the bargaining unit covered by this Agreement and (b) the Employer shall at all times hold and exercise full control of the terms and conditions of employment of all such employees pursuant to the terms of this Agreement. CBA, Article 2.01<sup>1</sup>

[\*5] The CBA was approved and executed in November 2002.

On October 31, 2002, the Port and HERE entered into a Memorandum of Understanding (the "MOU") describing a 3-tier concession structure which included an Exhibit A entitled "Position on Labor Harmony for Concessions." That exhibit's "General Statement" declared:

The Port of Seattle values and requires Labor Harmony among all of the vendors operating at the Airport. To this end, it will be the responsibility of concessionaires to furnish labor that can work in harmony with all other

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<sup>1</sup> Plaintiff makes much of the fact that, in the discussions leading up to the approval of the CBA, HERE notated a draft of the document with the language "Proposal to Apply to Current DBE's" appended to this section. Pltf Exh. 25, p. UNION 000241. The union makes much of the fact that the proposed language was ultimately withdrawn and does not appear in the final language.

labor employed at the Airport and to propose and implement a Labor Harmony plan. This requirement is a material element of the concessionaire lease agreements (the "Contracts"). Failure by a concessionaire or any of its sublessees to comply with this requirement will be deemed a breach of the contract, which will subject the Concessionaire to termination of the Contract with the Port.<sup>2</sup>

[\*6] In June 2003, the Port and Host entered into a new lease (which also contained reference to "labor harmony" and required Port approval of any sublease).

The Port had previously run into difficulty for requiring a third-party tenant to use union labor. An injunction issued by Judge Barbara J. Rothstein of this district in CityIce v. Port of Seattle (C99-1647BJR, Dkt. No. 29) prohibited the Port from engaging in "any conduct that interferes, either by the Port's actions or inactions, with the exercise of the federally protected rights of . . . third parties using Port facilities to assign work to their own employees . . ." It is this order that is the basis of Plaintiff's assertion that the Port is liable for civil contempt of court.

Shortly after these agreements were in place, Plaintiff's owner Jean Elmer ("Elmer") was informed on at least two occasions by Linda LaCombe ("LaCombe"), the Port's retail manager at the facility, that she would have to unionize in order to continue at SeaTac. Elmer Decl. P 9, Pltf. Exh.'s 59, 66. Later testimony by LaCombe indicated that both her position (vis-a-vis the requirements for renewal) and her communications to Elmer were reviewed and [\*7] approved by her superiors. Pltf. Exh. 70.

Elmer polled her employees and was told that they did not wish to join a union. Elmer Decl. P 8. Throughout much of 2003, Elmer received communications, oral and written, from officials for the Port and Host to the effect that she would be required to join the union and that she would have to submit a Labor Harmony Plan (approved by the union) before her sublease would be renewed. Internal communications between representatives of the Defendants indicate that the Port and Host had discussed the issue and agreed that "all facilities covered by the HMS Host contract must be covered by collective bargaining." Pltf. Exh. 73.

On August 27, 2003, Host employee Robert van Snik sent Elmer a Letter of Intent ("LOI") offering to renew her sublease conditioned on the Port's approval of the sublease and FEE's submission of a Labor Harmony Plan. She was encouraged to "meet with representatives of HERE Local 8 to . . . assist you in developing your plan." Van Snik's letter stated that FEE's Labor Harmony Plan ("LHP") "is to contain a statement as to whether HERE Local 8 is in agreement with your plan." Pltf. Exh. 42. Within ten days, Plaintiff responded [\*8] with inquiries about the LHP and whether it meant she had to unionize. Pltf. Exh. 43. Twenty-five days later, Mr. Van Snik of Host responded, but his response included no information about the LHP or the unionization requirement. Instead, Elmer was advised that FEE would have to relocate if they wished to renew their airport lease. Pltf. Exh. 44. Defendants do not controvert Plaintiff's allegation that the nature and substance of the LHP were never explained to her. Elmer Decl. P 15.

In the wake of these exchanges, Elmer alleges that she tried to meet with union officials to discuss the LHP requirement. Elmer Decl. P 13, Pltf. Exh's 49, 52, 55. She was unsuccessful in this attempt until November 13, 2003, when she met with Rick Sawyer of HERE ("Sawyer"). She alleges (and HERE does not deny) that Sawyer said he knew nothing about Host's LHP requirement and had no intention of getting involved in negotiations between FEE and Host on the issue.<sup>3</sup> Elmer Decl. P 13. Accepting his representations, Elmer concluded that there was no requirement that FEE become unionized to continue on at SeaTac and left a voicemail to that effect with Port officials. Pltf. Exh. 93.

[\*9] FEE submitted a Letter of Intent on November 7, 2003. Pltf. Exh. 55. However, having had no success obtaining a meeting with a union representative to that point, the LOI did not contain the LHP Host had indicated was required. Following submission of the November 2003 LOI, FEE made attempts to submit a draft of a LHP to

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<sup>2</sup> The Port's and HERE's position is that this provision applied only to Tier II tenants (a category which not include FEE).

<sup>3</sup> Sawyer testified that he was unaware of the LHP provision and believed the union had no role in approving sublessees' labor harmony plans. Noble Decl. F, Sawyer Dep., pp. 128-132.

Host (Pltf. Exh's 85, 86). On December 19, 2003, van Snik sent a letter to Elmer terminating their negotiations and indicating Host's intent to seek another candidate to fulfill their DBE requirement. Pltf Exh. 87. The termination was confirmed in a letter to FEE's attorneys several days later. Pltf Exh. 88.

Plaintiff did eventually send a finalized version of their LHP (unapproved by HERE and indicating FEE's intent to remain non-union) to Host in January of the following year, but negotiations had completely broken down by that point. Plaintiff alleges that every other DBE in the airport submitted a LHP which indicated (usually in a single paragraph) their intent to adopt the CBA (Pltf Exh's 95 -- 101), and that every one of those requests for renewal was granted.

### **Summary Judgment Standard**

**HN1** Summary judgment is not warranted if a material issue of [\*10] fact exists for trial. *Warren v. City of Carlsbad*, 58 F.3d 439, 441 (9th Cir. 1995), cert. denied, 516 U.S. 1171, 116 S. Ct. 1261, 134 L. Ed. 2d 209 (1996).

**HN2** The underlying facts are viewed in the light most favorable to the party opposing the motion. *Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587, 106 S. Ct. 1348, 89 L. Ed. 2d 538 (1986). **HN3**"Summary judgment will not lie if . . . the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S. Ct. 2505, 91 L. Ed. 2d 202 (1986).

**HN4** The party moving for summary judgment has the burden to show initially the absence of a genuine issue concerning any material fact. *Adickes v. S.H. Kress & Co.*, 398 U.S. 144, 159, 90 S. Ct. 1598, 26 L. Ed. 2d 142 (1970). This can be done by either producing evidence negating an essential element of plaintiff's claim, or by showing that plaintiff does not have enough evidence of an essential element to carry its ultimate burden at trial. *Nissan Fire & Marine Ins. Co. v. Fritz Companies, Inc.*, 210 F.3d 1099, 1103 (9th Cir. 2000).

**HN5** Once the moving party has met its initial burden, the burden shifts to the nonmoving party to establish the existence [\*11] of an issue of fact regarding an element essential to that party's case, and on which that party will bear the burden of proof at trial. *Celotex Corp. v. Catrett*, 477 U.S. 317, 323-24, 106 S. Ct. 2548, 91 L. Ed. 2d 265 (1986). To discharge this burden, the nonmoving party cannot rely on its pleadings, but instead must have evidence showing that there is a genuine issue for trial. *Id. at 324*. Additionally, **HN6** "at the summary judgment stage the judge's function is not . . . to weigh the evidence . . . but to determine whether there is a genuine issue for trial." *Liberty Lobby*, 477 U.S. at 249.

### **Discussion**

The first two causes of action (§§ 1 and 2 of the Sherman Act) in Plaintiff's Second Amended Complaint have been previously dismissed upon motion of Defendants (Dkt. No. 31) and will not be discussed further. This opinion will first address the causes of action upon which summary judgment will be granted.

The Court GRANTS summary judgment on:

#### **§§ 3 and 4 of the Washington Consumer Protection Act/Anti-Trust (Fourth and Fifth Causes of Action)**

The Court's dismissal of Plaintiff's Sherman Act federal anti-trust claims was premised on a finding [\*12] of "state actor" immunity for all defendants under the circumstances presented by this litigation. See *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 38, 44, 105 S. Ct. 1713, 85 L. Ed. 2d 24 (1985); *Lorrie's Travel & Tours, Inc. v. SFO Airporter, Inc.* 753 F.2d 790, 793 (9th Cir. 1985); *Snake River Valley Electric Association v. Pacificorp.*, 357 F.3d 1042, 1047-48 (9th Cir. 2004). Defendants argue that "[s]tate actor immunity bars Flying Eagle from asserting antitrust claims under state law to the same extent that it bars such claims under the Sherman Act." Port's 1st Motion, p. 13.

The argument is made that the Washington legislature intended that the Consumer Protection Act ("CPA") be interpreted along the guidelines set up by the federal courts for corresponding federal statutes (*State v. Black*, 100 Wn.2d 793, 799, 676 P.2d 963 (1984)); since §§ 3 and 4 of the CPA are the state equivalent of the Sherman Act, Defendants claim the same protection afforded them under applicable federal precedents. However, the case law

indicates that the [HN7](#) state courts are to look to federal precedent for "guidance," (*Id.*), not that federal precedent is controlling. [\*13]

[HN8](#) The directive to be "guided by" federal law does not mean that we are bound to follow it. But neither are we free to ignore it, and indeed in practice Washington courts have uniformly followed federal precedent in matters described under the Consumer Protection Act.

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Any departure from federal law . . . must be for a reason rooted in our own statutes or case law and not in the general policy arguments this court would weigh if the issue came before us as a matter of first impression.

[\*Blewett v. Abbott Laboratories, et al., 86 Wash.App. 782, 787-88, 938 P.2d 842 \(1997\).\*](#)

[\*Assurance Co. of America v. Wall & Assoc's, LLC of Olympia, 379 F.3d 557 \(9th Cir. 2004\)\*](#) provides some further insight regarding how this Court should proceed regarding the application of the state actor doctrine to Washington anti-trust law: [HN9](#) "[W]hen interpreting state law, federal courts are bound by decisions of the state's highest court. In the absence of such a decision, a federal court must predict how the highest state court would decide the issue . . ." *Id. at 560*. Therefore, we look to Washington state law for guidance.

[HN10](#) The Washington CPA is [\*14] patterned after federal law and the legislature anticipated that state courts would be guided by federal court interpretation of federal [antitrust law](#). [RCW 19.86.920](#). See, [\*State v. Black, supra\*](#). This statute also commands that the regulatory scheme "be liberally construed that its beneficial purposes may be served." [RCW 19.86.920](#). However, as noted above, this admonition does not mean that state courts are bound to follow federal law. See [\*Blewett v. Abbott Laboratories, supra\*](#). As the [\*Blewett\*](#) court indicated, a departure from following the federal precedent of the state actor immunity doctrine must have a firm foundation in state authority.

The closest Washington state corollary to the state actor immunity doctrine appears in the exemption section of the CPA which governs state action or state regulated entities. [HN11](#) The pertinent language states that the CPA laws, including the anti-trust provisions, do not apply to "actions or transactions permitted by any other regulatory body or officer acting under statutory authority of this state." [RCW 19.86.170](#). [\*15] <sup>4</sup> This appears to be the Washington codification of the state actor doctrine.

[HN12](#) In delineating the application of this exception, Washington courts have taken the approach that "[l]iberal construction' is a command that the coverage of an act's provisions in fact be liberally construed and that its exceptions be narrowly confined." [\*Vogt v. Seattle-First National Bank, 117 Wn.2d 541, 552, 817 P.2d 1365 \(1991\)\*](#) (en banc). As a result, Washington courts have carefully scrutinized both the "action or transaction" involved and the permission required to qualify for [\*16] exemption under [RCW 19.86.170](#).

In [\*Dick v. Attorney General \(83 Wn.2d 684, 521 P.2d 702 \(1974\)\)\*](#) [HN13](#) the Court articulated a narrow interpretation of "action or transaction" such that a generally regulated practice does not automatically receive exemption from CPA claims. *Id. at 688*. "If a particular practice found to be unfair or deceptive is not regulated, even though the business is regulated generally, it would appear to be the legislative intent that the provisions of the act should apply." *Id.* Although [\*Dick\*](#) analyzed an older version of the exemption section of the CPA, more recent cases likewise uphold the narrow interpretation of activity defined in the case. See [\*Vogt, 117 Wn.2d at 551\*](#). [HN14](#) Washington courts making an "exemption" analysis have closely analyzed the activity at issue for specific permission and narrowly construed that permission in order to avoid conflict with the "liberal construction" intent of the Washington legislature. As a result, "permission" necessitates overt affirmative action to permit the activity by

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<sup>4</sup> The statute states that the CPA does not apply to "actions and transactions otherwise permitted, prohibited or regulated under laws administered by the insurance commissioner of this state, the Washington utilities and transportation commission, the federal power commission." The narrower "actions or transactions permitted" language applies only to "any other regulating body or authority." [RCW 19.86.170](#).

the entity involved in the complaint. [Vogt, Id. at 552](#). Washington [\*17] takes a very limited approach to its application of the exemption for activities permitted by most agencies.

As the parties' briefing indicates, there are no Washington cases directly on point. The reasoning and ruling of [Robinson v. Avis Rent A Car Systems, Inc. \(106 Wn.App. 104, 22 P.3d 818 \(2001\)\)](#) provides the closest analogous example, all the more so considering that it involved the Port's relationship with car rental dealerships at the airport. The Port charged rental car companies a concession fee for leasing space at the airport. The concession agreement originally prevented rental car companies from charging customers a separate fee to cover this expense. In order to recoup the expense, the car companies included the fee within the total charge quoted to the customer. When the Port decided not to enforce the provision preventing the charging of the separate fee, the rental companies began "unbundling" or separating the concession fee from the basic rental rate. Customers brought suit alleging that the additional concession fee was not quoted to them when making their reservations and the additional, separate charge was unfair or deceptive.

Several aspects of Robinson [\*18] apply to the case at hand and suggest that Washington courts would not find state actor immunity applicable to Defendants' actions here. First, both cases involve oversight activity by the Port. [Robinson](#) identifies the Port as a "regulatory body" as defined by [RCW 19.86.170](#). Since the Port occupies the same landlord authority over Host as over Avis, the Port would qualify as a "regulatory body" within the meaning of the statute for this case.

The [Robinson](#) court also examined the powers granted to the Port as a regulating body for evidence of specific statutory authority permitting the activities of the rental car agencies. The opinion defined what must be demonstrated for specific permission: "[I]t is not enough to show that the Port . . . permitted' unbundling . . . [t]he car rental companies must also show that unbundling is within the statutory authority' of the Port to permit." [Robinson, 106 Wn.App. at 110-113, 22 P.3d at 822](#). The court found no authority in the Port's enabling statutes to permit the complained-of activities of the defendant car companies. [RCW 14.08.120\(6\)](#) gives the Port the authority to "determine [\*19] the charges or rental for the use of any properties under its control and the charges for any services or accommodations, and the terms and conditions under which such properties may be used." [Id. at 823](#) (citing [RCW 14.08.120\(6\)](#)). The [Robinson](#) court's reading of this statute concluded that "this statute neither expressly nor impliedly grants to the Port the power to permit unbundling for purposes of exemption under the CPA." [Id. At 823](#).

This Court's order dismissing the Sherman Act claims focuses on two other sections of [HN15](#) [14.08.120](#) permitting the Port

to confer the privileges of concession of supplying upon its airports goods, commodities, things, services and facilities . . . ([RCW 14.08.120\(4\)](#)) and . . . to sell or lease any property, real or personal, acquired for airport purposes and belonging to the municipality, which in the judgment of its governing body, may not be required for aircraft landings, aircraft takeoffs, or related aeronautic purposes, in accordance with the laws of this state. [RCW 14.08.120\(5\)](#)

Dkt. No. 31, Order on Motion To Dismiss, [\*20] pp. 4-5.

Similar to the provision allowing for rental car companies, this grant of authority allows the Port to lease to concessionaires like Host. However, it does not appear to give any authority for regulating subtenants of those concessionaires by requiring things like LHPs. Given Washington's narrow application of the exemption, the fact that the statute does not expressly or impliedly allow the Port to permit a lessee to require that subtenants have a LHP (regardless of what that document consists of) is highly significant. Since the statute does not contain specific language discussing the Port's regulation of subtenants of concessionaires, the "overt affirmative action to permit the activity by the entity involved" required for exemption under [RCW 19.86.170](#) is missing. [Vogt, 117 Wn.2d at 552](#). This suggests that the Washington courts would not find state actor immunity for the Port or the other defendants in this case.

As discussed in this Court's previous Order, the Ninth Circuit has been increasingly willing to broaden the state actor exemption. (Order, *supra* at 4-5). The federal precedents indicated that the structure of [\*21] concession leasing at the airport was a reasonable consequence of the Port's authorizing statute. *Id.* at 5. However, Washington courts require a specific grant of permission for the discrete transaction or action involved. Concession leasing structure in general may be regulated under the Port statutes, but this general regulation is not adequate for exemption under the CPA.

This case fits the situation described in *Dick v. Attorney General*, where "a particular practice found to be unfair or deceptive is not regulated, even though the business is regulated generally." [83 Wn.2d at 684](#). Based on a finding that the Washington courts have spoken on the issue of state actor immunity by announcing tests far stricter than the federal precedents applying state actor immunity, this Court is not inclined to allow dismissal of the state antitrust claims based only on the prior dismissal of the Sherman Act claims.

However, even with a finding that "state actor immunity" will not be extended to these Defendants for the allegations of violating the Washington anti-trust statutes, Defendants are nevertheless entitled to summary judgment on these causes of action. [HN16\[!\[\]\(6672efaf27c0e6cf66ff97afab598eec\_img.jpg\)\]](#) Plaintiff [\*22] has the burden to prove possession of monopoly power in a relevant market. [High Technology Careers v. San Jose Mercury News, 996 F.2d 987, 989-90 \(9th Cir. 1993\)](#). What is fatal to FEE's anti-trust allegations is its failure to offer proof of what the relevant market is (in terms of geography or product) over which they allege Defendants are exercising a monopoly. They argue that the definition of the requisite geographic market is a fact issue and contend (without citation to any evidence) that "SeaTac is a self-contained geographic market" and that "the logical geographic market is the SeaTac site." Plaintiff's 1st Response, p. 40. The case law cited in support of their argument ([International Boxing Club v. United States, 358 U.S. 242, 79 S. Ct. 245, 3 L. Ed. 2d 270 \(1959\)](#)) is not helpful: the Supreme Court in *International Boxing* found a "separate, identifiable market" based on "detailed findings" (*Id. at 250-51*) which are completely absent from Plaintiff's pleadings.

At oral argument, Plaintiff argued that the "market" which they were claiming had been monopolized by Defendants' activities was not the airport concessions market (generally) or coffee retail [\*23] service (specifically) but rather the "labor market" represented (presumably) by all the jobs available within the airport. Plaintiff's complaint makes no mention of the "labor market" as the intended object of the anti-trust allegations. Their reply brief does make mention of an attempt to "monopolize the provision of labor in the concessions market at SeaTac" (Pltf's 1st Reply, p. 39), but neither the Court nor Defendants read this to mean that Plaintiff's complaint was aimed at the monopolization of a "labor market." In any event, the deficiency in Plaintiff's proof is unaffected by this contention -- whether monopolization of coffee stands or labor markets is the object of the complaint, Plaintiff has still failed to proffer the requisite proof of a "separate, identifiable market."

Plaintiff's anti-trust claims also suffer from a failure of proof of injury to competition. [Intergraph Corp. v. Intel Corp., 195 F.3d 1346, 1354 \(Fed.Cir. 1999\)](#). [HN17\[!\[\]\(f8871c62756c32ab96ba4c6a49ad0985\_img.jpg\)\]](#) It is not enough to claim that FEE's own operations were injured; "[t]he antitrust laws were enacted for the protection of competition, not competitors," *Id.*, quoting [Brunswick Corp. v. Pueblo-Bowl-O-Mat, Inc., 429 U.S. 477, 488, 97 S. Ct. 690, 50 L. Ed. 2d 701 \(1977\)](#). [\*24] Plaintiff has provided no evidence, in the form of declarations, expert testimony or statistics, that Defendants' alleged activities have injured competition. The fact that the rest of the DBEs signed renewed leases after submitting pro-union LHPs may be probative on the issue of mandatory unionization, but it falls short of proof of actual injury for anti-trust purposes (nor does Plaintiff present any statutory authority that mandatory unionization is "injury per se"). Based on these findings, summary judgment will be GRANTED on Plaintiff's state anti-trust law claims.

The Court also GRANTS summary judgment on:

#### § 2 of the Washington Consumer Protection Act (Sixth Cause of Action)

[HN18\[!\[\]\(c8d9c0db15dc120aef115cfd42f41f18\_img.jpg\)\]](#) To prevail in a private Consumer Protection Act action, a plaintiff must establish five distinct elements: (1) an unfair or deceptive act or practice; (2) occurring in trade or commerce; (3) public interest impact; (4) injury to plaintiff in his or her business or property; and (5) causation.

Hangman Ridge Training Stables, Inc. v. Safco Title Ins. Co., 105 Wn.2d 778, 780, 719 P.2d 531 (1986). Plaintiff must satisfy all five elements in order to prevail; in the summary [\*25] judgment context, a plaintiff has the burden to establish, at a minimum, the existence of disputed issues of material fact regarding each of the elements of its cause of action. Celotex, supra at 323-24. Plaintiff's CPA cause of action in this case is vulnerable to summary judgment because they have not established any facts supporting the existence of a "public interest impact" as regards any of the defendants.

Despite Plaintiff's attempts to characterize its circumstances in a different light, the Court finds that the facts in this case constitute a private contractual dispute. HN19[ "Ordinarily, a breach of a private contract affecting no one but the parties to the contract is not an act or practice affecting the public interest." Id. at 790. A complainant can refashion a private dispute into one with an impact on the public by (1) a "per se" showing of the violation of a statute with a specific legislative declaration of public interest (not alleged here) or (2) a showing that additional plaintiffs have been or will be impacted in a similar manner. The factors which need to be proven in this regard include:

- (1) Were the alleged acts committed in the [\*26] course of defendant's business?
- (2) Did defendant advertise to the public in general?
- (3) Did defendant actively solicit this particular plaintiff, indicating potential solicitation of others?
- (4) Did plaintiff and defendant occupy unequal bargaining positions?

While no one factor is dispositive and it is not necessary that all of them be established, FEE is required to establish sufficient "indicia of effect on public interest from which a trier of fact could reasonably find public interest impact." Id. at 790-91.

Plaintiff's evidence regarding HERE and the Port is simply non-existent with respect to three of the four factors. Neither the union nor the municipal governmental body advertise to the public in general, nor is there any proof that they solicited this particular plaintiff for anything. Since FEE was therefore not in a bargaining posture with either entity, there is no element of "unequal bargaining positions."

The CPA claim as regards Defendant Host presents somewhat different issues. Plaintiff certainly makes the case that the alleged acts were committed in the course of Host's business as a master concessionaire at the airport; that it was [\*27] actively solicited by Host (as evidenced by the presentation to FEE of the August 27, 2003 LOI, Pltf Exh. 42); and (viewing the evidence in the light most favorable to Plaintiff) that the parties did not occupy equal bargaining positions (Host, as an international corporation, being possessed of far greater resources to bring to the bargaining/ negotiating process than a single-stand coffee retailer like FEE).

But there is no evidence that Host advertised "to the public in general" and indeed no evidence that they even solicited the replacement DBE who took over the sublease formerly held by Plaintiff. FEE concedes that Defendants "may" not have advertised to the general public, but states conclusorily that Host did solicit new tenants for SeaTac space. While the Court may imagine that new applicants for vacant subleases found out about their availability somehow, this is no substitute for the requirement that a nonmovant in a summary judgment action produce evidence showing that there is a genuine issue for trial. Plaintiffs provide no proof of this solicitation, nor do they provide any case authority for the larger issue of whether the solicitation of a few DBEs constitutes the [\*28] kind of "advertising to the public in general" which goes to the heart of the "public impact" issue.

In the final analysis, Plaintiff has not borne its burden of establishing genuine disputes of material fact tending to establish that its private contract dispute with Defendant Host has any public interest or public impact whatsoever. All Defendants are entitled to summary judgment dismissing the CPA § 2 claims against them.

The opinion now turns to those causes of action upon which summary judgment will not be granted.

Summary judgment will be DENIED on:

## **Civil Conspiracy under State Law (Seventh Cause of Action)**

**HN20** [+] The establishment of a civil conspiracy among these defendants requires Plaintiff to demonstrate two elements: (1) that two or more parties combined to accomplish an unlawful purpose or combined to accomplish a lawful purpose by unlawful means, and (2) the conspirators entered into an agreement to accomplish the conspiracy. [Newton Ins. Agency & Brokerage, Inc. v. Caledonian Ins. Group, Inc., 114 Wn.App. 151, 160, 52 P.3d 30 \(2002\).](#)

None of the defendants disputes that requiring FEE to unionize as a condition of the renewal of their lease at SeaTac [\*29] is legally impermissible. If Plaintiff succeeds in establishing the existence of genuine disputes of material fact concerning each of the two prongs of the civil conspiracy proof as regards each of these Defendants, they are entitled to a denial of summary judgment on this cause of action. The Court finds that Plaintiff has carried this burden.

Plaintiff's proof regarding these two prongs falls into two general categories: first, the documented agreements between Defendants -- the MOU (between the Port and HERE) and the CBA (between Host and HERE); second, the evidentiary proof of the conduct and communications between representatives of each defense entity, both amongst themselves and with Elmer. This opinion will examine them each in turn.

### **1. Documented Agreements Supporting Plaintiff's Theory of Conspiracy**

#### **A. Memorandum of Understanding**

The MOU is a multi-part document, two parts of which are at issue in this lawsuit. There is a "Memorandum of Understanding" which describes a three-tiered system of concessions within the airport. There is no dispute that, as described in the agreement, FEE was to be a "Tier I" concessionaire. The other part of the MOU which is [\*30] relevant to this case is Exhibit A to the Memorandum (which is labeled "Position on Labor Harmony for Concession") -- specifically, the "General Statement" which has been quoted *supra* and admonishes that "failure by a concessionaire or any of its sublessees" to implement a LHP will be deemed a breach of contract. Pltf Exh. 29, UNION002460.

Both of the parties to the MOU argue strenuously that Exhibit A is inapplicable to Tier I concessionaires, including Plaintiff. At the very least, the document is unclear in this regard. In the portion of the memorandum describing Tier II concessionaires, the following language appears: "See 2., below, for provisions related to Labor and Worker Retention that will be included in the solicitation for and selection of these concessionaires." Paragraph 2 states, in relevant part: "The Port will solicit qualifications of interested parties, and choose, the two Tier II prime concessionaires through Request for Qualifications ("RFQ") . . . These RFQs will be governed by the Position on Labor Harmony for Concessions (Exhibit A) . . ." *Id.* at UNION002458-59.

This Court finds, as a matter of law, that the MOU and specifically Exhibit A, "Position [\*31] on Labor Harmony" could be applied to Tier I as well as Tier II concessionaires. The language quoted above from Paragraphs 1 and 2 of the memorandum does not, as Defendants argue, clearly and unequivocally indicate that Exhibit A applied exclusively to Tier II concessionaires; it can only be read as indicating that Tier II concessionaires were to be included in the "labor harmony" requirements of Exhibit A which, by its own language, applied to "all vendors operating at the airport." (Emphasis supplied.) The Court notes the following factors in reaching this conclusion: the labeling of the provision at issue as a "General Statement," the use of the phrase "all vendors," the language admonishing against "[f]ailure by a concessionaire or any of its sublessees" and the complete absence of any language indicating that the provisions contained in the "General Statement" were to be restricted to Tier II concessionaires only.

HERE claims, as regards the MOU, the protection of **HN21** [+] the Noerr-Pennington doctrine, which provides First Amendment protection to lobbying and legislative activities regardless of the party's subjective goal or interest.

*Eastern R. Presidents' Conference v. Noerr Motor Freight, Inc.*, 365 U.S. 127, 137-38, 81 S. Ct. 523, 5 L. Ed. 2d 464 (1961); [\*32] *United Mine Workers v. Pennington*, 381 U.S. 657, 669-72, 85 S. Ct. 1585, 14 L. Ed. 2d 626 (1965).

**HN22** [↑] That protection was extended to unions in *Franchise Realty Interstate Corp. v. San Francisco Local Joint Executive Board of Culinary Workers*, 542 F.2d 1076 (9th Cir. 1976), cert. denied, 430 U.S. 940, 97 S. Ct. 1571, 51 L. Ed. 2d 787 (1977). As long as FEE is unable to produce evidence of any acts of unlawful economic coercion, the union argues that their lobbying and persuasion efforts are afforded constitutional sanction.

In evaluating HERE's claim, the Court does not have to view the MOU in isolation. In addition to lobbying for a "labor harmony" requirement in its agreement with the Port, the union was also negotiating for language in its CBA which mandated that the Tier I concessionaires (such as Host) require all their sublessees whose businesses involved work "customarily performed" by the union to employ union labor. Noerr-Pennington has never been upheld as a shield to protect from liability a union defendant who lobbies a governmental body to support concessionaires in a requirement to unionize third-party subcontractors; especially with a court injunction already in place prohibiting such activity.

[\*33] Nor is the Court required to ignore the fact that Plaintiff has produced evidence that seven other DBEs submitted the "labor harmony plans" called for in the MOU (and in the Port's lease with Host) which consisted of nothing more than a single paragraph agreeing to adopt the CBA and accept union representation for their workers. Pltf Exh's 95-101. It is circumstantial evidence of exactly what Plaintiff is claiming -- that the cost of receiving a renewed sublease at the airport was unionization -- and if Plaintiff's claim is ultimately upheld the union's activities will be outside the shield of Noerr-Pennington. A jury is entitled to consider whether that evidence tends to establish the existence of an agreement to achieve an unlawful purpose.

The union produces no case authority limiting the definition of "coercion" to actual strikes, boycotts or violence. Plaintiff has produced circumstantial evidence that the union was willing to increase the pressure on the other parties in order to accomplish what it desired; e.g., statements by union officials concerning "a campaign of escalating actions" (Noble Decl. E, Nelson Dep., p. 36; Exh. 119) and "a lot more coming" (Noble Decl. [\*34] J, Wise Dep., pp. 15 20; Exh. 6) create genuine issues of fact regarding the existence of coercion in the union's conduct.

Furthermore, if it is ultimately found that the MOU violated the CityIce injunction, there will be no question of a need to produce evidence of "economic coercion:" the CityIce injunction (1) already prohibited the Port from doing what FEE alleges the MOU accomplished (thus making it illegal *per se*) and (2) was based on a finding by Judge Rothstein that HERE had "committed an illegal secondary boycott," not that it had engaged in "economic coercion."

HERE replies that it is not required to predict whether the results of its lobbying will be judicially upheld to invoke the protections of Noerr-Pennington. *Subscription Television, Inc. v. So.Cal. Theatre Owners Ass'n*, 576 F.2d 230, 233-34 (9th Cir. 1978). Since it genuinely sought a legitimate result through governmental action, the union argues, it is shielded. This is not a persuasive position: the union did not simply seek "work preservation" as a general concept; it specifically lobbied for the particular language of the MOU, and (as one of the other parties in the CityIce [\*35] litigation) it can be held responsible if it knowingly trespassed the constraints established by the court's order in that case. If the MOU is found to be an illegal attempt to mandate third-party unionization as a condition of lease renewal, HERE should not be shielded from the consequences of seeking such a result. To the extent that the defendant union seeks summary judgment as a matter of law concerning its part in the creation of the MOU, that motion is denied.

## B. Collective Bargaining Agreement

The crucial provision in this document is Article 2.01 and its requirement that "no work customarily performed by employees covered by this Agreement" will be contracted out under sublease unless those employees are likewise covered by the CBA. HERE argues that Plaintiff misreads Article 2.01: (1) it was intended to apply only to "new" Host sublessees. and (2) the union never sought to enforce it against anyone, including FEE. The union points to the lack of proof that 2.01 was ever cited to coerce or persuade Host not to renew FEE's lease.

The union's arguments in this regard are not persuasive. Concerning the intended objective of Article 2.01, there is nothing in the language [\*36] that differentiates between "current" and "new" subleases. Furthermore, as a renewing tenant, Plaintiff was negotiating a "new" sublease with Host. Viewing the evidence in the light most favorable to Plaintiff, the fact that all the DBEs except FEE filed labor harmony plans indicating their agreement to unionize tends to prove that all the renewing sublessees were treated as "new" tenants. Furthermore, if the CBA is ultimately found to represent a "hot cargo" agreement in violation of [§ 8\(e\) of the NLRA](#)<sup>5</sup>, it will be illegal regardless of whether either party to the agreement attempted to enforce it. See [Teamsters Local 728 \(Brown Transport Corp., 140 N.L.R.B. 1436, 1437, 52 LLRM 1258 \(1963\)\)](#).

Regarding the union's "lack of coercion" argument: if coercion had been applied (as Plaintiff contends) [\*37] its effects were felt when Host informed FEE that they would have to obtain union approval for a LHP which Plaintiff seeks to prove was simply a disguised requirement of mandatory unionization. As discussed in the MOU analysis *supra*, FEE has produced evidence of statements by union officials suggesting repercussions would ensue if these agreements were not adopted. A jury could reasonably infer the existence of coercion from these statements.

The union takes the further position that the CBA is valid because they had a right to preserve work for the union which had traditionally been performed by union labor, such as coffee service. [HN24](#)[<sup>↑</sup>] The two-part test for a lawful work-preservation clause (set out in [NLRB v. Int'l Longshoremens Assoc., 447 U.S. 490, 504, 100 S. Ct. 2305, 65 L. Ed. 2d 289 \(1980\)](#) (a/k/a ILA)) requires proof that (1) the object of the clause is preservation of work traditionally performed by the union and (2) the contracting employer has the power to give the employees the work at issue (the "right of control" test).<sup>6</sup> This situation, according to HERE, meets both those criteria. Plaintiff has not disputed that, at some point in the past, retail coffee service was the exclusive [\*38] domain of the union -- ILA says that the focus is on the "lost work" of the union and that they have a right to recapture that work. [Id. at 507-508](#). The fact that no union worker ever worked out of FEE's particular location is irrelevant -- it is the kind of work historically performed by union labor and that is what matters in a "work preservation" analysis. [Id.](#)

The union has not convinced this Court, however, that their agreement satisfies the "right to control" part of the ILA test. The Supreme Court stated in that case that "if the contracting employer [\*39] has no power to assign the work, it is reasonable to infer that the agreement has a secondary objective, that is, to influence whoever does have such power over the work." [447 U.S. at 504-05](#). Since Host (the contracting employer) had no power to assign the work of FEE's employees, a jury would be free to draw the inference that the intent of the "work preservation clause" was in fact to satisfy other union objectives; i.e., to influence the non-union DBEs. HERE's response to this argument is that Host's right to renew FEE's lease is sufficient to satisfy the "right of control" test. HERE attempts to analogize to the ILA situation, but the situations in fact appear to be different in one crucial respect: the agreements in the ILA cases were directly with the contractors who controlled the container work, while the CBA at issue here requires Host to impose the agreement on subcontracting employers who had no part in negotiating the original agreement. It is a critical distinction and goes to the heart of the inquiry regarding whether the purpose of the agreement was "to satisfy union objectives elsewhere" ([Id. at 504](#)), thus crossing the boundary [\*40] into unlawful activity. Plaintiff has raised sufficient questions of material fact regarding the existence of a "secondary objective" underlying the CBA to permit that question to go to a jury.

Although Defendants are not entitled to summary judgment as a matter of law on the basis of either the MOU or the CBA, ultimately, as Plaintiff points out, the civil conspiracy case does not stand or fall on these documents alone. Even though the agreements themselves may be found to have lawful ends, if they are proved to have been used for unlawful purposes, or if Defendants engaged in other activities which were themselves outside the bounds of

<sup>5</sup> [HN23](#)[<sup>↑</sup>] A "hot cargo agreement" is an agreement between a union and a secondary (union) employer to boycott the goods or services of a primary (non-union) business; it is discussed in greater depth *infra*.

<sup>6</sup> The ILA cases involved a situation where a new technology -- the use of stackable shipping containers -- had obviated the need for the traditionally union-performed service of loading and unloading cargo from ships. The Supreme Court upheld the right of the union to recapture through CBAs the work lost through the advent of the containers, even though container loading/unloading had never been performed by union labor.

permissible conduct in the context of labor and lease negotiation, Defendants may still be found to have conspired against Plaintiff. The Court finds, as discussed below, that Plaintiff has also raised genuine disputes of material fact in regards to Defendants' conduct which entitle them to survive summary judgment on their conspiracy cause of action.

## 2. Defendants' Conduct Supporting Plaintiff's Theory of Conspiracy

Plaintiff has raised disputed issues of material fact regarding whether the conduct of Defendants during the time period [\*41] in question evidences (1) a combination "to accomplish an unlawful purpose or . . . to accomplish a lawful purpose by unlawful means and (2) "an agreement to accomplish the conspiracy. Newton, supra.

Again, the parties are not in dispute regarding the impermissibility of forcing FEE to unionize as a condition of receiving a lease renewal at the airport. Yet communications from officials from each of the defendants, viewed in the light most favorable to Plaintiff, could lead a reasonable jury to conclude that this was in fact the goal of Defendants and that they had agreed amongst each other to accomplish that goal.

The Court will not review the voluminous submissions by the parties in their entirety, but will instead focus on representative pieces of evidence which suffice to create issues of material fact on the key elements of Plaintiff's case which are challenged by Defendants' summary judgment motions. First are the written statements by the Port's airport retail manager, Linda LaCombe ("LaCombe") to her superiors and then to Elmer. In March of 2003, LaCombe wrote an e-mail stating:

I met with Jean Elmer, Flying Eagle Espresso, this morning. She was told by Host [\*42] that, per the new labor Agreement, she would need to become a union represented business . . . I believe this is all true according to the Labor Agreement that Host has currently.

Pltf Exh. 63.

Two months later, she communicated not only the Port's understanding of the CBA to Elmer, but also the fact that the Port had discussed both the new lease and the labor agreement with representatives of Defendant Host:

I have gone over the specifics of the new lease with Host and their new contract with H.E.R.E. I understand that Pat Hedges and Art Spring [of Host] have also taken you through the contract and its requirements. It states in the Labor Agreement that any subtenant of Host must be unionized. It further states that any business/subtenant operating as a non-union shop, under this agreement, violates the contract between Host and H.E.R.E. Host has met with their attorney and there is no negotiating on this point.

Pltf Exh. 66. LaCombe closes the letter by indicating that "[t]he Port supports the contract between Host and H.E.R.E." Id. LaCombe repeated the Port's position to Elmer almost *verbatim* in another letter dated June 12, 2003, including that [\*43] "Host has met with their attorney and there is no negotiating on this point. The Port is unaware of anything illegal in the Host Lease agreement with H.E.R.E." Pltf Exh. 59.

In fact, it would have been illegal for Host and the union to agree to force subcontractors to unionize as a condition of having their leases renewed. Plaintiff succeeds, by virtue of this evidence, in creating a disputed material factual issue regarding the Port's participation in and support of a plan to accomplish mandatory unionization of subcontractors. In its briefing, the Port has done its best to distance itself from LaCombe's statements and portray them as the opinion or mistaken belief of a lone employee. But again Plaintiff produces documentary evidence which, viewed in a favorable light to FEE, suggests that this position was endorsed by her superiors. From a May 23, 2003 LaCombe e-mail to Mr. Reis and Mr. Natarajan of the Port:

She [Elmer] really must become a union member. I completely understand [Elmer]'s reluctance to do so. However, it was made very clear by the Commissioners that they value the fair and positive treatment of our employees here at Sea Tac. Currently, [Elmer] [\*44] does not pay any benefits vacations, etc. for her employees.

Pltf Exh. 70 (emphasis supplied). Both LaCombe and her direct manager, Mr. Natarajan, testified at deposition that her communications were vetted by not only her superiors but the Port's attorneys as well. Noble Decl. C, LaCombe Dep., pp. 36-41; Noble Decl. D, Natarajan Dep., pp. 37-39.

Regarding Defendant Host, it is likewise the finding of this Court that the evidence produced by Plaintiff is sufficient to create material issues of disputed fact regarding Host's participation in a civil conspiracy to force a third-party subcontractor to accept a CBA they did not negotiate. It was Host's Letter of Intent to FEE which first advised Plaintiff that a LHP approved by the union was a prerequisite to obtaining a new lease at the airport (a requirement that was at least partially responsible for the delay in finalizing a lease renewal which was cited by Host in terminating negotiations with Plaintiff). Since Host was not even a party to the MOU which established the labor harmony requirement, this alone is evidence from which a jury could conclude there had been a meeting of the minds between these defendants as to the [\*45] necessity of Plaintiff adopting the CBA between Host and HERE.

Additionally, there is evidence that representatives of both of the other defendants had been told that Host supported mandatory unionization for subcontractors. LaCombe's correspondence on behalf of the Port has been thoroughly discussed *supra*. Plaintiff also produced evidence that representations had been made to the union by Host that they would work toward the unionization of the DBEs.<sup>7</sup> Plaintiff has satisfied its burden of raising disputed issues of material fact regarding proof of the elements of a civil conspiracy involving Defendant Host.

Finally, the union contests FEE's proof of a "conspiracy" between HERE, Host [\*46] and the Port. Their argument concerning the CBA has already been analyzed *supra*. As discussed above, the Court will not declare Article 2.01 of the CBA a legally-protected "work preservation clause" as a matter of law. FEE has produced sufficient facts to permit the issue of whether 2.01 was understood by the defendants to require subcontractor unionization to go to a jury.

HERE also maintains that no evidence supports Plaintiff's contention that the MOU was part of some larger conspiracy between these three entities and that Plaintiff has submitted no evidence of other communications between all the defendants (much less any agreements between them) concerning FEE's attempts to renew its lease. But it has already been established as a matter of law that Exhibit A of the MOU (with its mandatory LHP requirement) could be applied to Tier I concessionaires such as Plaintiff; indeed, it is apparent that Defendant Host did apply such a requirement, as reflected in its communications to FEE through the LOI.<sup>8</sup>

[\*47] The union argues that, even if a LHP was a prerequisite to lease renewal, it was not synonymous with "mandatory unionization" and that the elements of the plan, listed at the end of Exhibit A, support this position. This argument is greatly weakened, however, by apparent contradiction represented by union president Sawyer (who signed the MOU containing the LHP requirement) telling Elmer that he was unaware of any LHP requirement (Elmer Decl. P 13) and didn't consider it "appropriate" to discuss with her. Noble Decl. F, Sawyer Dep. p. 129. Although Elmer reported immediately after this meeting that she now believed there was no unionization requirement (Decl. of Natarajan, P 14, Exh. F), she later came to believe that in fact Sawyer had been deceptive in his responses to her. The Court does not weigh evidence at this stage of the proceedings, but it is appropriate to determine if Plaintiff has established a genuine issue for trial, and the inconsistency between Sawyer's participation

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<sup>7</sup> From contemporaneous notes taken by a union official during negotiations between Host and HERE, union official Sawyer is quoted as saying "Art [Spring, of Host] made commitment that attorneys would work together to develop language that would bind all HMS and DBEs to be unionized." Noble Decl. E, p.36, Pltf Exh. 119.

<sup>8</sup> The August 27, 2003 LOI from Host to FEE stated:

Host is prepared to offer you the opportunity to continue operation of a coffee concession . . . subject to the execution of a new sublease agreement for your location, which sublease will include the following terms and conditions:

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. A Labor Harmony Plan. . . . Your Labor Harmony Plan is to contain a statement as to whether HERE Local 8 is in agreement with your plan. Pltf Exh. 42, HOST0000138.

in the drafting of the MOU and his representations to Elmer could lead a jury to infer the existence of an agreement to freeze FEE out of the re-leasing process based on Plaintiff's resistance to unionizing.

[\*48] Proof of a conspiracy will rarely be achieved through direct evidence, and Plaintiff is entitled to establish its case circumstantially. *Gilbrook v. Westminster*, 177 F.3d 839, 856-57 (9th Cir. 1999). The circumstances established by Plaintiff's evidence are that HERE and the Port entered into a MOU which required the submission of LHPs by the sublessees of any concessionaire at the facility; that Host and HERE entered into a CBA which required Host to sublease out work "customarily performed" by union labor only to employers covered by the agreement; and that Host then told Plaintiff it would not receive a new lease unless it submitted a union-approved LHP.

The point is not that Plaintiff has produced enough evidence to win a summary judgment motion of its own or to prevail at trial. FEE's burden in responding to these summary judgment motions is to produce evidence sufficient to raise a genuine dispute of material fact. A jury hearing this evidence (and the evidence of the other statements by representatives of defendants regarding mandatory unionization) could reasonably infer that there had been a meeting of the minds between all three Defendants that all sublessees [\*49] would have to agree to join the union and that the vehicle for accomplishing that agreement would be the LHP. The Court must view the evidence produced in the light most favorable to Plaintiff, and the evidence produced suffices to create disputed material issues of proof on the civil conspiracy cause of action. On that basis, summary judgment must be DENIED.

The Court also DENIES summary judgment as to:

#### **Unfair Labor Practices (Third Cause of Action)**

This cause of action is directed only against the union and alleges violations of two sections of the National Labor Relations Act ("NLRA"), 29 U.S.C. § 158 et seq.: HN25 [↑] § 8(b)(4)(ii)(B), which bars unions from "forcing or requiring any person . . . to cease doing business with any other person; and HN26 [↑] § 8(e), which defines as an unfair labor practice "any contract or agreement, express or implied" between a union and an employer "to cease doing business with any other person." HN27 [↑] Both of these provisions are aimed at the practice of "secondary boycotts," whereby a union can apply pressure on one (non-union) employer through the union's relationship with another (union) employer. Violations of 8(b)(4) cover [\*50] a wide range of actions but require some proof of coercion (*Shepard v. NLRB*, 459 U.S. 344, 351, 103 S. Ct. 665, 74 L. Ed. 2d 523 (1983)), while 8(e) is aimed at "hot cargo agreements" wherein a union and employer enter into an agreement that the employer will not do business with a second employer whom the union considers to be unfair to organized labor. *Betal Environmental Corp. v. Local Union No. 78*, 123 F. Supp. 2d 156, 158, fn. 2 (S.D.N.Y. 2000) (citations omitted).

The union's arguments regarding "work preservation clauses" and the Noerr-Pennington doctrine appear to be addressed to both its alleged participation in the conspiracy to violate Plaintiff's federal rights and its alleged violations of the NLRA. The Court's analysis of those arguments *supra* will not be repeated here, but that analysis requires denial of the union's summary judgement motion as it applies to the 8(b)(4) and 8(e) claims as well.

The union makes the additional argument, aimed at FEE's 8(b)(4) claim, that there is no evidence of "coercion" to sustain that violation. But HN28 [↑] the term "coerce" extends to "any form of economic pressure of a compelling or restraining nature" (*Association of General Contractors of Calif., Inc. v. NLRB*, 514 F.2d 433, 438-39 (9th Cir. 1975)) [\*51] and the MOU contains unmistakable language that "[f]ailure by a concessionaire or any of its sublessees" to implement a LHP "will be deemed a breach of the Contract, which will subject the Concessionaire to termination of the Contract with the Port." Pltf Exh. 29, UNION 002460. A jury could reasonably infer, from this and other evidence produced by FEE, that this constituted "economic pressure of a compelling . . . nature." Further, statements by union officials regarding a "campaign of escalating actions" and "a lot more coming" also combine to create a genuine issue for trial regarding the existence of "coercion" in the union's statements and actions.

The union's request for summary judgment of dismissal of the claims of NLRA violations will be denied.

Summary judgment will likewise be DENIED regarding:

### **Tortious Interference With Business Expectancy (Eighth Cause of Action)**

Plaintiff alleges this cause of action against the Port and HERE. [HN29](#)[] There are five elements to establishing this cause of action: (1) a valid contract or business expectancy; (2) of which the Port and HERE had knowledge; (3) an intentional interference inducing or causing a breach of the contract [\*52] or expectancy; (4) existence of an improper motive or use of an improper means in the interference; (5) resulting in damages. [Leingang v. Pierce Co. Med Bureau, Inc.](#), 131 Wn.2d 133, 157, 930 P.2d 288 (1997).

Plaintiff has brought forward evidence sufficient to create genuine disputes of material fact on all of these elements and is entitled to go forward with this claim. [HN30](#)[] "A valid business expectancy includes any prospective contractual or business relationship that would be of pecuniary value." [Newton Insurance Agency & Brokerage, Inc. v. Caledonian Insurance Group, Inc.](#), 114 Wn. App. 151, 158, 52 P.3d 30 (2002). Certainly FEE's negotiations with Host regarding renewal of its lease constituted a "prospective contractual or business relationship," and neither the Port nor HERE have disputed that they were aware that the negotiations were taking place and that Plaintiff was seeking a new lease to continue its business at the airport.

The existence of "intentional interference inducing or causing a breach of . . . the expectancy" arising out of "an improper motive or use of an improper means" parallels Plaintiff's allegations regarding the existence of a conspiracy. The analysis [\*53] of Defendants' motions for summary judgment on the conspiracy cause of action also suffices regarding their request for dismissal of this claim. Sufficient evidence has been adduced to create genuine issues of material fact regarding whether the Port and HERE interfered for an improper motive or using improper means with FEE's business expectancy in a new airport lease. Neither of those defendants has challenged the adequacy of Plaintiff's pleading of damages arising out of these facts.

The motion for summary judgment on Plaintiff's eighth cause of action will be DENIED.

Finally, the Court DENIES summary judgment on:

### **42 U.S.C. § 1983/Violation of Plaintiff's Federally Protected NLRA Rights (Ninth Cause of Action)**

All Defendants have sought dismissal of this cause of action, which was added by amendment rather late in the case. For reasons largely explored under the analysis of the summary judgment motions on the civil conspiracy claim, this portion of the motion will be denied as to all Defendants as well.

[HN31](#)[] The elements of a [§ 1983](#) claim are: (1) that the conduct complained of was committed by a person acting under color of state law; [\*54] and (2) that the conduct deprived a person of rights, privileges, or immunities secured by the Constitution or laws of the United States.

[Johnson v. Hawe](#), 388 F.3d 676, 681 (9th Cir. 2004) (quoting [Alford v. Haner](#), 333 F.3d 972, 975-76 (9th Cir. 2003)). [HN32](#)[] The "state actor" component can be established by showing that a private person conspired with a local governmental official. See, e.g., [Adickes v. Kress & Co.](#), 398 U.S. 144, 90 S. Ct. 1598, 26 L. Ed. 2d 142 (1970).

The Port satisfies the "state actor" requirement by virtue of being a municipal governmental entity. For the same reasons that neither of the private defendants are entitled to summary judgment on Plaintiff's civil conspiracy cause of action, the Court finds that Plaintiff has sufficiently established disputed issues of material fact regarding whether Host and HERE conspired with the Port to satisfy this element of its [§ 1983](#) claim for summary judgment purposes. [HN33](#)[] "A defendant's knowledge of and participation in a conspiracy may be inferred from circumstantial evidence from evidence of the defendant's actions." [Gilbrook v. City of Westminster](#), 177 F.3d 839, 856-57 (9th Cir. 1999). [\*55]

Regarding the deprivation of "rights . . . secured by the Constitution or laws of the United States" required for proof of the second element of [§ 1983](#), the Court finds that, as regards Plaintiff, those rights are represented by the protections afforded under the NLRA. Plaintiff has a right to operate free from "hot cargo" agreements and any

other activities or conspiracies aimed at conditioning its continued operation on involuntary unionization, and, under certain circumstances (which have been found here), [§ 1983](#) represents a bulwark against that kind of activity.

Defendants reiterate many of their previous arguments regarding the legality of the MOU and the CBA and the lack of other circumstantial evidence demonstrating their intent to trespass on FEE's federally-protected rights under the NLRA. The analysis of those arguments will not be repeated here; for the same reasons this Court found that Plaintiff has established the existence of genuine issues for trial on the allegations of civil conspiracy to violate its rights, Plaintiff has also shown that disputed issues of material fact remain concerning its allegations of [§ 1983](#) violations. Even if the documents at the heart [\*56] of this case are ultimately found to either not apply to Plaintiff or not to contain explicit or implicit unionization requirements for airport sublessees, there remains sufficient evidence of oral and written statements by representatives of all defendants to create genuine factual disputes regarding whether these Defendants supported the forced, illegal unionization of this Plaintiff.

The union, however, does approach its summary judgment request on this claim from a different angle. To the extent that the [§ 1983](#) claim is premised on the illegality of the CBA between Host and the union, HERE argues the NLRA preempts use of any other remedy, except in very limited circumstances which HERE alleges are not present. HERE claims that Plaintiff's claims regarding the CBA are premised exclusively on [§ 8\(e\) of the NLRA](#) (HERE's [§ 1983](#) Motion, p. 7) and cites case law that [8\(e\)](#) allegations are outside a federal court's Taft-Hartley Act jurisdiction. [Atchison, Topeka & Santa Fe RR v. Teamsters Local 70, 511 F.2d 1193, 1195 \(9th Cir. 1975\)](#). Thus, the argument concludes, the sole remedy is a claim with the National Labor Relations Board ("NLRB").

The union does not entirely [\*57] ignore the fact that Plaintiff has also alleged [§ 8\(b\)\(4\)](#) violations against them (which is one of the exceptions to exclusive NLRA jurisdiction), but tries to argue that the fact that Plaintiff was not a party to the CBA means they cannot assert an [8\(b\)\(4\)](#) violation as regards that agreement. It is not a compelling argument -- the case they cite in support of it ([Betal Environmental Corp. v. Local No. 78, 123 F. Supp. 2d 156 \(S.D.N.Y. 2000\)](#)) was also dependent on a finding that the Plaintiff there had presented no evidence that it had been forced or required to unionize. That is hardly the case here -- as pointed out previously, there are many areas of disputed material fact regarding the issue of mandatory unionization

The union claims further preemption in the form of the exclusivity of § 303 of the Labor Management Relations (Taft-Hartley) Act, [29 U.S.C. § 187](#). They cite [Teamsters v. Morton, 377 U.S. 252, 258-60, 84 S. Ct. 1253, 12 L. Ed. 2d 280 \(1964\)](#) for the holding that the congressional intent behind § 303 bars any non-NLRA remedies. They argue by analogy that the case law which prohibits punitive damages, attorneys' fees ([Summit Valley Industries v. Carpenters Local 112, 456 U.S. 717, 723-24, 102 S. Ct. 2112, 72 L. Ed. 2d 511 \(1982\)](#)) [\*58] and [§ 1985](#) violations ([Amoco Oil Co. v. Electrical Workers Local 99, 536 F.Supp. 1203, 1217-19 \(D.R.I. 1982\)](#)) also acts to bar relief under [§ 1983](#).

The Court finds none of the union's "exclusivity" arguments persuasive. Plaintiff's claims against them are premised on violations of [8\(b\)\(4\)](#) as well as [8\(e\)](#) and as such are exempt from the exclusive jurisdiction of the NLRB. [HN34](#)[<sup>1</sup>] Congress gave parties with allegations of [8\(b\)\(4\)](#) violations the right to sue a union for damages "in any district court of the United States." [29 U.S.C. § 187\(b\)](#). Plaintiff cites Supreme Court case law which holds that [HN35](#)[<sup>1</sup>] the NLRA does not preclude a [§ 1983](#) action arising from government interference with federally-protected labor rights. [Golden State Transit Corp. v. City of Los Angeles, 493 U.S. 103, 108-09, 110 S. Ct. 444, 107 L. Ed. 2d 420 \(1989\)](#). Further, [HN36](#)[<sup>1</sup>] private parties may be liable under [§ 1983](#) when they join with government entities to interfere with federally-protected rights. [Dennis v. Sparks, 449 U.S. 24, 27-29, 101 S. Ct. 183, 66 L. Ed. 2d 185 \(1980\)](#).

[Golden State, supra](#), also holds that [HN37](#)[<sup>1</sup>] the burden is on the union to establish that [§ 1983](#) protection has been withdrawn for [\*59] violation of a particular federal right. [493 U.S. at 107](#). None of the union's cases involve a holding that § 303 is the exclusive remedy which pre-empts [§ 1983](#) in cases where [8\(b\)\(4\)](#) violations are alleged. A recent District Court opinion from this circuit states:

[S]ection 303 has scant legislative history. The little historical guidance that does exist fails to indicate any Congressional intent that sections 8(b)(4) and 303 be the exclusive remedy for persons injured by secondary labor activities.

Sutter Health v. UNITE HERE, F. Supp. 2d , 2005 U.S. Dist. LEXIS 20892, 2005 WL 1925910, \*5 (E.D.Cal. Aug. 10, 2005).

It is the finding of this Court that Plaintiff has established sufficient disputed facts regarding violations of its rights under § 1983 to withstand summary judgment on that cause of action. None of Defendants' arguments that they are entitled to summary judgment as a matter of law has succeeded in persuading the Court that a jury should not hear and decide this matter.

As regards Plaintiff's final cause of action:

#### **Contempt of Court (Tenth Cause of Action)**

This allegation is made against the Port only and concerns [\*60] Plaintiff's assertion that the Port's activities in the circumstances at issue in this case violate the terms of the injunction issued by Judge Rothstein in Citylce, *supra*. The Order and Consent which contain the injunction state:

Court's Continuing Jurisdiction to Adjudicate Any Disputes Regarding This Consent Judgment. The Court hereby RETAINS JURISDICTION over the parties for the purposes of deciding any disputes or issues regarding the interpretation or application of, or compliance with, this Consent Judgment. Any such disputes or issues must be adjudicated in this Court, and only in this Court. Consent and Order, p. 5.

Defendant's motion for summary judgment on this claim will be DENIED at this stage of the proceeding to permit a referral of this claim to Judge Rothstein to permit her to determine whether she wishes to retain jurisdiction over this particular dispute concerning the application of the injunction.

#### **Conclusion**

Summary judgment will be GRANTED on Plaintiff's claims of violations of the Washington anti-trust laws and Consumer Protection Act. Summary judgment will be DENIED as to the following causes of action, which remain active [\*61] in the case:

- . Civil conspiracy under Washington state law (as to all Defendants)
- . Violations of 42 U.S.C. § 1983 (as to all Defendants)
- . Violations of the National Labor Relations Act, 29 U.S.C. §§ 158(b)(4) and (e) (as to Defendant HERE only)
- . Allegations of tortious interference with a business expectancy (as to Defendants the Port of Seattle and HERE only).

Plaintiff's cause of action for contempt against the Port will be referred to Judge Barbara J. Rothstein for a determination of whether she wishes to retain jurisdiction over this particular application of her previous order.

The clerk is directed to provide copies of this order to all counsel of record.

Dated: September 21, 2005

Marsha J. Pechman

United States District Judge



## Howard Hess Dental Labs. Inc. v. Dentsply Int'l, Inc.

United States Court of Appeals for the Third Circuit

April 7, 2005, Argued ; September 21, 2005, Filed

No. 04-1979, No. 04-1980

### **Reporter**

424 F.3d 363 \*; 2005 U.S. App. LEXIS 20228 \*\*; 2005-2 Trade Cas. (CCH) P74,934

HOWARD HESS DENTAL LABORATORIES INCORPORATED; PHILIP GUTTIEREZ, \* d/b/a Dentures Plus, on behalf of themselves and all other similarly situated, Appellants v. DENTSPLY INTERNATIONAL, INC.; JERSEY DENTAL LABORATORIES, f/k/a Howard Hess Dental Laboratories Incorporated; PHILIP GUTTIEREZ, \* d/b/a Dentures Plus, on behalf of themselves and all others similarly situated, Appellants v. DENTSPLY INTERNATIONAL, INC.; A. LEVENTHAL & SONS, INC.; ACCUBITE DENTAL LAB, INC.; ADDIUM DENTAL PRODUCTS; ARNOLD DENTAL SUPPLY COMPANY; ATLANTA DENTAL SUPPLY COMPANY; BENCO DENTAL COMPANY; BURKHART DENTAL SUPPLY COMPANY; DARBY DENTAL LABORATORY SUPPLY CO., INC.; DENTAL SUPPLIES AND EQUIPMENT, INC.; EDENTALDIRECT.COM, INC., as successor to Crutcher Dental, Inc.; HENDON DENTAL SUPPLY, INC.; HENRY SCHEIN, INC., and its affiliates including, without limitation, Zahn Dental Co., Inc.; IOWA DENTAL SUPPLY CO.; JAHN DENTAL SUPPLY COMPANY; JB DENTAL SUPPLY CO., INC.; JOHNSON & LUND CO., INC.; KENTUCKY DENTAL SUPPLY COMPANY, INC. a/k/a KDSC Liquidation Corp.; MARCUS DENTAL SUPPLY CO; MIDWAY DENTAL SUPPLY INC.; MOHAWK DENTAL CO., INC.; NASHVILLE DENTAL, INC.; NOWAK DENTAL SUPPLIES, INC.; PATTERSON DENTAL COMPANY, its subsidiaries, predecessors, successors, assigns, affiliates and related companies; PEARSON DENTAL SUPPLIES, INC.; RYKER DENTAL OF KENTUCKY, INC.; THOMPSON DENTAL COMPANY

**Subsequent History:** As Amended, October 4, 2005.

As Amended, December 1, 2005.

Amended by [Howard Hess Dental Labs., Inc. v. Dentsply Int'l, Inc., 2005 U.S. App. LEXIS 21445 \(3d Cir. Del., Oct. 4, 2005\)](#)

US Supreme Court certiorari denied by *Jersey Dental Labs. v. Dentsply Int'l, Inc.*, 547 U.S. 1163, 126 S. Ct. 2320, 164 L. Ed. 2d 839, 2006 U.S. LEXIS 4170 (May 30, 2006)

Transferred by [Nowak Dental Supplies v. Dentsply Int'l, 2008 U.S. Dist. LEXIS 144008 \(M.D. Pa., Aug. 4, 2008\)](#)

**Prior History:** [\*\*1] On Appeal from the United States District Court for the District of Delaware. (D.C. Civil Action Nos. 99-cv-00255 / 01-cv-00267). District Judge: Honorable Sue L. Robinson.

[Jersey Dental Labs. v. Dentsply Int'l, Inc., 2002 U.S. Dist. LEXIS 17018 \(D. Del., Aug. 27, 2002\)](#)

## **Core Terms**

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dealers, purchasers, overcharge, damages, co-conspirator, conspiracy, lost profits, indirect, teeth, antitrust, Dental, recover damages, anti trust law, duplicative, involvement, labs, drop, exclusive-dealing, competitors', manufacturer,

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\* Amended per Clerk's Order dated 4/30/04

price-fixing, middlemen, conspired, seller, resale price, Plaintiffs', decreasing, parties, shipped, measure of damages

## LexisNexis® Headnotes

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Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Regulated Practices > Private Actions > Prioritizing Resources & Organization for Intellectual Property Act

### **HN1** [down arrow] **Private Actions, Purchasers**

See [15 U.S.C.S. § 15\(a\)](#).

Antitrust & Trade Law > ... > Private Actions > Standing > Clayton Act

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > Remedies > Damages

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

Civil Procedure > ... > Justiciability > Standing > General Overview

### **HN2** [down arrow] **Standing, Clayton Act**

Direct purchasers are the only parties "injured" in a manner that permits them to recover damages under § 4 of the Clayton Act, [15 U.S.C.S. § 15\(a\)](#). Indirect purchaser plaintiffs do not have statutory standing to recover damages under [§ 15\(a\)](#).

Civil Procedure > Appeals > Appellate Jurisdiction > Certified Questions

Civil Procedure > Appeals > Appellate Jurisdiction > Interlocutory Orders

### **HN3** [down arrow] **Appellate Jurisdiction, Certified Questions**

In a [28 U.S.C.S. § 1292\(b\)](#) appeal, the appellate court's review is not limited to the specific question certified by the district court. The appellate court may consider all grounds which might require a reversal of the order appealed from. It may address any issue fairly included within the certified order because it is the order that is appealable, and not the controlling question identified by the district court.

Civil Procedure > Judgments > Relief From Judgments > Altering & Amending Judgments

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

Civil Procedure > Appeals > Standards of Review > De Novo Review

#### [HN4](#) **Relief From Judgments, Altering & Amending Judgments**

Where the district court has based its decision to deny leave to amend on a legal conclusion that the amended pleading would not withstand a motion to dismiss, the appellate court reviews such a decision de novo.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

#### [HN5](#) **Purchasers, Direct Purchasers**

The general rule is that only direct purchasers from antitrust violators may recover damages in antitrust suits.

Antitrust & Trade Law > ... > Private Actions > Standing > Clayton Act

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

#### [HN6](#) **Standing, Clayton Act**

Courts have rejected attempts to invoke a coconspirator exception to the bar on indirect purchaser standing under § 4 of the Clayton Act, [15 U.S.C.S. § 15\(a\)](#) when the plaintiffs have not named the coconspirators immediately upstream as defendants.

Contracts Law > Third Parties > Beneficiaries > Claims & Enforcement

Contracts Law > Third Parties > Beneficiaries > General Overview

Contracts Law > ... > Beneficiaries > Types of Third Party Beneficiaries > General Overview

Contracts Law > ... > Beneficiaries > Types of Third Party Beneficiaries > Intended Beneficiaries

## **HN7** Beneficiaries, Claims & Enforcement

Only intended beneficiaries of a contract made between two or more other parties have enforceable rights under the contract.

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

## **HN8** Private Actions, Purchasers

The United States Supreme Court has rejected the assertion that the absence of a particular Illinois Brick concern in an individual case would remove its bar on an indirect purchaser claim under § 4 of the Clayton Act, [15 U.S.C.S. § 15\(a\)](#).

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Mergers & Acquisitions Law > Antitrust > Interlocking Directorates

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

## **HN9** Purchasers, Direct Purchasers

The "control exception" to Illinois Brick "might" permit an indirect purchaser to sue an initial seller under § 4 of the Clayton Act, [15 U.S.C.S. § 15\(a\)](#), when the initial seller owns or controls the direct purchaser. The United States Court of Appeals for the Third Circuit has applied the control exception only when the initial seller owns the direct purchaser. Courts that have extended the control exception beyond a parent-subsidiary relationship still require relationships involving such functional economic or other unity between the direct purchaser and either the defendant or the indirect purchaser that there effectively has been only one sale. Modes of control that might qualify for the control exception include interlocking directorates, minority stock ownership, loan agreements that subject the wholesalers to the manufacturers' operating control, or trust agreements.

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > General Overview

Business & Corporate Compliance > ... > Types of Damages > Consequential Damages > General Overview

Antitrust & Trade Law > ... > Monopolies & Monopolization > Actual Monopolization > General Overview

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Business & Corporate Compliance > ... > Seller's Damages & Remedies > Limitation & Modification > General Overview

#### **HN10** [ ] Price Fixing & Restraints of Trade, Exclusive & Reciprocal Dealing

When antitrust violators cause prices to increase through monopolization, a price-fixing conspiracy, or exclusionary conduct, the harm they cause members of the distribution chain comes in two ways: (1) overcharges paid for goods actually purchased; and (2) lost profits resulting from the lost opportunity to buy and resell a greater volume of goods.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Business & Corporate Compliance > ... > Types of Damages > Consequential Damages > General Overview

Business & Corporate Compliance > ... > Types of Commercial Transactions > Sales of Goods > General Overview

Business & Corporate Compliance > ... > Sales of Goods > Remedies > General Overview

#### **HN11** [ ] Private Actions, Remedies

When antitrust plaintiffs claim that anticompetitive behavior caused prices to increase, two measures of damages can theoretically be used: (1) the overcharge (i.e., the difference between the price paid for goods actually purchased and the price that would have been paid absent the illegal conduct), or (2) lost profits (i.e., the overcharge paid minus the overcharge passed on for goods actually purchased and resold, plus lost profits from the lost opportunity to buy and resell a greater volume of goods). A court might potentially use a lost profits measure of damages, as the United States Supreme Court has not explicitly held that any particular measure of damages is required or precluded. However, the standard method of measuring damages in price enhancement cases is overcharge, not lost profits.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

#### **HN12** [ ] Private Actions, Remedies

Lost profits damages are disfavored in antitrust actions, at least in part because they are more difficult to prove than overcharge damages. Furthermore, overcharge damages, unlike lost profits, may induce antitrust plaintiffs to make arguments that will protect rather than injure consumers.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

#### **HN13** [ ] Private Actions, Remedies

If a cartel sells to an intermediate purchaser who resells to another, both purchasers are likely to lose profits as a result of the price fix, but under the Illinois Brick rule, the second intermediate purchaser, or the indirect purchaser from the cartel, cannot recover damages.

[Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview](#)

[Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > Elements](#)

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

#### **[HN14](#) [blue icon] **Private Actions, Purchasers****

The United States Court of Appeals for the Third Circuit has expressly refused to adopt a coconspirator exception to the antitrust law Illinois Brick rule when the alleged co-conspirators immediately upstream have not been joined.

[Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview](#)

[Contracts Law > Defenses > Illegal Bargains](#)

[Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview](#)

#### **[HN15](#) [blue icon] **Private Actions, Purchasers****

Illinois Brick does not limit suits by consumers against a manufacturer who illegally contracted with its dealers to set the latter's resale price. There is no problem of duplication or apportionment, because the consumer is the only party who has paid any overcharge. The court simply computes the retail price that would have prevailed absent the illegal contract fixing the price. Lost profits damages for the intermediary and overcharge damages for the consumer are not in any way duplicative; they are both losses caused by the unlawful resale price maintenance.

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Exclusive & Reciprocal Dealing > General Overview](#)

[Criminal Law & Procedure > ... > Inchoate Crimes > Conspiracy > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview](#)

[Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > Resale Price Maintenance](#)

[Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview](#)

#### **[HN16](#) [blue icon] **Price Fixing & Restraints of Trade, Exclusive & Reciprocal Dealing****

There is, in addition to a co-conspirator exception for resale price maintenance (RPM, i.e., vertical price-fixing) conspiracies, a co-conspirator exception for non-RPM conspiracies, such as exclusive-dealing or price-fixing at the manufacturer level (the general co-conspirator exception). The United States Court of Appeals for the Third Circuit holds that such an exception would only exist in circumstances where the middlemen would be barred from bringing a claim against their former co-conspirator--the manufacturer--because their involvement in the conspiracy was

"truly complete" (i.e., if the middlemen would be barred from suing by the complete involvement defense of a manufacturer).

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Vertical Restraints > General Overview

Civil Procedure > ... > Summary Judgment > Entitlement as Matter of Law > General Overview

Antitrust & Trade Law > ... > Price Fixing & Restraints of Trade > Cartels & Horizontal Restraints > General Overview

## **HN17** [ ] Price Fixing & Restraints of Trade, Vertical Restraints

Summary judgment for a defendant is proper, even if there is some evidence of an antitrust violation, if the plaintiff's theory of violation makes no economic sense.

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > Clayton Act > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > Indirect Purchasers

## **HN18** [ ] Private Actions, Remedies

An antitrust plaintiff (whether he be a direct or an indirect purchaser) is only entitled to recover "threefold the damages by him sustained." [15 U.S.C.S. § 15\(a\)](#). Therefore, to the extent that the middleman retained (i.e., did not pass on to the indirect purchaser) a portion of any overcharge imposed upon him, the damages actually sustained by the indirect purchaser would be reduced by that amount.

Civil Procedure > Remedies > Damages > General Overview

## **HN19** [ ] Remedies, Damages

Injured parties cannot be penalized and left without recourse because measurement of their damages is difficult.

Antitrust & Trade Law > ... > Private Actions > Purchasers > Direct Purchasers

Antitrust & Trade Law > ... > Private Actions > Remedies > General Overview

Antitrust & Trade Law > ... > Private Actions > Purchasers > General Overview

## **HN20** [ ] Purchasers, Direct Purchasers

The United States Court of Appeals for the Third Circuit is unwilling to hold that if initial sellers and "completely involved" direct purchasers conspire, then no plaintiff outside the conspiracy may sue the initial seller for damages in an antitrust case.

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**Judges:** Before: BARRY, AMBRO and GREENBERG, Circuit Judges.

**Opinion by:** AMBRO

## Opinion

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### [\*366] OPINION OF THE COURT

AMBRO, Circuit Judge

We consider consolidated appeals involving the same parties in two antitrust suits, *Howard Hess Dental Laboratories, Inc. v. Dentsply International, Inc.* ("Hess [\*2]") and *Jersey Dental Laboratories v. Dentsply International, Inc.* ("Jersey Dental").<sup>1</sup> Plaintiffs are dental laboratories who have brought these antitrust class actions on behalf of themselves and a class of similarly situated labs. Defendant Dentsply International, Inc. ("Dentsply") markets artificial teeth used by the dental labs to make dentures. Plaintiffs allege, among other things, an exclusive-dealing conspiracy and a retail price-fixing conspiracy among Dentsply and its dealer-middlemen.

The District Court denied Plaintiffs standing to recover damages in both suits based primarily on *Illinois Brick Co. v. Illinois*, 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 (1977), which held that indirect purchaser plaintiffs do not have statutory standing to recover damages for "passed-on" overcharges.<sup>2</sup> We hold that Plaintiffs may not recover damages in *Hess* (a) under the "co-conspirator" exception to *Illinois* [\*3] *Brick*, (b) under the "control" exception to *Illinois Brick*, (c) under a non-overcharge theory of damages, or (d) for "drop shipments." While Plaintiffs may not recover damages under either the control exception or a lost profits theory in *Jersey Dental*, they do have statutory standing under the co-conspirator exception to pursue an action for overcharge damages (including for drop shipped teeth) caused by the alleged retail price-fixing conspiracy, although not for the alleged exclusive-dealing conspiracy.

### [\*\*4] Background

Plaintiffs allege the following in one or both of the complaints.

[\*367] (1) Manufacturers of artificial teeth need to distribute through dealers in order to compete effectively. Dealers are the primary source of distribution to dental labs, which use the teeth to produce dentures. Dentsply uses a network of authorized dealers.

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<sup>1</sup> Hess Dental changed its name to "Jersey Dental" during the period between the two suits.

<sup>2</sup> Section 4 of the Clayton Act provides that HN1 "any person who shall be *injured* in his business or property by reason of anything forbidden in the antitrust laws . . . shall recover threefold the damages by him sustained." 15 U.S.C. § 15(a) (emphasis added). *Illinois Brick* determined that HN2 direct purchasers are the only parties "injured" in a manner that permits them to recover damages. 431 U.S. at 729, 735. It thus held that indirect purchaser plaintiffs do not have statutory standing to recover damages under Section 4 of the Clayton Act. *Id.*

(2) Plaintiffs have purchased Dentsply's teeth both indirectly through Dentsply's dealers and directly through "drop shipping." Drop shipping occurs when a dealer does not have certain teeth in stock or cannot fulfill a lab's order for some other reason and asks Dentsply to ship the teeth directly to a lab. When teeth are drop shipped, the dealer never has physical custody of them, but it does bill the lab for the teeth, collect payments from the lab, and pay Dentsply.

(3) Dentsply has foreclosed its competitors' access to dealers by explicitly agreeing with some dealers that they will not carry certain competing brands of teeth and by inducing other dealers not to carry those competing brands of teeth. Pursuant to its written policy called "Dealer Criterion Number 6," Dentsply threatens to terminate, and does terminate, dealers that add to their **[\*\*5]** inventory teeth made by Dentsply's competitors. Thus, unless Dentsply's dealers were already selling another manufacturer's teeth before Dentsply imposed its exclusive-dealing policies, its dealers cannot sell other manufacturers' teeth unless they give up the opportunity to continue to sell Dentsply's teeth. No rational dealer would be likely to make such a switch because, given Dentsply's monopoly position (it has a 75-80% market share on a revenue basis), losing the ability to sell Dentsply's teeth would hurt a dealer more than gaining the ability to sell Dentsply's competitors' teeth would help a dealer. By explicitly agreeing with some dealers that they will not carry certain competing brands of teeth and by enacting Dealer Criterion Number 6, Dentsply has foreclosed its rivals' access to adequate channels of distribution, and competition has been restricted. This has caused Dentsply's market share to increase, the price of Dentsply's and other manufacturers' teeth to increase, and the availability of rival teeth to decrease.

(4) Furthermore, by agreement among Dentsply and its dealers, Dentsply sets the dealers' resale prices. It distributes a list of "suggested" prices for **[\*\*6]** its dealers to charge dental labs. Before a dealer can charge a lower price, Dentsply must approve this "price deviation." Price deviations have been granted only when a lab has been buying, or is thinking of buying, a competitor's teeth because they are being sold for less than those of Dentsply. In those instances, Dentsply negotiates with the lab to allow it to buy teeth from the dealer at a price below Dentsply's suggested price. The dealer then agrees to the price negotiated by Dentsply.

(5) Dentsply's foreclosing of its competitors' access to dealers and setting of the dealers' resale prices have caused Plaintiffs to purchase Dentsply's teeth at artificially high prices and lose profits from unrealized sales of Dentsply's competitors' teeth.

## Procedural History

In 1999, Plaintiffs filed the *Hess* suit against Dentsply alleging conspiracy to monopolize, attempt to monopolize, and maintenance of monopoly in violation of Section 2 of the Sherman Act, [15 U.S.C. § 2](#), and restraint of trade in violation of Section 3 of the Clayton Act, [15 U.S.C. § 14](#). Plaintiffs asked for both damages and an injunction. Dentsply moved for summary **[\*\*7]** judgment, claiming that Plaintiffs lacked standing under *Illinois Brick*. The District Court granted Dentsply's motion on Plaintiffs' damages claims. The **[\*368]** Court reasoned that: (1) a co-conspirator exception to *Illinois Brick* did not apply because Plaintiffs had not joined Dentsply's dealers as codefendants; (2) the control exception to *Illinois Brick* did not apply because Dentsply does not own its dealers; (3) Plaintiffs could not recover on a non-overcharge theory of damages because they had not articulated any such theory; and (4) Plaintiffs could not recover for drop shipments because they had specifically alleged that they were not direct purchasers, and even if they had alleged they were direct purchasers, they were indirect purchasers of drop shipments.

In 2001, Plaintiffs filed the *Jersey Dental* suit, this time naming as Dentsply's co-defendants twenty-six of its then twenty-eight authorized dealers. Plaintiffs made substantially the same allegations as they did in *Hess* with one key addition: they claimed they were not only indirect purchasers but also direct purchasers. As in *Hess*, Plaintiffs asked for both damages and an injunction. Dentsply moved under **[\*\*8]** [Federal Rule of Civil Procedure 12\(b\)\(6\)](#) to dismiss the claims for damages, citing *Illinois Brick*. The District Court granted the motion. The Court reasoned that: (1) Plaintiffs could not recover under a coconspirator exception to *Illinois Brick* because the suit still implicated *Illinois Brick's* policy concerns; (2) in *Hess* it had already rejected Plaintiffs' argument that they could recover under the control exception to *Illinois Brick*; (3) Plaintiffs could not recover damages for lost profits because their complaint

sought only overcharge damages and because, as Plaintiffs were indirect purchasers, *Illinois Brick* would bar recovery of lost profits anyway; and (4) in *Hess* it had already rejected Plaintiffs' argument that they could recover for drop shipped teeth.

Plaintiffs then moved for leave to amend their complaint. Among the proposed additions to the complaint were allegations that "the Dealer Defendants agree with Dentsply and and with each other" to abide by suggested retail prices and that "the prices at which the Dealer Defendants sell to dental laboratories are controlled by Dentsply and agreed to by the [\*\*9] Dealer Defendants." The District Court denied leave to amend because the amended pleading would not withstand a motion to dismiss.

It reasoned that: (1) the co-conspirator exception to *Illinois Brick* did not apply because the dealers could still sue Dentsply; (2) the control exception to *Illinois Brick* did not apply because the dealers were not subsidiaries of Dentsply; and (3) *Illinois Brick* barred recovery of lost profits damages because Plaintiffs were indirect purchasers.

Plaintiffs moved pursuant to [28 U.S.C. § 1292\(b\)](#) for certification of appealability of the orders dismissing the damage claims in *Hess* and *Jersey Dental* and the order denying their motion for leave to amend in *Jersey Dental*. The District Court granted these motions and certified the following question:

Whether, under the circumstances here, application of [\*Illinois Brick\*, 431 U.S. 720, 52 L. Ed. 2d 707, 97 S. Ct. 2061 \(1977\), McCarthy v. Recordex Service, Inc., 80 F.3d 842 \(3d Cir. 1996\)](#), or other Third Circuit opinions dealing with *Illinois Brick*, prevents Plaintiffs from being able to recover damages against Dentsply International, [\*\*10] Inc.

Plaintiffs then petitioned our Court for permission to appeal, pursuant to [28 U.S.C. § 1292\(b\)](#), the three orders certified by the District Court. We granted the petition and consolidated the appeals. [HN3](#)<sup>1</sup> In a [Section 1292\(b\)](#) appeal, our review is not limited to the specific question certified by the District Court. We may "consider all grounds which might require a reversal of the order appealed from." [\*Merican, Inc. \[\\*369\] v. Caterpillar Tractor Co.\*, 713 F.2d 958, 962 n.7 \(3d Cir. 1983\)](#). We "may address any issue fairly included within the certified order because it is the order that is appealable, and not the controlling question identified by the District Court." [\*Yamaha Motor Corp., U.S.A. v. Calhoun\*, 516 U.S. 199, 205, 116 S. Ct. 619, 133 L. Ed. 2d 578 \(1996\)](#) (emphasis in original) (internal quotation marks omitted).<sup>3</sup>

## [[\*\*11] Standard of Review

As the *Hess* order partially granted Dentsply's motion for summary judgment, our review is *de novo*. [\*Mass. Sch. of Law at Andover, Inc. v. ABA\*, 107 F.3d 1026, 1032 \(3d Cir. 1997\)](#). The first *Jersey Dental* order granted Dentsply's motion to dismiss for failure to state a claim. Review of this order also merits *de novo* review. [\*Worldcom, Inc. v. Graphnet, Inc.\*, 343 F.3d 651, 653 \(3d Cir. 2003\)](#). The second *Jersey Dental* order denied Plaintiffs' motion for leave to amend the complaint on the ground that "the proposed amended complaint would not survive a motion to dismiss under [Fed. R. Civ. P. 12 \(b\)\(6\)](#)." Dist. Ct. Mem. Ord. at 7 (Aug. 27, 2002). [HN4](#)<sup>2</sup> Where, as here, "the District Court has based its decision to deny leave to amend on a legal conclusion that the amended pleading would not withstand a motion to dismiss, we review such a decision *de novo*." [\*Ziegler v. IBP Hog Mkt., Inc.\*, 249 F.3d 509, 518 \(6th Cir. 2001\)](#). Thus we review all three orders *de novo*.

## Discussion

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<sup>3</sup> We note that the Government has also sued Dentsply for alleged antitrust violations. See [\*United States v. Dentsply Int'l, Inc.\*, 399 F.3d 181 \(3d Cir. 2005\)](#). There we reversed the District Court's judgment in favor of Dentsply and granted injunctive relief. In so doing, we determined that Dentsply had monopoly power (*i.e.*, the power to exclude competitors) and that its exclusionary practices, particularly Dealer Criterion Number 6, had an anticompetitive effect. [\*Id. at 188-97\*](#).

*Illinois Brick* lays many of the markers for our decision. In that case, [\[\\*\\*12\]](#) the Supreme Court established [HN5](#) the general rule that only direct purchasers from antitrust violators may recover damages in antitrust suits. The plaintiffs alleged that concrete block manufacturers conspired to fix the prices at which concrete blocks were sold to masonry contractors. They in turn "passed on" overcharges to the general contractors, who then passed them on to the plaintiffs, who had purchased buildings made from the concrete block. The plaintiffs, therefore, were "indirect purchasers" of concrete block, which "passee[d]" through two separate levels in the chain of distribution before reaching them. [431 U.S. at 726](#).

Before the Court was whether the indirect purchaser plaintiffs could use this pass-on theory to state a damages claim against the alleged antitrust violators upstream. It had previously held that an antitrust defendant could not argue that a plaintiff who had purchased a product directly from the defendant was not injured because it had passed on the illegal overcharge to its own customers. [Hanover Shoe, Inc. v. United Shoe Mach. Corp., 392 U.S. 481, 494, 20 L. Ed. 2d 1231, 88 S. Ct. 2224 \(1968\)](#). To maintain consistency, the Court held in [\[\\*\\*13\]](#) *Illinois Brick* that direct purchasers are the only parties "injured" in a manner that permits them to recover damages. [431 U.S. at 729, 735](#). The indirect purchaser plaintiffs were thus ineligible to recover damages for the passed-on overcharges.

The Court gave three policy reasons for its holding: (1) a risk of duplicative liability for defendants and potentially inconsistent adjudications could arise if courts permitted both direct and indirect purchasers [\[\\*370\]](#) to sue defendants for the same overcharge; (2) the evidentiary complexities and uncertainties involved in ascertaining the portion of the overcharge that the direct purchasers had passed on to the various levels of indirect purchasers would place too great a burden on the courts; and (3) permitting direct and indirect purchasers to sue only for the amount of the overcharge they themselves absorbed and did not pass on would cause inefficient enforcement of the antitrust laws by diluting the ultimate recovery and thus decreasing the direct purchasers' incentive to sue. [Id. at 730-35 & nn.11-12, 737 & n.18, 740-43 & nn. 23, 27, 745](#).

## I. May Plaintiffs recover damages in *Hess* ?

### a. May [\[\\*\\*14\]](#) Plaintiffs recover damages in *Hess* under a co-conspirator exception to *Illinois Brick* ?

Although the *Hess* complaint alleged that Dentsply's dealers conspired with Dentsply by agreeing to the exclusive-dealing arrangements, Plaintiffs did not name any of the dealers as co-defendants. [HN6](#) We have rejected attempts to invoke a coconspirator exception to *Illinois Brick*'s bar on indirect purchaser standing when plaintiffs have not named the coconspirators immediately upstream as defendants. See [McCarthy v. Recordex Serv., Inc., 80 F.3d 842, 854 \(3d Cir. 1996\)](#); [Link v. Mercedes-Benz, 788 F.2d 918, 933 \(3d Cir. 1986\)](#).

In *Link*, for example, Mercedes car owners sued Mercedes-Benz for allegedly requiring dealers to purchase parts exclusively from it. [788 F.2d at 929](#). Plaintiffs had purchased parts from the dealers, whom they named as co-conspirators but not as defendants. Plaintiffs claimed that *Illinois Brick* did not bar their vertical conspiracy claims because "the intervening parties in the distribution process [were] co-conspirators." [Id. at 931](#).

We concluded that, unless the dealers were joined as [\[\\*\\*15\]](#) parties, plaintiffs' suit implicated the policy concerns of *Illinois Brick* and was barred. We explained that if a jury found that Mercedes and its dealers were co-conspirators, but the dealers were not parties to the suit, that determination would not have any collateral estoppel effect in a subsequent suit by a dealer against Mercedes. [Id. at 932](#). Therefore, because the dealers were not named as defendants, the risk of duplicative liability identified in *Illinois Brick* remained. Similarly in *Hess*, because the dealers may also sue Dentsply, the risk of duplicative liability looms.

Plaintiffs attempt to distinguish *Hess* from *Link* by pointing to stipulations they entered into with most of Dentsply's dealers. As part of Plaintiffs' opposition to Dentsply's motion for summary judgment in *Hess*, they executed stipulations with twenty-two of Dentsply's dealers. In each stipulation, the dealer agrees "to release [Dentsply] from any and all claims for antitrust violations" set forth in the complaints in *Hess* or *United States v. Dentsply* (the Government's suit against Dentsply), and Plaintiffs agree to "refrain[] from filing suit" against [\[\\*\\*16\]](#) that dealer for the same antitrust violations. The parties to each stipulation agree that "Dentsply is a third party beneficiary of this stipulation" and that the stipulation "may be specifically enforced by the parties hereto or by Dentsply." Plaintiffs'

expert calculated that the group of dealers who executed these stipulations "represents approximately 95% of the gross sales" of Dentsply's artificial teeth. Plaintiffs argue that the stipulations give Dentsply a safe harbor from dealer suits, thus eliminating the risk of duplicative liability.

[\*371] Many problems attend Plaintiffs' argument. First, while in the stipulations Plaintiffs expressly agree not to sue the dealers, they *did* sue the dealers in *Jersey Dental*. Thus, the stipulations are likely unenforceable by Plaintiffs or Dentsply.<sup>4</sup>

[\*\*17] Furthermore, in *Kansas v. Utilicorp United, Inc.*, 497 U.S. 199, 111 L. Ed. 2d 169, 110 S. Ct. 2807 (1990), [HN8](#) the Supreme Court rejected the assertion that the absence of a particular *Illinois Brick* concern in an individual case would remove its bar on an indirect purchaser claim. *Id. at 217*. "Even assuming that any economic assumptions underlying the *Illinois Brick* rule might be disproved in a specific case, we think it an unwarranted and counterproductive exercise to litigate a series of exceptions." *Id.* Thus, Plaintiffs would not necessarily have standing even if the stipulations did eliminate *Illinois Brick*'s duplicative liability concern.

In addition, in *Merican* the indirect purchasers argued that there was no danger of duplicative recovery because the direct purchaser had executed an affidavit that said it had not suffered injury from the policy that was alleged to violate the antitrust laws. [713 F.2d at 968](#). We nevertheless held that plaintiffs were barred from seeking damages under *Illinois Brick*, recognizing the remaining potential of a direct purchaser suit. *Id. at 968-69*; see also *Dickson v. Microsoft Corp.*, 309 F.3d 193, 215 (4th Cir. 2002) [\*\*18] (applying *Illinois Brick* despite argument that "there is no danger of duplicative recovery because the [direct purchasers] apparently have elected not to sue [the defendant].") (internal quotation marks omitted)).

As our Court has expressly refused to adopt a coconspirator exception to *Illinois Brick* absent the joinder as defendants of the alleged co-conspirators immediately upstream, Plaintiffs in *Hess* lack standing to pursue claims for monetary relief. Before the applicability of that exception may be considered, the dealers must be joined.

### b. May Plaintiffs recover damages in *Hess* under the control exception to *Illinois Brick* ?

[HN9](#) The "control exception" to *Illinois Brick* "might" permit an indirect purchaser to sue an initial seller when the initial seller "own[s] or control[s]" the direct purchaser. *Illinois Brick*, 431 U.S. at 736 n.16. In *Hess*, Plaintiffs argued that they come within this exception because "Dentsply exerts virtual control over its . . . dealers." Dist. Ct. Mem. Op. at 30 (March 30, 2001).

We have applied the control exception only when the initial seller owned the direct purchaser. See *In re Sugar Indus. Antitrust Litig.*, 579 F.2d 13, 18-19 & n.8 (3d Cir. 1978) [\*\*19] (holding that, in certain circumstances, the "first noncontrolled purchaser" has standing to sue when it has purchased from a subsidiary of the violator); see also *Mid-West-Paper Prods. Co., v. Continental Group, Inc.*, 596 F.2d 573, 589 (3d Cir. 1979) (indicating that control exception may apply "when the parent dominates [\*372] and controls the subsidiary to such an extent that the subsidiary is deemed to be an agent of the parent."). But Dentsply does not own any interest in its dealers.

Courts that have extended the control exception beyond a parent-subsidiary relationship still require "relationships involving such functional economic or other unity between the direct purchaser and either the defendant or the indirect purchaser that there effectively has been only one sale." *Jewish Hospital Asso. v. Stewart Mechanical Enterprises, Inc.*, 628 F.2d 971, 975 (6th Cir. 1980); see also *Fisher v. Wattles*, 639 F. Supp. 7, 9 (M.D. Pa. 1985) (to fall within the control exception, plaintiffs must show "such significant control" that the two companies are "virtually the same entity"). Modes of control that might qualify for the control exception include "interlocking [\*\*20]

<sup>4</sup> Even if Plaintiffs had not sued the dealers, Dentsply may not be able to enforce the stipulations in any event. The stipulations state that "Dentsply is a third party beneficiary of this stipulation" and that the stipulations "may be specifically enforced by the parties hereto or by Dentsply." However, [HN7](#) "only intended beneficiaries of a contract made between two or more other parties have enforceable rights under the contract." 13 Williston on Contracts § 37:8, at 67 (Richard A. Lord ed., 4th ed. 2000) (citing *Restatement (Second) of Contracts* § 302). In this case, the contracting parties arguably did not intend that Dentsply benefit from the stipulations, as their purpose was to allow Plaintiffs to sue Dentsply.

directories, minority stock ownership, loan agreements that subject the wholesalers to the manufacturers' operating control, [or] trust agreements."

In re Brand Name Prescription Drugs Antitrust Litig., 123 F.3d 599, 605 (7th Cir. 1997) (Posner, J.). Plaintiffs in *Hess*, however, do not allege that Dentsply exerts any of these modes of control over its dealers.

Furthermore, even assuming that Dentsply does exert some degree of control over its dealers, *Illinois Brick*'s policy reasons for denying standing remain. Nothing about Dentsply's "control" over its dealers would prevent the dealers from suing Dentsply, thus creating a risk of duplicative liability for Dentsply and potentially inconsistent judgments. Also, if Plaintiffs wanted to recover overcharge damages, they would still have to demonstrate the portion of the overcharge dealers had passed on to them, leaving intact the evidentiary complexities and uncertainties of concern in *Illinois Brick*. Moreover, permitting Plaintiffs to sue for damages could potentially lead to inefficient enforcement of the antitrust laws, because the ultimate recovery for the dealers would be diluted (assuming that, [\*\*21] rather than the dealers being permitted to recover the entire overcharge, it was apportioned among the dealers and the labs), thereby decreasing the dealers' incentive to sue.

In sum, Plaintiffs do not come within the control exception because Dentsply does not own any interest in its dealers and no functional unity exists among them and Dentsply. Notwithstanding whatever lesser degree of control Dentsply may exert over its dealers, *Illinois Brick*'s policy reasons for denying

standing apply.

#### **c. May Plaintiffs recover non-overcharge damages in *Hess* ?**

In their opposition to summary judgment in *Hess*, Plaintiffs argued that, even if *Illinois Brick* barred them from proving overcharge damages, they might still be able to present a non-overcharge theory of damages after further discovery. The District Court rejected this claim "because the *Hess* plaintiffs have failed to articulate any theory of damages that would be anything other than overcharges." Dist. Ct. Mem. Op. at 31 (March 30, 2001). We agree, and thus Plaintiffs' claim was properly dismissed at summary judgment.

#### **D. May Plaintiffs recover damages based on drop shipments in *Hess* ?**

Plaintiffs in [\*\*22] *Hess* claimed that, for teeth drop shipped directly from Dentsply to the labs, they were direct purchasers not subject to *Illinois Brick*. However, the *Hess* complaint limited the plaintiff class to "all dental laboratory purchasers of any Dentsply products who purchased such products *through Dentsply Dealers*." (emphasis added). Plaintiffs cannot avoid *Illinois Brick* by claiming they were direct purchasers of drop shipments when their [\*373] complaint specifically alleges that they did not directly purchase from Dentsply.

Furthermore, the fact that some of the teeth are drop shipped directly from Dentsply to Plaintiffs does not affect the economic substance of the transaction. That is, the dealers still make the sale to Plaintiffs and Dentsply makes the sale to the dealers. Plaintiffs pay the dealers their usual price, the dealers take their profit, and then the dealers pay Dentsply. See Dist. Ct. Mem. Op. at 29 (March 30, 2001). While it is true that the dealers do not take physical possession of the teeth, this is nothing but a formal difference from the typical transactions. Thus, even as to teeth drop shipped directly from Dentsply to the labs, Plaintiffs are indirect [\*\*23] purchasers potentially subject to *Illinois Brick*.

### **II. May Plaintiffs recover damages in *Jersey Dental* ?**

#### **a. May Plaintiffs recover lost profits damages caused by their lost opportunities to purchase and resell Dentsply's competitors' products?**

Plaintiffs argue that, even if they do not have standing to recover damages for overcharges they paid to dealers for Dentsply's teeth, they have standing to recover lost profits damages caused by their lost opportunities to purchase

and resell products of Dentsply's competitors.<sup>5</sup> Plaintiffs allege that, as a result of Dentsply's exclusive-dealing, its competitors are denied adequate access to a necessary means of distribution--the dealers. Thus Dentsply's competitors' products are not available. Plaintiffs are theoretically correct that, "but for [Dentsply's] exclusion of more efficient rivals, purchasers would have shifted at least some of their business to the rivals." ABA Section of **Antitrust Law**, *Proving Antitrust Damages: Legal and Economic Issues* 194 (1996).

[\*\*24] **HN10** When antitrust violators cause prices to increase through monopolization, a price-fixing conspiracy, or exclusionary conduct, the harm they cause members of the distribution chain comes in two forms: (1) overcharges paid for goods actually purchased;<sup>6</sup> and (2) lost profits resulting from the lost opportunity to buy and resell a greater volume of goods. Jeffrey L. Harrison, *The Lost Profits Measure of Damages in Price Enhancement Cases*, 64 Minn. L. Rev. 751, 753, 770-72 [\*374] (1980) ("The gross overcharge measure [of damages] ignores the impact that the enhanced price has had on the volume of the final good eventually produced."); see also ABA Section of **Antitrust Law**, *supra*, at 195 ("It is the fundamental law of demand that as the price of a product increases the amount purchased decreases. A collusive price increase, therefore, will result in a reduction of the quantity of the good purchased.").

[\*\*25] Thus, as some scholars see it, **HN11** when antitrust plaintiffs claim that anticompetitive behavior caused prices to increase, two measures of damages could theoretically be used: (1) the overcharge (*i.e.*, the difference between the price paid for goods actually purchased and the price that would have been paid absent the illegal conduct), or (2) lost profits (*i.e.*, the overcharge paid minus the overcharge passed on for goods actually purchased and resold, plus lost profits from the lost opportunity to buy and resell a greater volume of goods). See 2 Phillip E. Areeda, Herbert Hovenkamp & Roger D. Blair, **Antitrust Law** P 394, at 521 (2d ed. 2000).<sup>7</sup>

A court might potentially use a lost profits measure of damages, as "the Supreme Court has not explicitly held that any particular measure of damages is required [\*\*26] or precluded." ABA Section of **Antitrust Law**, *supra*, at 184 (citing *Thomsen v. Cayser*, 243 U.S. 66, 61 L. Ed. 597, 37 S. Ct. 353 (1917)); see also *Illinois Brick*, 431 U.S. at 733 n.13, 743 n.27 (observing that even if the pass-on defense were permitted and "the defendant show[ed] that as a result of the overcharge the direct purchaser increased its price by the full amount of the overcharge, the direct purchaser m[ight] still claim injury from a reduction in the volume of its sales caused by its higher prices").

However, the standard method of measuring damages in price enhancement cases is overcharge, not lost profits. See ABA Section of **Antitrust Law**, *supra*, at 172 ("The typical measure of damages is the difference between the actual price and the presumed competitive price multiplied by the quantity purchased. This was the calculation that the Supreme Court approved in *Chattanooga Foundry & Pipe Works v. Atlanta*, 203 U.S. 390, 396, 51 L. Ed. 241, 27 S. Ct. 65 (1906)."); *id.* at 193-94 (Where "a group of suppliers conspires to drive a more efficient competitor out

<sup>5</sup> If Dentsply's exclusionary conduct enabled it to raise its prices, thereby reducing (at least in theory) the demand for its own products, Plaintiffs might also have claimed lost profits damages caused by their lost opportunities to purchase and resell Dentsply's products. However, we would reject such a claim for the same reasons we reject Plaintiffs' claim for lost profits damages caused by their lost opportunities to purchase and resell Dentsply's competitors' products.

<sup>6</sup> Members of the distribution chain usually mitigate this harm by passing on some of the overcharge to their buyers. However, much of this harm is not actually avoided, but rather takes the form of the second type of harm--lost profits from the lost opportunity to buy and resell a greater volume of goods. This is because, as members of the distribution chain pass on the overcharge (*i.e.*, raise their prices), their volume of sales theoretically decreases.

Like the second type of harm, the overcharge paid minus the overcharge passed on for goods actually purchased and resold are a form of "lost profits." The overcharge paid minus the overcharge passed on for goods actually purchased and resold is one component of the loss an antitrust violation causes to the bottom line (*i.e.*, the profits) of members of the distribution chain. However, because *Illinois Brick* precludes indirect purchasers from recovering overcharge damages, Plaintiffs do not seek in their lost profits claim the component of their lost profits that includes the overcharge paid minus the overcharge passed on for teeth they actually purchased and resold.

<sup>7</sup> We note that Professor Areeda, who gained recognition for his scholarly work in **antitrust law**, is deceased, and that the treatise is now the responsibility principally of Professor Hovenkamp.

of the market or, equivalently, prevent a more efficient [\*\*27] supplier from entering the market," the excluded supplier (competitor) "would have a claim for antitrust damages based on lost profits" and "purchasers from the conspirators would also have antitrust claims because they pay higher prices as a result of the exclusionary practice." The purchasers' damages would be based on the overcharge they paid measured by "the difference between the price actually paid and the price that would have been paid absent collusion, multiplied by the quantity."); 2 Areeda *et al.*, *supra*, P 394b, at 529 (observing that "in spite of the (arguably) theoretical superiority of lost profits as a measure of damages in a price-enhancement case, nearly all plaintiffs claim damages on the basis of an overcharge calculation"); Harrison, *supra*, at 755-56 ("When the specific activity at issue [is] price enhancement, courts consistently allow[] recoveries based on the gross overcharge instead of lost profits." (footnote omitted)).

**HN12** [+] "Lost" profits damages are disfavored, at least in part because they are more difficult [\*375] to prove than overcharge damages. See ABA Section of *Antitrust Law*, *supra*, at 171 ("The overcharge measure has the virtues of conceptual simplicity [\*\*28] . . . and relative ease of calculation."); Roger D. Blair & William H. Page, "Speculative" Antitrust Damages, *70 Wash. L. Rev.* 423, 433-34 (1995) ("Overcharge damages . . . were recognized by the Supreme Court [in *Chattanooga Foundry*] primarily because of the difficulty of proving lost profits in price-fixing cases. Rather than require the complex netting associated with lost profits, and thus practically deny recovery, the Court permitted plaintiffs to prove damages by showing a price enhancement."); Harrison, *supra*, at 756 ("The advantage to plaintiffs of using a gross overcharge measure is that it is less speculative and therefore easier to prove than lost profits.").

Furthermore, overcharge damages, unlike lost profits, may induce antitrust plaintiffs to make arguments that will protect rather than injure consumers. See Frank H. Easterbrook, *Treble What?*, 55 Antitrust L.J. 95, 96-97, 100-01 (1986). Judge Easterbrook argues that the overcharge to consumers, not lost profits, "should be the basis of all [antitrust] damages." *Id.* at 101. He reasons that

the lure of damages for lost profits induces firms to [\*\*29] make arguments that will injure rather than protect consumers. Profits get lost primarily from hard competition or from the elimination of monopoly. . . . The more competitive the market, the more profits are 'lost.' . . . [Because] it is hard to tell competition apart from exclusion, [] we must be wary of remedies that give the victims of hard competition a strong incentive to sue.

*Id.* at 100-01.

But most importantly, Plaintiffs may not recover lost profits damages because they are indirect purchasers. The District Court concluded that "the intermediate dental dealers suffer the direct harm from any lost opportunity to sell a greater volume of Dentsply products or to sell competitive product lines and profit therefrom. Any harm suffered by plaintiffs remains indirect." Dist Ct. Mem. Op. at 24 n.9 (Dec. 19, 2001). We agree.

Even commentators who advocate for indirect purchaser standing and a lost profits measure of damages admit that their position is currently precluded by Supreme Court case law. As Professor Harrison concedes in his article arguing for indirect purchaser standing and a lost profits measure of damages, "the *Illinois Brick* decision [\*\*30] seems absolutely to foreclose the possibility of indirect-purchaser standing in price enhancement suits," even if the indirect purchaser plaintiffs seek lost profits as opposed to overcharge damages. See Harrison, *supra*, at 777; see also *Illinois Brick*, 431 U.S. at 746 ("In elevating direct purchasers to a preferred position as private attorneys general, [our case law] denies recovery to those indirect purchasers who may have been actually injured by antitrust violations.").

Harrison also acknowledges that

the legal precedents and policy arguments relied on by the [*Hanover Shoe*] Court in rejecting the pass-on defense do not support even the theoretical appropriateness of the lost profits measure. In addition, the Court hinted that it was actually rejecting the very notion that damages should be apportioned among various layers of buyers and sellers. . . . To the extent that the apportionment process has been rejected by the Court, it would be inappropriate to infer that the lost profits measure has received even implicit approval.

*Id.* at 764-65 (footnotes omitted) (citing *Hanover Shoe, 392 U.S. at [\*376] 489-90 & n.8, 494*, ). [\*\*31] Similarly, while Professors Areeda, Hovenkamp and Blair argue that "the correct solution is to permit damages actions based on lost profits to all intermediaries," they concede that their position "is at variance with the case law." 2 Areeda et al., *supra*, P 346a, at 359-60. Finally, the ABA's Antitrust Section recognizes that HN13[] "if a cartel sells to an intermediate purchaser who resells to another, both purchasers are likely to lose profits as a result of the price fix," but concedes that "under the *Illinois Brick* rule, the second intermediate purchaser, or the indirect purchaser from the cartel, cannot recover damages." ABA Section of Antitrust Law, *supra*, at 183-84.

If we were to hold that indirect purchaser plaintiffs could recover lost profits from their decreased volume of purchases and resales, we would be implying (1) that past indirect purchaser plaintiffs who have been denied standing based on *Illinois Brick* could have recovered if only they had framed their claim as one for lost profits rather than for overcharge damages, and (2) that the *Illinois Brick* Court--which was concerned with simplifying and controlling the costs of antitrust litigation and with conserving [\*\*32] judicial resources--really meant that indirect purchasers do have standing to sue, but for lost profits rather than overcharge damages. We find both of these propositions untenable.

For all of these reasons, we hold that Plaintiffs do not have statutory standing to recover lost profits damages caused by their lost opportunities to purchase and resell Dentsply's competitors' products.

**b. May Plaintiffs recover damages caused by the alleged retail price-fixing conspiracy in *Jersey Dental* under a co conspirator exception to *Illinois Brick* ?**

In *Jersey Dental*, Plaintiffs claim that they come within the "co-conspirator exception" to *Illinois Brick* because their purchases from Dentsply's dealers were made from members of a retail price-fixing conspiracy. Other circuit courts have adopted a co-conspirator exception to *Illinois Brick* that applies in retail price-fixing cases. See *Arizona v. Shamrock Foods Co., 729 F.2d 1208, 1211-12 (9th Cir. 1984)* (holding that purchasers from down-stream conspirators may sue up-stream conspirators for damages and noting that "numerous other courts have found *Illinois Brick* inapplicable to claims against remote [\*\*33] sellers when the plaintiffs allege that the sellers conspired with intermediates in the distribution chain to fix the price at which the plaintiffs purchased"); *Paper Sys. Inc. v. Nippon Paper Indus. Co., 281 F.3d 629, 631-32 (7th Cir. 2002)* (Easterbrook, J.) (holding that *Illinois Brick* does not bar suits for damages by plaintiffs against an initial seller when it is alleged to have conspired in violation of the antitrust laws with the seller directly upstream from plaintiffs); *Prescription Drugs, 123 F.3d at 604* (same); see also *Fontana Aviation, Inc. v. Cessna Aircraft Co., 617 F.2d 478, 481 (7th Cir. 1980)* (approving co-conspirator exception in *dicta*).

Our Court has not explicitly adopted a co-conspirator exception to *Illinois Brick*. In *McCarthy*, we neither adopted nor rejected the exception because it was inapplicable to the case, but we did explain its "nature": "In order to fall within the exception, plaintiffs here would have to allege that the intermediaries immediately upstream . . . colluded with the defendants to overcharge plaintiffs . . . . Moreover, plaintiffs would be obliged to join the [intermediaries] [\*\*34] as defendants . . . ." *80 F.3d at 855* (emphasis omitted). In our case, Plaintiffs allege that they made purchases from Dentsply's dealers (the intermediaries immediately upstream from Plaintiffs) [\*377] and that Dentsply and its dealers are co-conspirators. In addition, in *Jersey Dental* Plaintiffs sued not only Dentsply, but also joined as defendants twenty-six of Dentsply's then twenty-eight authorized dealers.<sup>8</sup> Thus, under *McCarthy*, Plaintiffs potentially qualify for the co-conspirator exception.

Furthermore, Professors Areeda, Hovenkamp, and Blair approve of the co-conspirator exception. They explain that

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<sup>8</sup> Plaintiffs may not recover from Dentsply for teeth purchased from the two non-joined dealers under a coconspirator exception to *Illinois Brick* because, as previously mentioned, HN14[] our Court has expressly refused to adopt a coconspirator exception when the alleged co-conspirators immediately upstream have not been joined.

**HN15** [↑] *Illinois Brick* does not limit suits by consumers against [\*\*35] a manufacturer who illegally contracted with its dealers to set the latter's resale price. . . . There is no problem of duplication or apportionment, because the consumer is the only party who has paid any overcharge. . . .

The court simply computes the retail price that would have prevailed absent the illegal contract fixing that price. Further emphasizing that *Illinois Brick* does not apply is that a dealer challenging resale price maintenance imposed upon itself would not base its damages on an "overcharge" at all. Its action is not based on a higher product price to itself, but rather on the constraint on its resale price; its damages would be for lost profits resulting from the reduced volume of sales. As that case illustrates, lost profits damages for the intermediary and overcharge damages for the consumer are not in any way duplicative; they are both losses caused by the unlawful resale price maintenance.

2 Areeda *et al.*, *supra*, P 346h, at 369-70 (footnote omitted).

In fact, a recent supplement to their treatise analyzed *Jersey Dental* and concluded that the District Court "incorrectly refus[ed] to apply a co-conspirator exception to *Illinois Brick*. . ." 2 Areeda *et al.*, *supra*, P [\*\*36] 346a, at 88 n.1 (2003 Supp.). It reasoned that, to the extent that Dentsply imposed resale price maintenance <sup>9</sup> on its dealers, they

might have their own damage action against the supplier, but if so, it would be an action for lost profits, not for an overcharge; the dealer's injury would accrue from the profits lost by . . . lost output resulting from being required to sell at the maintained price; as a result, there was nothing to pass on . . .

*Id.* <sup>10</sup>

[\*\*37] Not only are overcharge pass-on calculations not a concern, the other two *Illinois Brick* policy justifications are also inapplicable to Plaintiffs' price-fixing conspiracy claim. First, there is no risk of duplicative liability or potentially inconsistent judgments because Plaintiffs and Dentsply's dealers would not be suing for the same injury. To the extent that Dentsply imposed resale price maintenance on the dealers, the dealers' claim against Dentsply would be for lost profits, not for an overcharge.<sup>11</sup> Lost profits would be [\*378] caused by lost output, which in turn is caused by resale price maintenance. 2 Areeda *et al.*, *supra*, P 346a, at 88 n.1 (2003 Supp.). Second, permitting Plaintiffs to sue would not cause inefficient enforcement of the antitrust laws by diluting the ultimate recovery and thus decreasing direct purchasers' incentive to sue. Dealers would still recover the same amount on their hypothetical lost profits claim even if Plaintiffs recovered on their separate price-fixing claim.

[\*\*38] Finally, we have found no precedent holding that plaintiffs, who purchase from dealers who are part of a price-fixing conspiracy with the initial seller, may not recover damages from the initial seller.

In this context, we hold that Plaintiffs in *Jersey Dental* have statutory standing to recover damages from Dentsply for its alleged price-fixing conspiracy with its dealers.

#### c. May Plaintiffs recover damages caused by the alleged exclusive-dealing conspiracy in *Jersey Dental* under a co conspirator exception to *Illinois Brick* ?

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<sup>9</sup> "Resale price maintenance"--the term used by Areeda *et al.*--is simply another way of describing the vertical price fixing in which Plaintiffs allege Dentsply and its dealers engaged. In resale price maintenance, the initial seller dictates the dealers' resale price.

<sup>10</sup> In fact, Areeda implies that even the alleged exclusive-dealing could not have caused the dealers to be overcharged. 2 Areeda *et al.*, *supra*, P 346a, at 88 n.1 (2003 Supp.). This appears to be incorrect, for if the exclusive-dealing led to exclusion of Dentsply's competitors, Dentsply may have been able to overcharge its dealers.

<sup>11</sup> We are, of course, not saying that the dealers could prevail on any particular claim. Rather, we merely point out that if the dealers proved that Dentsply imposed resale price maintenance on them, their measure of damages would be based on the lost profits from their decreased volume of purchases and resales. This lost profits harm is different from, and thus not duplicative of, the overcharge harm that any resale price maintenance would have caused Plaintiffs.

In *Jersey Dental*, Plaintiffs also claim that they come within the "co-conspirator exception" to *Illinois Brick* because their purchases from Dentsply's dealers were made from members of an exclusive-dealing conspiracy. Thus, we must decide whether [HN16](#) there is--in addition to a co-conspirator exception for RPM (resale price maintenance, i.e., vertical price-fixing) conspiracies--a co-conspirator exception for non-RPM conspiracies, such as exclusive-dealing or price-fixing at the manufacturer level ("the general co-conspirator exception").<sup>12</sup> We hold that such [\[\\*379\]](#) an exception would only exist in circumstances where the middlemen would [\[\\*\\*39\]](#) be barred from bringing a claim against their former co-conspirator--the manufacturer--because their involvement in the conspiracy was "truly complete" (i.e., if the middlemen would be barred from suing by the "complete involvement defense" of a manufacturer). See [\*Perma Life Mufflers, Inc. v. Int'l Parts Corp.\*, 392 U.S. 134, 140, 20 L. Ed. 2d 982, 88 S. Ct. 1981 \(1968\)](#) (expressly "not decid[ing] . . . whether . . . truly complete involvement and participation in a monopolistic scheme could ever be a basis . . . for barring a plaintiff's cause of action").

#### **[\*\*40] 1. Why we adopt a "limited" general co-conspirator exception.**

If there is a general co-conspirator exception, why do we limit it? To begin, we examine whether *Illinois Brick*'s policy justifications suggest we should adopt (1) a general coconspirator exception that would permit indirect purchaser standing when the middlemen conspired with the manufacturers even if the middlemen were not barred by the complete involvement defense from suing their former coconspirator--the manufacturer (the "unlimited exception")--or (2) an exception that would permit indirect purchaser standing only if the middlemen were barred by the complete involvement defense from suing the manufacturer (the "limited exception").<sup>13</sup>

<sup>12</sup> We recognize that one might ask why would it not always be unprofitable for a direct purchaser to join such a non-RPM conspiracy and effectively agree to be overcharged (as input costs increase, profits decrease). Further, if economics predicts that such overcharge conspiracies will never arise, why consider adopting an exception for them?

As an initial matter, because *Jersey Dental* is at the [\*Federal Rule of Civil Procedure 12\(b\)\(6\)\*](#) stage, we must take as true Plaintiffs' allegations that Dentsply and its dealers have conspired to fix, and have fixed, the prices that dealers charge Plaintiffs and that there was an exclusive-dealing conspiracy between Dentsply and its dealers to exclude Dentsply's competitors. We may not dismiss Plaintiffs' claims because we determine the alleged facts likely did not occur.

In fact, however, we can imagine how the exclusive-dealing conspiracy, *in combination with the RPM conspiracy*, could have been profitable to the dealers. As previously mentioned, it would presumably not have been profitable for the dealers to have joined a conspiracy in which they were overcharged (the exclusive-dealing conspiracy). However, the dealers might have joined such a conspiracy if they were compensated in some fashion. Plaintiffs argue that Dentsply conspired to fix the prices that its dealers charge. This is effectively a *horizontal* price fixing conspiracy at the dealer level (which could presumably be profitable to the dealers) that is policed by Dentsply. Thus, the RPM conspiracy could be the mechanism by which Dentsply compensates its dealers in exchange for the dealers' agreement (1) not to deal with Dentsply's competitors and (2) thus to be overcharged by Dentsply.

In addition, in *Prescription Drugs* Judge Posner rejected a similar argument that it would not have made sense economically for the wholesalers in that case to have joined what was arguably a horizontal price-fixing conspiracy at the manufacturer level. [123 F.3d at 614](#). He explained that "the theory is that the wholesalers were the manufacturers' cats-paws. There is nothing new about the idea that a cartel might 'hire' a customer to help police the cartel." *Id.* He also implied that, because drug wholesalers appeared to be "an endangered commercial species" and the manufacturers could have cut them out altogether and sold directly to buying groups for pharmacies, it was in the wholesalers' self-interest to join the conspiracy. *Id.*

Finally, [HN17](#) "summary judgment for a defendant is proper, even if there is some evidence of an antitrust violation, if plaintiff's theory of violation makes no economic sense." [\*Prescription Drugs\*, 123 F.3d at 614](#) (citing [\*Matsushita Electric Industrial Co. v. Zenith Radio Corp.\*, 475 U.S. 574, 587, 89 L. Ed. 2d 538, 106 S. Ct. 1348 \(1986\)](#); [\*Eastman Kodak Co. v. Image Technical Services, Inc.\*, 504 U.S. 451, 467-69, 119 L. Ed. 2d 265, 112 S. Ct. 2072 \(1992\)](#)). Thus, there is already a mechanism in place for courts to dismiss before trial claims of a conspiracy that would make no economic sense.

<sup>13</sup> The Seventh Circuit is the only Court of Appeals to engage head-on the general co-conspirator exception, and it has adopted it. See [\*Paper Systems\*, 281 F.3d at 631-32](#) ("The right to sue middlemen that joined the conspiracy is sometimes referred to as a

[\*\*41] *Illinois Brick's* first policy concern--the risk of duplicative liability--cuts against the unlimited exception, but in favor of the limited exception. For example, imagine the dealers had already sued and recovered overcharges from Dentsply for the exclusive-dealing conspiracy. If there was an unlimited exception, presumably nothing would stop the labs from then suing Dentsply to recover the duplicative portion of the overcharge that the dealers had passed on to them. Even under the conditions of this case (with the labs suing first and the dealers joined), duplicative recovery is a possibility. If the labs prove Dentsply engaged in an exclusive-dealing conspiracy with the dealers, the dealers could potentially sue Dentsply for duplicative damages the conspiracy caused them. See [Link, 788 F.2d at 932 n.12](#) (analyzing an alleged conspiracy analogous to our case and noting that, even if the dealers [\*380] were joined and were co-conspirators, they could still potentially sue the manufacturer for overcharges caused by the exclusive-dealing conspiracy). However, under the limited exception, the risk of duplicative liability is alleviated because that exception is only applicable [\*\*42] if the middlemen are barred from recovery.

*Illinois Brick's* second policy concern--avoiding the need to ascertain the portion of an overcharge that was passed on--cuts against both exceptions. Unlike vertical conspiracies involving RPM, other vertical conspiracies are designed to distort the *wholesale* market for a particular good. For example, assume that Dentsply and its dealers only engaged in an exclusive-dealing conspiracy. The effect of that conspiracy would be to deny Dentsply's competitors access to its authorized dealers. The absence of competition for these dealers' business would allow Dentsply to charge its dealers a supra-competitive price at wholesale. This overcharge would then be passed on (at least in part) to the dealers' customers, the dental laboratories. The damages that the laboratories could recover from Dentsply would thus be the treble portion of the overcharge that the dealers passed on to them.<sup>14</sup> [\*\*43] Thus both exceptions, which apply to conspiracies that attack the wholesale market, potentially create the problems of apportionment that underlie *Illinois Brick*.<sup>15</sup>

co-conspirator 'exception' to *Illinois Brick*, but it would be better to recognize that *Hanover Shoe* and *Illinois Brick* allocate to the first non-conspirator in the distribution chain the right to collect 100 of the damages."); [Prescription Drugs, 123 F.3d at 604](#); [Fontana Aviation, 617 F.2d at 481](#). However, we do not discern an explanation by the Court why it did so or an explicit delineation of the exception's scope (i.e., whether it is unlimited or limited).

<sup>14</sup> Because [Section 4](#) of the Clayton Act provides for damages of treble the amount a plaintiff is injured, presumably indirect purchaser plaintiffs would only be permitted to recover treble the amount of the manufacturer's overcharge that the direct purchasers passed on to them and would not be able to recover the portion of the manufacturer's overcharge that the direct purchasers absorbed because the indirect purchasers would not have been injured by that portion. See [15 U.S.C. § 15\(a\)](#) ([Section 4](#) of the Clayton Act provides that "any person who shall be injured in his business or property by reason of anything forbidden in the antitrust laws . . . shall recover threefold the damages *by him sustained*.")) (emphasis added). *But see Paper Systems, 281 F.3d at 631-32* ("The right to sue middlemen that joined the conspiracy is sometimes referred to as a co-conspirator "exception" to *Illinois Brick*, but it would be better to recognize that *Hanover Shoe* and *Illinois Brick* allocate to the first non-conspirator in the distribution chain the right to collect *100 of the damages*.")) (emphasis added); cf. [Hanover Shoe, 392 U.S. at 494](#) (holding that an antitrust defendant could not argue that a plaintiff who had purchased a product directly from the defendant was not injured because it had passed on the illegal overcharge to its own customers, thus creating a regime under which plaintiffs can arguably recover *more than* "threefold the damages *by him sustained*"). Of course, if under the limited exception (where direct purchasers are barred from recovering) indirect purchaser plaintiffs were allowed to recover the entire overcharge that the manufacturers imposed on the direct purchasers (even though the direct purchasers absorbed some of that overcharge and did not pass on that absorbed portion to the indirect purchasers), then the portion of the overcharge that was passed on from the direct purchasers to the indirect purchasers would not need to be ascertained and *Illinois Brick's* second policy justification would cut *in favor* of the limited exception.

<sup>15</sup> Technically speaking, there would be no need to "apportion" damages between direct and indirect purchasers under the limited exception. This is because, as we have explained, the limited exception would only permit indirect purchaser standing in circumstances where the direct purchaser would be barred from bringing suit against the manufacturer. As such, there would be no need to apportion any damages to the direct purchasing middleman.

Nevertheless, even under the limited exception, the finder of fact would be required to ascertain the amount of the overcharge that had been passed on by the middleman. After all, [HN18](#) an antitrust plaintiff (whether he be a direct or an indirect purchaser) is only entitled to recover "threefold the damages *by him sustained*." [15 U.S.C. § 15\(a\)](#) (emphasis added). Therefore, to the extent that the middleman retained (i.e., did not pass on to the indirect purchaser) a portion of any overcharge imposed upon him, the damages actually sustained by the indirect purchaser would be reduced by that amount.

[\*381] *Illinois Brick's* third policy [\*\*44] concern--risk of inefficient enforcement of the antitrust laws because the ultimate recovery for the dealers would be diluted, thereby decreasing the dealers' incentive to sue--cuts against the unlimited exception, but in favor of the limited exception. Under the unlimited exception, when middlemen were not completely involved, their recovery would be diluted and their incentive to sue would decrease (assuming that, rather than the middlemen being permitted to recover the entire overcharge, it was apportioned among the middlemen and the indirect purchasers). However, under the limited exception, when middlemen were not completely involved, their recovery would not be diluted and their incentive to sue would not decrease. As the indirect purchasers would not have standing in this instance, no recovery by them could dilute the middlemen's recovery.

Thus, all three of the *Illinois Brick* policy justifications argue against adopting the unlimited exception, while the first and the third favor adopting the limited exception and only the second (the desire to avoid ascertaining the portion of an overcharge that was passed on) cuts against it. Further, while it is true that adopting the [\*\*45] limited exception creates the need to ascertain the portion of an overcharge that was passed on, we think the alternative, adopting no general co-conspirator exception, is less desirable. Cf. *In re Lower Lake Erie Iron Ore Antitrust Litig.*, 998 F.2d 1144, 1169 (3d Cir. 1993) ("While complex apportionment problems are implicated here, we do not hold that litigation must be avoided solely because it might be difficult to ascertain damages. [HN19](#) [↑] Injured parties cannot be penalized and left without recourse because measurement of their damages is difficult."). The *Illinois Brick* Court was concerned with promoting "the longstanding policy of encouraging vigorous private enforcement of the antitrust laws." [431 U.S. at 745](#). [HN20](#) [↑] We are unwilling to hold that if initial sellers and "completely involved" direct purchasers conspire, then *no* plaintiff outside the conspiracy may sue the initial seller for damages.

## 2. Is there a "complete involvement" defense?

We hold that a general co-conspirator exception would only exist if the complete involvement defense barred the middlemen from bringing a claim against their former coconspirator--the manufacturer. However, [\*\*46] our Court has not decided whether the complete involvement defense even exists. We thus examine this question.

In *Perma Life*, the Supreme Court held that "the doctrine of *in pari delicto*. . . is not to be recognized as a defense to an antitrust action." [392 U.S. at 140](#).<sup>16</sup> But as previously mentioned, the Court expressly did "not decide . . . whether . . . truly complete involvement and participation in a monopolistic scheme could ever be a basis . . . for barring a plaintiff's cause of action." *Id.* Further, in concurrences, five members of the *Perma Life* Court favored barring suit by antitrust plaintiffs who were involved in a conspiracy at a high enough level.<sup>17</sup>

[\*\*47] [\*382] Further, every Court of Appeals that has decided the issue has held that antitrust plaintiffs who were involved in a conspiracy at a requisite level are barred from suing. See, e.g., *Sullivan v. National Football League*, 34 F.3d 1091, 1107 (1st Cir. 1994); *Columbia Nitrogen Corp. v. Royster Co.*, 451 F.2d 3, 16 (4th Cir. 1971); *Gen. Leaseways, Inc. v. Nat'l Truck Leasing Ass'n*, 830 F.2d 716, 720-23 (7th Cir. 1987); *Javelin Corp. v. Uniroyal, Inc.*, 546 F.2d 276, 279 (9th Cir. 1976). But cf. *Greene v. Gen. Foods Corp.*, 517 F.2d 635, 646-47 (5th Cir. 1975) ("seriously question[ing]" whether antitrust plaintiffs should ever be barred from suing because of their "unclean

<sup>16</sup> The Court explained that, "although *in pari delicto* literally means 'of equal fault,' the doctrine has been applied . . . in a wide variety of situations in which a plaintiff seeking damages or equitable relief is himself involved in some of the same sort of wrong doing." [Perma Life, 392 U.S. at 138](#).

<sup>17</sup> See *Perma Life, 392 U.S. at 146* (White, J., concurring) ("I would deny recovery where plaintiff and defendant bear substantially equal responsibility for injury resulting to one of [the co-conspirators] . . . ."); *id. at 147* (Fortas, J., concurring) (Suit should be barred when "the fault of the parties is reasonably within the same scale."); *id. at 149* (Marshall, J., concurring) ("I would hold that where a defendant in a private antitrust suit can show that the plaintiff actively participated in the formation and implementation of an illegal scheme, and is substantially equally at fault, the plaintiff should be barred from imposing liability on the defendant."); *id. at 153* (Harlan, J., concurring in part and dissenting in part) (Stewart, J., joining) ("Properly used[, *in pari delicto*] refers to a defense that should be permitted in antitrust cases.").

hands"). In *Link*, our Court recognized that co-conspirators who were completely involved in a conspiracy might be barred from suing. [788 F.2d at 932](#). However, we did not decide the issue because we concluded that the co-conspirators in that case were not completely involved in the conspiracy. *Id.*

We recognize that the weight of authority favors barring suit by antitrust plaintiffs who were involved in a conspiracy at a high enough [\[\\*\\*48\]](#) level. We also recognize, however, the strong policy argument in favor of allowing suits by co-conspirators even when their involvement in a conspiracy was large. The Ninth Circuit has recognized that "the formulation of the 'complete involvement' defense reflects a somewhat uneasy balance between the compelling policy of enforcement of the antitrust laws and the natural desire of any court to recognize the equities as between parties." [THI-Hawaii, Inc. v. First Commerce Fin. Corp., 627 F.2d 991, 995 \(9th Cir. 1980\)](#). It is notable, however, that, while the courts who have adopted the complete involvement defense have struck the "enforcement/equities balance" in favor of equities, the Supreme Court in the holdings of *Illinois Brick* and *Perma Life* struck the balance in favor of enforcement.

In *Illinois Brick*, the Court

conclude[d] that the legislative purpose in creating a group of private attorneys general to enforce the antitrust laws under [§ 4](#) [of the Clayton Act] is better served by holding direct purchasers to be injured to the full extent of the overcharge paid by them than by attempting to apportion the overcharge among all that may [\[\\*\\*49\]](#) have absorbed a part of it.

[431 U.S. at 746](#) (citation and internal quotation marks omitted). Thus the *Illinois Brick* Court made the balancing decision to deny (some might argue inequitably<sup>18</sup>) injured indirect purchasers standing to recover while granting direct purchasers the windfall of the entire overcharge [\[\\*383\]](#) in order to further efficient antitrust law enforcement.

In *Perma Life*, the Court believed that allowing the *in pari delicto* defense in an antitrust action would "threaten the effectiveness of the private action as a vital means for [\[\\*\\*50\]](#) enforcing . . . antitrust policy." [392 U.S. at 136](#). It noted that it had "often indicated the inappropriateness of invoking broad common-law barriers to relief where a private suit serves important public purposes." [Id. at 138](#). It concluded that

the plaintiff who reaps the reward of treble damages may be *no less morally reprehensible* than the defendant, but the law encourages his suit to further the *overriding public policy* in favor of competition. A more fastidious regard for the relative moral worth of the parties would only result in seriously undermining the usefulness of the private action as a bulwark of antitrust enforcement.

[Id. at 139](#) (emphases added). Thus, the Court chose to allow the inequity of letting plaintiffs, though as "morally reprehensible" as defendants, sue in order to foster antitrust law enforcement.

We further point out that a rule prohibiting antitrust plaintiffs who were completely involved in a conspiracy to sue co-conspirators need not be absolute and could be crafted to maximize antitrust enforcement and cartel instability. For example, the law might allow the first, but only the first, [\[\\*\\*51\]](#) completely involved co-conspirator the right to sue its fellow coconspirators. This would give each co-conspirator incentive to be the first to defect from a cartel and enforce the antitrust laws because (1) each would want to be the one and only coconspirator to gain the right to recover treble damages and (2) each would be afraid that if it did not defect, another would, and it would then be liable for treble damages. Under such a rule, the incentive to defect and cartel instability would increase, and cartel breakdown and failure should become more common. Further, if potential co-conspirators knew their potential cartel had a decreased chance of succeeding, they would be less likely to form a cartel in the first place.

<sup>18</sup> See 2 Areeda et al., *supra*, P 346k, at 378 ("The obvious difficulty with denying damages for consumers buying from an intermediary is that they are injured, often more than the intermediary, who may also be injured but for whom the entire overcharge is a windfall. The indirect purchaser rule awards greatly overcompensate intermediaries and greatly undercompensate consumers in the name of efficiency in the administration of the antitrust laws.").

Regardless, as we will explain, it turns out that we need not resolve whether there is a complete involvement defense to antitrust actions in order to determine whether Plaintiffs come within a general co-conspirator exception.

### 3. Could Plaintiffs come within a general co-conspirator exception?

If there is a general co-conspirator exception, it would only apply if the middlemen were barred from bringing a claim against their former co-conspirator--the manufacturer--because **[\*\*52]** their involvement in the conspiracy was "truly complete." However, in our case, Plaintiffs could not qualify for such an exception because the District Court concluded, and Plaintiffs have conceded, that the dealers' involvement in the alleged conspiracy with Dentsply was *not* "truly complete." The District Court concluded that there was "no way to construe the facts alleged such that the dental dealers could be considered 'substantially equal' participants in the alleged conspiracy . . . or that their participation was 'voluntary in any meaningful sense.'" Dist Ct. Mem. Op. at 20-21 (Dec. 19, 2001) (citation omitted). Further, Plaintiffs acknowledged in their brief that they "have not based any part of [their] appeal on any argument that the dealers' involvement was 'substantially equal' to Dentsply's." Appellants' Reply Br. at 23 n.16. Thus, Plaintiffs may not recover damages caused by the exclusive-dealing conspiracy under **[\*384]** a general co-conspirator exception to *Illinois Brick*.

### Conclusion

We thus hold that Plaintiffs may not recover damages in *Hess* (a) under the "co-conspirator" exception to *Illinois Brick*, (b) under the "control" exception to *Illinois Brick*, **[\*\*53]** (c) under a non-overcharge theory of damages, or (d) for "drop shipments." In *Jersey Dental*, however, while Plaintiffs may not recover damages under the control exception or under a lost profits theory, they do have statutory standing under the co-conspirator exception to pursue an action for overcharge damages (including for drop shipped teeth) caused by the alleged retail price-fixing conspiracy, although not for the alleged exclusive-dealing conspiracy.<sup>19</sup>

**[\*\*54]**

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<sup>19</sup> Plaintiffs also allege in *Jersey Dental* that--as to teeth Dentsply drop shipped to them--they were direct purchasers not subject to *Illinois Brick*. Further, the *Jersey Dental* complaint does not have the *Hess* complaint's defect, as it specifically alleges that Plaintiffs were direct purchasers. As we hold that the *Jersey Dental* Plaintiffs have standing to recover damages from Dentsply for its alleged price-fixing conspiracy with its dealers under the co-conspirator exception to *Illinois Brick*, Plaintiffs may potentially recover on the drop-shipped teeth under that theory.

Finally, as in *Hess*, Plaintiffs in *Jersey Dental* do not come within the control exception to *Illinois Brick* because, as already noted, Dentsply does not own any interest in its dealers, there is no functional unity among Dentsply and its dealers, and all of *Illinois Brick*'s policy reasons for denying standing apply.

## **PSN III., Inc. v. Ivoclar Vivadent, Inc.**

United States District Court for the Northern District of Illinois, Eastern Division

September 21, 2005, Decided ; September 21, 2005, Filed

No. 04 C 7232

**Reporter**

2005 U.S. Dist. LEXIS 21044 \*; 2005 WL 2347209

PSN ILLINOIS, INC., Plaintiff, v. IVOCLAR VIVADENT, INC.; DENTSPLY INTERNATIONAL, INC.; DEN-MAT CORPORATION; MICRO DENTAL LABORATORIES; NATIONAL DENTEX CORPORATION; and KNIGHT DENTAL STUDIO, INC., Defendants. IVOCLAR VIVADENT, INC., Counterclaimant and Third Party Plaintiff, v. PSN ILLINOIS, INC., Counterclaimant-defendant, and GERALD G. MCLAUGHLIN, Third-Party Defendant.

**Subsequent History:** Summary judgment denied by [PSN III., Inc. v. Ivoclar Vivadent, Inc., 398 F. Supp. 2d 902, 2005 U.S. Dist. LEXIS 23494 \(N.D. Ill., Oct. 10, 2005\)](#)

## **Core Terms**

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counterclaim, unfair competition, patent, infringement, patent misuse, alleges, deceptive trade practices, motion to dismiss, filing of the lawsuit, marketplace, damages, lawsuit, argues, trade practice, instant case, customers, bad faith, litigation privilege, inequitable conduct, patent infringement, invalidity, porcelain, asserts, fails

## **LexisNexis® Headnotes**

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Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > ... > Responses > Defenses, Demurrsers & Objections > Motions to Dismiss

### **HN1[ Motions to Dismiss, Failure to State Claim]**

For the purposes of a motion to dismiss, the court accepts all well-pleaded allegations as true and draws all reasonable inferences in favor of the plaintiff.

Civil Procedure > ... > Defenses, Demurrsers & Objections > Motions to Dismiss > Failure to State Claim

Civil Procedure > Pleading & Practice > Pleadings > Rule Application & Interpretation

Civil Procedure > Dismissal > Involuntary Dismissals > Failure to State Claims

### **HN2[ Motions to Dismiss, Failure to State Claim]**

In ruling on a motion to dismiss for failure to state a claim, the court considers whether relief is possible under any set of facts that could be established consistent with the allegations. A complaint should not be dismissed for failure to state a claim unless there is no doubt that the plaintiff cannot prove a set of facts that would entitle her to relief based on her claim. The purpose of a motion to dismiss is to test the sufficiency of the complaint, not to decide its merits.

Civil Procedure > ... > Pleadings > Counterclaims > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

### **HN3** **Pleadings, Counterclaims**

See [Fed . R. Civ. P. 15\(a\)](#).

Civil Procedure > ... > Pleadings > Crossclaims > General Overview

Civil Procedure > ... > Pleadings > Counterclaims > General Overview

### **HN4** **Pleadings, Crossclaims**

Pursuant to [Fed. R. Civ. P. 8\(c\)](#), a counterclaim is clearly a pleading.

Civil Procedure > ... > Pleadings > Amendment of Pleadings > Leave of Court

Civil Procedure > Pleading & Practice > Pleadings > General Overview

Civil Procedure > ... > Pleadings > Amendment of Pleadings > General Overview

### **HN5** **Amendment of Pleadings, Leave of Court**

The decision to grant a [Fed . R. Civ. P. 15\(a\)](#) motion for leave to file an amended pleading is a matter purely within the sound discretion of the district court and shall be freely given when justice so requires.

Business & Corporate Compliance > ... > Infringement Actions > Defenses > Misuse

Civil Procedure > ... > Pleadings > Counterclaims > General Overview

Patent Law > Remedies > Declaratory Judgments

Antitrust & Trade Law > ... > Intellectual Property > Misuse of Rights > Patent Misuse Defense

Civil Procedure > ... > Defenses, Demurrers & Objections > Affirmative Defenses > General Overview

Civil Procedure > ... > Pleadings > Crossclaims > General Overview

Civil Procedure > ... > Declaratory Judgments > Federal Declaratory Judgments > General Overview

Civil Procedure > Remedies > Damages > Monetary Damages

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > Appeals

Patent Law > Remedies > General Overview

Patent Law > Remedies > Damages > General Overview

#### **HN6** [] Defenses, Misuse

The United States Court of Appeals for the Federal Circuit (Federal Circuit) has held that patent misuse cannot be brought as a claim for damages because it is an affirmative defense. The Federal Circuit has held that monetary damages may not be awarded under a declaratory judgment counterclaim based on patent misuse because patent misuse simply renders the patent unenforceable. In other words, the defense of patent misuse may not be converted to an affirmative claim for damages simply by restyling it as a declaratory judgment counterclaim. Other courts have dismissed counterclaims for patent misuse.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Effect of Inequitable Conduct

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Patent Law > ... > Inequitable Conduct > Effect, Materiality & Scienter > General Overview

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > Appeals

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Designation of Origin > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

Trademark Law > ... > Federal Unfair Competition Law > Lanham Act > General Overview

#### **HN7** [] Inequitable Conduct, Effect of Inequitable Conduct

Section 43(a) ([15 U.S.C.S. § 1125\(a\)](#)) of the Lanham Act prohibits false designations of origin or false or misleading descriptions of goods or services that are likely to cause confusion. The United States Court of Appeals for the Federal Circuit has held that obtaining a patent through inequitable conduct does not constitute a violation of [15 U.S.C.S. § 1125\(a\)](#) and that the established remedy for inequitable conduct is unenforceability of the patent.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Patent Law > Jurisdiction & Review > Subject Matter Jurisdiction > Appeals

Patent Law > ... > Defenses > Inequitable Conduct > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Effect of Inequitable Conduct

Patent Law > Infringement Actions > General Overview

Trademark Law > ... > Unfair Competition > Federal Unfair Competition Law > General Overview

#### **HN8** [] Inequitable Conduct, Anticompetitive Conduct

The United States Court of Appeals for the Federal Circuit (Federal Circuit) has noted that there are adequate remedies to deal with inequitable conduct in the patent context when it is found. Resort to federal unfair competition law is not one of them. The Federal Circuit has held that the remedy under federal law available to a defendant who is made the subject of an infringement suit, when the defendant alleges that the suit is based on a patent procured through inequitable conduct in dealing with the United States Patent & Trademark Office, is the traditional remedy of having the patent adjudge unenforceable, or perhaps, in appropriate circumstances, holding the patentee liable for an antitrust violation.

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Effect of Inequitable Conduct

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Business & Corporate Compliance > ... > Defenses > Inequitable Conduct > Anticompetitive Conduct

Patent Law > Infringement Actions > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Designation of Origin > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

#### **HN9** [] Inequitable Conduct, Effect of Inequitable Conduct

The United States Court of Appeals for the Federal Circuit has held that false, marketplace statements of infringement, if made in bad faith, are damaging to competition and are not the type of statements protected by the patent laws and can be reached by section 43(a) ([15 U.S.C.S. § 1125\(a\)](#)) of the Lanham Act.

Patent Law > Infringement Actions > General Overview

Trademark Law > ... > Federal Unfair Competition Law > Trade Dress Protection > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Advertising > General Overview

Trademark Law > ... > Federal Unfair Competition Law > False Designation of Origin > General Overview

Business & Corporate Compliance > ... > Federal Unfair Competition Law > False Designation of Origin > Elements of False Designation of Origin

#### **HN10** [] Patent Law, Infringement Actions

The United States Court of Appeals for the Federal Circuit has noted that the initiation of an infringement suit is clearly not covered by the text of section 43(a) ([15 U.S.C.S. § 1125\(a\)](#)) of the Lanham Act, while a communication to the customers of the accused infringer, in certain circumstances, may be.

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Torts > Intentional Torts > Malicious Prosecution > General Overview

## [\*\*HN11\*\*](#) **Regulated Practices, Trade Practices & Unfair Competition**

Under Illinois law, the only causes of action that can arise from the wrongful filing of a lawsuit are malicious prosecution and abuse of process. Courts applying Illinois law have repeatedly dismissed unfair competition claims based on the allegedly improper use of litigation as a means of competition.

Torts > ... > Defenses > Privileges > Absolute Privileges

Torts > Vicarious Liability > Partners > General Overview

## [\*\*HN12\*\*](#) **Privileges, Absolute Privileges**

The absolute litigation privilege affords immunity to attorneys (and other participants in the judicial process) from tort liability arising out of statements made in connection with litigation.

Evidence > Burdens of Proof > General Overview

Patent Law > US Patent & Trademark Office Proceedings > General Overview

Trademark Law > ... > Unfair Competition > Federal Unfair Competition Law > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

## [\*\*HN13\*\*](#) **Evidence, Burdens of Proof**

Allegations that a defendant's conduct before the U.S. Patent & Trademark Office was intended to interfere with the plaintiff's expected business relationships with third parties is required to state a claim for unfair competition under Illinois common law.

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > General Overview

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

## [\*\*HN14\*\*](#) **Consumer Protection, Deceptive & Unfair Trade Practices**

The Illinois Uniform Deceptive Trade Practices Act, [815 Ill. Comp. Stat. 510/2](#), is violated when, in the course of his or her business, vocation, or occupation a person disparages the goods, services, or business of another by false or misleading representations of fact. [815 Ill. Comp. Stat. 510/2](#).

Antitrust & Trade Law > ... > Trade Practices & Unfair Competition > State Regulation > Scope

Patent Law > Infringement Actions > Infringing Acts > Intent & Knowledge

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > General Overview

Antitrust & Trade Law > Consumer Protection > Deceptive & Unfair Trade Practices > State Regulation

Antitrust & Trade Law > Regulated Practices > Trade Practices & Unfair Competition > General Overview

Patent Law > Infringement Actions > General Overview

#### **HN15** [+] **Trade Practices & Unfair Competition, State Regulation**

The United States District Court for the Northern District of Illinois (Northern District of Illinois) has held that a bad faith assertion of patent infringement to a competitor's customer constitutes a violation of the Illinois Uniform Deceptive Trade Practices Act (Illinois Trade Practices Act), [815 Ill. Comp. Stat. 510/2](#). Importantly, however, this holding concerns a defendant's threats of infringement suits and statements to consumers, competitors, and others that the plaintiff is infringing, which are not statements made in the judicial or administrative process. The Northern District of Illinois has further held that bad faith assertions of patent infringement are intended to be actionable under the Illinois Trade Practices Act, but only based on marketplace statements to potential customers about the existence of a patent infringement lawsuit, not based on the filing of the lawsuit itself.

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For Micro Dental Labs, Counter Claimant: Edward Anthony Mas, II, Robert Anthony Surrette, [\*4] McAndrews, Held & Malloy, P.C., Chicago, IL; Mark S Freeman, Choate, Hall & Stewart, Boston, MA.

**Judges:** Judge Robert W. Gettleman.

**Opinion by:** Robert W. Gettleman

## **Opinion**

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### ***MEMORANDUM OPINION AND ORDER***

Plaintiff PSN Illinois, Inc. ("PSN") filed a complaint against fourteen defendants <sup>1</sup> on November 10, 2004, alleging infringement of patent number 4,579,530 ("530 patent") entitled "Fabrication of Porcelain Restorations." The '530 patent claims methods for making dental porcelain veneers. On December 6, 2004, Ivoclar filed its answer and counterclaim against PSN seeking a declaratory judgment of patent invalidity. On June 9, 2005, PSN filed an amended complaint. On July 7, 2005, defendant Ivoclar Vivadent, Inc. ("Ivoclar") filed an answer to the amended complaint, including a two-count amended counterclaim against PSN and Dr. Gerald G. McLaughlin ("McLaughlin"), the named inventor of the '530 patent. Count I of the amended counterclaim seeks a declaration of noninfringement, invalidity, and unenforceability. Count II alleges patent misuse, unfair competition, and deceptive trade practices. PSN has moved pursuant to [Fed. R. Civ. P. 12\(b\)\(6\)](#) to strike [\*5] and dismiss Count II of Ivoclar's counterclaim and third party complaint against McLaughlin. For the reasons discussed below, the court denies in part and grants in part PSN's motion to strike and grants PSN's motion to dismiss.

### **FACTS**

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<sup>1</sup> Eight of the original defendants are no longer parties to the instant action.

The following is a brief recitation of facts necessary for the adjudication of PSN's motion to dismiss Count II of Ivoclar's counterclaim only.

PSN is an Illinois corporation, and the owner of the '530 patent, Ivoclar is a Delaware corporation [\*6] that manufactures materials used to fabricate porcelain veneer restorations, including those sold under the "Empress" trade name. The '530 patent was issued April 1, 1986. Reexamination Certificate BI 4,579,530 was issued 11, 1989. The '530 patent expired November 21, 2004.

In its answer and amended counterclaim Ivoclar alleges on information and belief that the method of fabricating porcelain veneer restorations claimed in the '530 patent was developed in whole or in substantial part by Roger Sigler ("Sigler") and/or others associated with Myron's Dental Laboratories ("Myron's") in late 1982 or early 1983.

McLaughlin filed applications for the '530 patent with the United States Patent and Trademark Office ("PTO") on November 21, 1984, and the patent was issued on April 1, 1986. Ivoclar alleges on information and belief that McLaughlin knew at the time he filed the applications for the '530 patent that he was not the sole inventor of the porcelain veneer restorations, and that the method was being used commercially more than a year prior to the filing of his patent application, Ivoclar also alleges that on August 12, 1988, McLaughlin, as president of Yukiyo, Ltd. ("Yukiyo"), PSN's [\*7] predecessor-in-interest and assignee of the '530 patent, filed a verified statement with the PTO falsely claiming small entity status.<sup>3</sup>

On October 11, 2004, PSN filed a certificate of correction with the PTO on behalf of McLaughlin seeking to correct claim 1 of the '530 patent. The PTO denied the request for a certificate of correction on December 2, 2004. On November 2, 2004, PSN acquired the entire right, title and interest in and to the '530 patent from McLaughlin and Yukiyo. On November 9, 2004, PSN filed its complaint in the instant action.

## **LEGAL STANDARD**

**HN2** In ruling on a motion to dismiss for failure to state a claim, the court considers "whether relief is possible under any set of facts that could be established consistent with the allegations." *Bartholet v. Reishauer A.G.*, 953 F.2d 1073, 1078 (7th Cir. 1992). [\*8] A complaint should not be dismissed for failure to state a claim unless there is no doubt that the plaintiff cannot prove a set of facts that would entitle her to relief based on her claim. *Pressalite Corp. v. Matsushita Elec. Corp. of Am.*, 2003 U.S. Dist. LEXIS 5600, 2003 WL 1811530, at \*2 (N.D.Ill. Apr. 4, 2003). The purpose of a motion to dismiss is to test the sufficiency of the complaint, not to decide its merits. See *Gibson v. City of Chicago*, 910 F.2d 1510, 1520 (7th Cir. 1990).

## **DISCUSSION**

Ivoclar's amended counterclaim is asserted against PSN and McLaughlin, and seeks dismissal of PSN's claims, a declaration of non-infringement and patent invalidity, and damages. Count II of Ivoclar's amended counterclaim asserts a claim for "patent misuse, unfair competition, and deceptive trade practices." In addition to lumping three distinct causes of action into a single count. Count II does not reference a particular law or statute. PSN argues that Count II should be dismissed because patent misuse is an affirmative defense, not a counterclaim, and because Ivoclar has failed to state a claim for unfair competition or deceptive trade practices.

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<sup>2</sup> **HN1** For the purposes of a motion to dismiss, the court accepts all well-pleaded allegations as true and draws all reasonable inferences in favor of the plaintiff. *Travel All Over the World, Inc. v. Kingdom of Saudi Arabia*, 73 F.3d 1423, 1428 (7th Cir. 1996).

<sup>3</sup> For the purposes of charging reduced fees to patent holders, the PTO rules define a "small entity" as a small business concern, independent inventor, or non-profit organization. *37 C.F.R. § 1.9(f)*.

## I. Motion [\*9] to strike amended counterclaim and third party complaint

PSN asserts that under [Fed. R. Civ. P. 15\(a\)](#), Ivoclar was required to obtain leave to amend its counterclaim because PSN had filed a responsive pleading, its reply to Ivoclar's counterclaim, on December 20, 2004. [Rule 15\(a\)](#) provides, [HN3](#)[] "A party may amend the party's pleading once as a matter of course at any time before a responsive pleading is served.... Otherwise, a party may amend the party's pleading only by leave of court or by written consent of the adverse party; and leave shall be freely given when justice so requires." Ivoclar responds that leave was not required because [Rule 15](#)'s reference to "pleadings" does not apply to a counterclaim.<sup>4</sup>

[HN5](#)[] The decision to grant a [Rule 15\(a\)](#) motion for leave to file an amended pleading is a matter "purely within the sound discretion of [\*10] the district court" and shall be freely given when justice so requires. [J.D. Marshall Int'l, Inc. v. Redstart, Inc.](#), 935 F.2d 815, 819 (7th Cir. 1991); [Fed. R. Civ. P. 15\(a\)](#). PSN does not argue that it was prejudiced by the amended counterclaim or that it was made for an improper purpose. Accordingly, although the better practice would have been for Ivoclar to seek leave to file, the court grants Ivoclar leave to file its amended counterclaim instanter, and denies PSN's motion to strike the amended counterclaim.

PSN also argues that Ivoclar required leave under [Rule 14](#) to add McLaughlin as a party to the lawsuit, and that his addition on July 7, 2005, was untimely because expert reports are due September 30, 2005. In addition, PSN asserts that McLaughlin is not a proper party because he is not the owner of the '530 patent, and that Ivoclar's claims against him for allegedly participating in the lawsuit, including by signing interrogatories and being designated as a witness, are frivolous.

In the instant case, Ivoclar refers to McLaughlin in the amended counterclaim as a "third party defendant," but in its response Ivoclar argues [\*11] that [Rule 14](#) does not apply because it seeks damages from McLaughlin for independent wrongs. Indeed, a proper third party complaint under [Rule 14](#) would allege that if Ivoclar loses, McLaughlin is responsible for all or part of Ivoclar's liability to PSN. Because this is not what Ivoclar claims, McLaughlin cannot be added as a third party defendant. In addition, as discussed below, because Count II of the counterclaim (the only count alleging a claim against McLaughlin) fails to state a claim, the court dismisses McLaughlin from this action.

## II. Patent misuse

[HN6](#)[] The Federal Circuit held in [B. Braun Medical v. Abbott Lab.](#), 124 F.3d 1419, 1427 (Fed. Cir. 1997), that patent misuse could not be brought as a claim for damages because it is an affirmative defense. The *Braun* court held that monetary damages may not be awarded under a declaratory judgment counterclaim based on patent misuse "because patent misuse simply renders the patent unenforceable.... In other words, the defense of patent misuse may not be converted to an affirmative claim for damages simply by restyling it as a declaratory judgement counterclaim." [124 F.3d at 1428](#). Other [\*12] courts have relied on *Braun* to dismiss counterclaims for patent misuse. See, e.g., [Bernhardt L.L.C. v. Collezione Europa USA, Inc.](#), 2002 U.S. Dist. LEXIS 13832, 2002 WL 1602447, at \*2 (M.D.N.C. July 3, 2002); see also, [Depuy Inc. v. Zimmer Holdings, Inc.](#), 343 F. Supp. 2d 675, 684 n. 4 ("patent misuse is an affirmative defense, not a counterclaim") (citing *Braun*).

In the instant case, as in *Braun*, Ivoclar's counterclaim repeats its affirmative defenses and seeks declaratory relief and damages, Ivoclar devotes one paragraph only in its response to its patent misuse counterclaim, and appears to concede that it is not viable. Accordingly, the court grants PSN's motion to dismiss Count II of Ivoclar's amended counterclaim to the extent that it attempts to state a claim for patent misuse.

## III. Unfair competition

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<sup>4</sup> Ivoclar is wrong. See, e.g., [HN4](#)[] [Fed. R. Civ. P. 8\(c\)](#). A counterclaim is clearly a pleading.

Count II of Ivoclar's amended counterclaim does not identify a statutory basis for its unfair competition claim, but Ivoclar clarifies in its response to the motion to dismiss that it brings the claim under § 43(a) of the Lanham Act, [15 U.S.C. § 1125\(a\)\(1\)](#), and under Illinois statutory and common law. Ivoclar's claims are based [\*13] on: (1) PSN's lawsuits against Ivoclar and its customers, consumers of Ivoclar's Empress ingots; and (2) PSN's alleged misrepresentations to the PTO. PSN argues that neither the filing of a patent infringement lawsuit nor inequitable conduct before the PTO can form the basis of an unfair competition claim under any federal or state law. For the reasons stated below, the court agrees that Ivoclar has failed to state a claim for unfair competition.

**HN7** [↑] [Section 43\(a\)](#) of the Lanham Act prohibits false designations of origin or false or misleading descriptions of goods or services that are likely to cause confusion. The Federal Circuit has held that obtaining a patent through inequitable conduct does not constitute a violation of [§ 43\(a\)](#) and that "the established remedy for inequitable conduct is unenforceability of the patent." [Pro-Mold and Tool Company, Inc. v. Great Lakes Plastics, Inc., 75 F.3d 1568, 1575 \(Fed. Cir. 1996\)](#) (affirming dismissal of the defendant's counterclaim for unfair competition). As here, the defendant in *Pro-Mold* counterclaimed for unfair competition alleging that the plaintiff violated federal [antitrust law](#) by filing an infringement suit on a patent [\*14] it knew was invalid. [Id. at 1571](#). Specifically, the defendant in *Pro-Mold* alleged that the plaintiff's failure to disclose prior art and a joint inventor to the PTO constituted unfair competition. *Id.*

**HN8** [↑] The *Pro-Mold* court noted that "there are adequate remedies to deal with inequitable conduct when it is found. Resort to federal unfair competition law is not one of them." [Id. at 1575](#). The Federal Circuit affirmed this holding in [Zenith Electronics Corp. v. Exzec, Inc., 182 F.3d 1340 \(Fed. Cir. 1999\)](#). "*Pro-Mold* tells us that the remedy under federal law available to a defendant who is made the subject of an infringement suit, when the defendant alleges that the suit is based on a patent procured through inequitable conduct in dealing with the Patent Office, is the traditional remedy of having the patent adjudge unenforceable, or perhaps, in appropriate circumstances, holding the patentee liable for an antitrust violation." [Id. at 1349](#). *Pro-Mold* and *Zenith* are on all fours with the instant case, and preclude Ivoclar federal unfair competition claim based on PSN's alleged misrepresentations to the [\*15] PTO.

PSN argues that the filing of a lawsuit also cannot form the basis of a [§ 43\(a\)](#) claim. Ivoclar responds that it alleges bad faith, and that **HN9** [↑] the Federal Circuit held in *Zenith* that false, marketplace statements of infringement, "if made in bad faith, are damaging to competition and are not the type of statements protected by the patent laws... [and] can be reached by [§ 43\(a\)](#)." [Zenith, 182 F.3d at 1354](#). In the instant case, Ivoclar alleges that PSN filed lawsuits against Ivoclar's customers in an attempt to coerce settlement, collect damages, and interfere with Ivoclar's business even though PSN knew that the '530 patent was invalid. Ivoclar has thus alleged that PSN acted in bad faith by filing the lawsuits. Ivoclar does not, however, allege that PSN made any marketplace statements outside of the litigation context.

The *Zenith* court specifically distinguished the facts before it from those in *Pro-Mold* and another unfair competition case, [Concrete Unlimited Inc. v. Cementcraft, Inc., 776 F.2d 1537 \(Fed. Cir. 1985\)](#). *Pro-Mold* and *Concrete Unlimited* dealt with threats of and actual infringement suits. In contrast, *Zenith* [\*16] dealt with marketplace misconduct, in which the counter-plaintiff alleged that the counter-defendant misrepresented the scope of its patent to the counter-plaintiff's potential customers, and falsely stated that the counter-plaintiff was infringing. The *Zenith* court noted, "The gravamen of [the defendant's] claim is marketplace misconduct, not abuse of the administrative and judicial process." [182 F.3d at 1349](#). **HN10** [↑] The *Zenith* court also noted that "the initiation of an infringement suit is clearly not covered by the text of [§ 43\(a\)](#), while a communication to the customers of the accused infringer, in certain circumstances, may be." *Id.*

In the instant case, the gravamen of Ivoclar's counterclaim is abuse of the judicial process, Ivoclar's response brief fails to acknowledge the *Zenith* court's distinction between litigation and marketplace statements, and does not address the fact that [§ 43\(a\)](#) does not apply to the filing of a lawsuit. For example, Ivoclar cites [Mitsubishi Electric Corp. v. IMS Technology, Inc., 1997 U.S. Dist. LEXIS 15350, 1997 WL 630187, at \\*8 \(N.D.Ill. Sept. 30, 1997\)](#), in which the court held that allegations of bad faith infringement letters, which [\*17] are specifically limited by the Lanham Act, stated a federal claim of unfair competition. In the instant case, Ivoclar does not allege infringement

letters or other marketplace conduct, nor does Ivoclar argue that the filing of a lawsuit is equivalent to a marketplace statement. Accordingly, Ivoclar has failed to allege a [§ 43\(a\)](#) violation.

Ivoclar argues that it has sufficiently alleged a claim for unfair competition under the Illinois Consumer Fraud and Deceptive Trade Practices Act ("Trade Practices Act"), [815 ILCS 505/2](#), and Illinois common law. PSN argues that the filing of lawsuits cannot form the basis of an Illinois unfair competition claim, and that its statements in the course of litigation are protected by the litigation privilege.

**HN11**[] Under Illinois law, the only causes of action that can arise from the wrongful filing of a lawsuit are malicious prosecution and abuse of process. [Havoco of America, Ltd. v. Holloway](#) 702 F.2d 643, 646 (7th Cir. 1983). Courts applying Illinois law have repeatedly dismissed unfair competition claims based on the allegedly improper use of litigation as a means of competition. See, e.g., [Knoll Pharmas. Co. v. Teva Pharmas. USA, Inc.](#), 2001 U.S. Dist. LEXIS 12999, 2001 WL 1001117, [\*18] at \*2 (N.D.Ill. Aug. 24, 2001); [WorldCom, Inc. v. Transcend Allegiance, Inc.](#), 1998 U.S. Dist. LEXIS 2693, 1998 WL 111636, at \*2 (N.D.Ill. Mar. 6, 1998); [Harris Custom Builders, Inc. v. Hoffmeyer](#), 834 F. Supp. 256, 262 (N.D.Ill. 1993). In [Doe v. Maywood Hous. Auth.](#), 1994 U.S. Dist. LEXIS 13451, 1994 WL 521050, at \*7 (N.D.Ill. Sept. 22, 1994), Judge Grady dismissed an unfair competition counterclaim and issued a rule to show cause against the lawyer who filed it, noting that "a reasonable prefiling inquiry into the law would have informed [the attorney] that his counterclaim in tort sounded in malicious prosecution, and that the tort of malicious prosecution required him to plead that the underlying case was terminated in his clients' favor." Ivoclar fails to cite an Illinois case in which an unfair competition claim was successfully based on the defendant's improper use of litigation as a means of competition.<sup>5</sup>

[\*19] PSN argues that even if litigation against customers of a competitor could form the basis of an unfair competition claim, any statements made during the course of litigation, including allegations of infringement, are protected by the litigation privilege. **HN12**[] The "absolute litigation privilege affords immunity to attorneys (and other participants in the judicial process) from tort liability arising out of statements made in connection with litigation." [Steffes v. Stepan Co.](#), 144 F.3d 1070, 1074 (7th Cir. 1998); see also, [Wilton Partners III, LLC v. Gallagher](#), 2003 U.S. Dist. LEXIS 21899, 2003 WL 22880834, at\* 1 (N.D. Ill. Dec. 5, 2003) (absolute litigation privilege precludes claims based upon filing of an allegedly "baseless lawsuit" and serving a third party subpoena). Ivoclar does not address this issue. Ivoclar has failed, therefore, to state an Illinois claim for unfair competition based on PSN's filing of lawsuits.

Ivoclar also alleges that it has stated an Illinois unfair competition claim based on PSN's alleged misrepresentations to the PTO. Ivoclar fails, however, to **HN13**[] allege that PSN's conduct before the PTO was intended to interfere with Ivoclar's expected business relationships [\*20] with third parties, as required to state a claim for unfair competition under Illinois common law. See [Zenith Elecs. Corp. v. ExZec, Inc.](#), 1997 U.S. Dist. LEXIS 6066, 1997 WL 223067, at \*6 (N.D.Ill. Mar. 27, 1997) (elements of common law unfair competition claim).

Accordingly, the court grants PSN's motion to dismiss Count II of Ivoclar's amended counterclaim to the extent that it attempts to state an unfair competition claim under either state or federal law.

#### IV. Deceptive trade practices

Ivoclar clarifies in its response to the motion to dismiss that it brings its deceptive trade practices claim under the Illinois Uniform Deceptive Trade Practices Act ("Illinois Trade Practices Act"), [815 ILCS 510/2](#). **HN14**[] The Illinois Trade Practices Act is violated when, "in the course of his or her business, vocation, or occupation" a person "disparages the goods, services, or business of another by false or misleading representations of fact." [815 ILCS 510/2](#).

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<sup>5</sup> [Concrete Unlimited](#), 776 F.2d 1537 (Fed. Cir. 1985) and [Dow Chemical Co. Exxon Corp.](#), 139 F.3d 1470 (Fed. Cir. 1998), cited by Ivoclar in support of its argument that its state unfair competition claims are not preempted by federal law, addressed marketplace conduct only.

Ivoclar relies on [\*Mitsubishi, 1997 U.S. Dist. LEXIS 15350, 1997 WL 630187 \(N.D. Ill. Sept. 30, 1997\)\*](#), in support of its argument. [HN15](#)[] The *Mitsubishi* court held that a "bad faith assertion" of patent [\*21] infringement to a competitor's customer constituted a violation of the Illinois Trade Practices Act. [\*1997 U.S. Dist. LEXIS 15350, WL at \\*7\*](#). Importantly, however, as discussed above, the *Mitsubishi* court was concerned with the defendant's threats of infringement suits and statements to consumers, competitors, and others that the plaintiff was infringing; these were not statements made in the judicial or administrative process. Ivoclar also cites [\*Herman Miller, Inc. v. Teknion Furniture Sys., 1996 U.S. Dist. LEXIS 8585, 1996 WL 341541, at \\*3 \(N.D.Ill. Jun. 20, 1996\)\*](#), in which the court held that "bad faith assertions of patent infringement were intended to be actionable under the [Illinois Trade Practices Act]." The deceptive trade practices counterclaim in *Herman Miller*, however, was based on marketplace statements to potential customers about the existence of a patent infringement lawsuit, not the filing of the lawsuit itself.

In the instant case, Ivoclar does not allege that PSN made any disparaging comments outside of the litigation or administrative contexts. In fact, the only public statements that Ivoclar alleges PSN made regarding the Empress products is that they do not infringe, which clearly [\*22] cannot be considered disparaging. Ivoclar fails, as it did regarding its unfair competition claim, to cite a single Illinois case in which a claim was successfully asserted on the ground that the filing of a lawsuit constituted a deceptive trade practice. Under Illinois law, as discussed above, alleged false statements of fact in judicial pleadings may form the basis of a malicious prosecution or abuse of process claim only. Ivoclar asserts neither type of claim. In addition, the litigation privilege also precludes Ivoclar's deceptive trade practices claim based on statements made in the course of litigation. Even if statements made in the administrative context could form the basis for a claim under the Illinois Trade Practices Act, Ivoclar fails to allege that PSN's misrepresentations to the PTO disparaged Ivoclar or its products in any way.

Accordingly, the court grants PSN's motion to dismiss Count II of Ivoclar's amended counterclaim to the extent that it attempts to state a claim under the Illinois Trade Practices Act.

## CONCLUSION

For the reasons stated above, the court denies counter-defendant PSN's motion to strike Count II of the amended counterclaim, and dismisses McLaughlin [\*23] from the action. The court grants PSN's motion to dismiss Count II of counter-plaintiff Ivoclar's amended counterclaim.

**ENTER: September 21, 2005**

**Robert W. Gettleman**

**United States District Judge**