UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF TEXAS
MARSHALL DIVISION

TSRS, Inc. d/b/a Kay's Kloset...Kay's Shoes; and Toni Cochran, L.L.C., d/b/a Toni's

Plaintiffs,

v.

Leegin Creative Leather Products, Inc.

Defendant.

Civil Action No. 2-03CV-107-TJW

LEEGIN'S REPLY IN SUPPORT OF ITS MOTION FOR NEW TRIAL

I. INTRODUCTION

In its Motion for New Trial, Leegin demonstrated that fundamental errors made both before and during trial affected the way in which the case was presented to the jury, thereby prejudicing Leegin's defenses to both liability and damages. Plaintiff responds to Leegin's Motion by misrepresenting Leegin's arguments and proferred evidence. Because Leegin was prejudiced by these errors, the Court should grant a new trial pursuant to Fed. R. Civ. P. 59(a).

II. ARGUMENT

A. The Court's Exclusion of Professor Elzinga's Testimony Prejudiced Leegin.

Leegin proffered antitrust economics expert Kenneth G. Elzinga to address multiple issues relating to the competitive effects of Leegin's pricing practices. Plaintiff's argument concerning the exclusion of Professor Elzinga's report is based on a fundamentally dishonest description of the report. While Professor Elzinga stated that, from the perspective of antitrust economics, the per se rule of illegality for vertical price fixing agreements was inappropriate both in general and in this case in particular, he gave many other opinions that are highly relevant to the case. As discussed below and in greater detail in Leegin's Motion, both Fifth Circuit law and the Fifth Circuit Pattern Jury Instructions for antitrust cases recognize the potential for the jury to find an exception to the per se rule under certain circumstances. The bulk of Professor Elzinga's

report addressed the economic circumstances of this case that justified the finding of such an exception to the per se rule in this case, as well as the conclusion that Plaintiff's case failed under the rule of reason.

In particular, Professor Elzinga showed that Leegin's policies and practices regarding pricing were far from the "naked restraint" claimed by Plaintiff. Rather, those policies and practices were an integral and necessary part of a system designed to create a new and different combination of product and shopping experience, and as such involved the creation of efficiencies that benefited consumers. Using the concept of free riding, Professor Elzinga explained how Leegin's policy and practices were necessary to the creation of this system, and how free riding by retailers like Plaintiff could destroy that system. Not only did Professor Elzinga show that Leegin's policies and practices benefited consumers; he also showed that market conditions were such that there was no risk of creation or exploitation of market power by Leegin or by any cartel of manufacturers or retailers. As shown in Leegin's Motion, these are precisely the kinds of facts that are directly relevant not only to the recognition of an exception under the Supreme Court's decision in *Broadcast Music, Inc. v. Columbia Broadcasting System, Inc.*, 441 U.S. 1, 19-25 (1979), as incorporated in the Fifth Circuit Pattern Jury Instructions, but also under the Fifth Circuit's decision in *United States v. Realty Mutli-List, Inc.*, 629 F.2d 1351, 1367 (5th Cir. 1980).

Plaintiff's Response to Leegin's Motion for New Trial ("Pl.") further opens the door to Professor Elzinga's report by arguing—incorrectly—that the jury's verdict can be justified under a "dealer cartel" theory. As discussed in Leegin's Reply in Support of Renewed Motion for Judgment as a Matter of Law ("JMOL Reply"), that theory has no factual basis, but Plaintiff's assertion further demonstrates the relevance of Professor Elzinga's testimony. In his report, Professor Elzinga explained that vertical price maintenance by a retailer cartel raises different competitive concerns from manufacturer-initiated vertical price maintenance. He also explained that there are no facts suggesting such a retailer cartel in this case.

B. The Denial of Leegin's Proffered Jury Instructions on the Rule of Reason and the Availability of an Exception to the Application of the Per Se Rule Prejudiced Leegin.

This case clearly demonstrates that, in light of the facts before the Court, vertical minimum price restraints do not meet the requirements for per se illegality. While the complete elimination of the per se rule must come from the Supreme Court which created it, [1] the case law from the Supreme Court and the Fifth Circuit clearly permitted this Court to give an instruction that would have allowed the jury to apply the rule of reason under an exception to the per se rule. By refusing Leegin's requested instructions and by excluding Leegin's economic evidence, the Court allowed the jury to condemn a policy and practice that benefited consumers without any risk of harm to competition.

Plaintiff also misrepresents the modified version of Fifth Circuit Pattern Jury Instruction 6.1 that Leegin proposed to the Court, and wrongly concludes "there is no exception to the per rule for vertical price fixing. Pl. at 4-5. Plaintiff accuses Leegin of misleading the Court by substituting the *Realty Multi-List* language for the qualification, "or, if you find that this case does not involve a price fixing agreement." Pl. at 5 (emphasis original). Leegin did no such thing.[2]

Leegin's proposed instruction included the original language from the Pattern Instruction (that an exception is available "If you find that this case involves an industry in which restraints on competition are essential if the industry's product (or service) is to be available at all"), and added the additional and somewhat broader language from *Realty Multi-List* ("or if you find that

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[1] While Leegin recognizes that this Court is bound by Supreme Court precedent for purposes of challenging that precedent on appeal, Leegin nevertheless continues to assert that a general rule of reason instruction should have been given to the jury.

[2] In the very next sentence, Plaintiff acknowledges: "By its terms, Instruction 6.1 applies only to situations in which the challenged restraints are essential, or to those that do not involve price fixing agreements." *Id.* (emphasis original). Contrary to Plaintiff's suggestion, the Pattern Instruction does not require the jury to find that the restraint does not involve a price-fixing agreement. Instead, the Pattern Instruction requires the jury to find that "this case involves an industry in which restraints on competition are essential if the industry's product (or service) is to be available at all," or (not "and" as claimed by Plaintiff) that "this case does not involve a price fixing agreement." Leegin did not "eliminat[e] this qualification." *Id.* Plaintiff is trying to convert an "alternative" into a "requirement."

Leegin's pricing practices are reasonably connected to an integration of productive activities or other efficiency-creating activity in such a manner as to require an inquiry into the net competitive effect"). Mot. at 8. Accordingly, contrary to Plaintiff's misleading arguments, the Fifth Circuit clearly has recognized *both* exceptions to the per se rule against price-fixing. Leegin correctly stated the standards for finding such an exception in its proposed instruction; and Leegin did not mislead the Court in any way.

C. The Denial of Leegin's Proffered Jury Instruction Defining Antitrust Injury Prejudiced Leegin, and the Jury's Finding of Antitrust Injury Is Against the Clear Weight of the Evidence.

Plaintiff's argument concerning antitrust injury is based on the simplistic argument that antitrust injury is present as a matter of law when a dealer is terminated for violating a vertical price-fixing agreement. Pl. at 5-6. That position simply cannot be squared with the Supreme Court's decision in *ARCO*, and this Court should not perpetuate the error. *See* Leegin's Renewed Motion for Judgment as a Matter of Law, and JMOL Reply in support thereof. In effect, the antitrust injury requirement is a "reality check" that allows a court to avoid injustice when a per se rule applies but the plaintiff's damages are not related to any harm to competition. That is precisely the situation in *ARCO*, and, assuming that a per se violation has occurred here, it is precisely the situation in this case.

Moreover, Plaintiff does not attempt to explain how the jury possibly could have found evidence of "antitrust injury" when "antitrust injury" was not defined in the jury instruction. Simple logic dictates that the jury could not find "antitrust injury" where it did not know what "antitrust injury" is or what facts could establish its presence. The jury could not find something from nothing. Antitrust injury is certainly not a concept in ordinary usage.

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D. The Denial of Leegin's Proffered Jury Instructions on Conspiracy and the Interpretation of Written Agreements Prejudiced Leegin.

Contrary to Plaintiff's arguments (Pl. at 7-8), the fact that the governing Supreme Court authorities on conspiracy in antitrust cases were in different procedural postures than the instant case does not change the legal principles stated in those authorities. The fact that there were written documents in this case does not eliminate the need for a proper instruction to the jury on the interpretation of those documents. Plaintiff's argument erroneously assumes the conclusion that the written documents constituted price fixing agreements.

Leegin contended the written documents were designed to make clear to the sub-set of Heart Store and Brighton Collectible stores that Leegin's general *Colgate* policy continued to apply to them notwithstanding their different status. Accordingly, Leegin's requested instructions were necessary for the jury to properly evaluate those documents in context. Plaintiff argued that the mere fact of written documents that referenced the pricing policy meant that there were price fixing agreements. Plaintiff's logic is incorrect, but without a proper instruction, the jury may have accepted it.

E. The Admission of Davis's Testimony and Denial of Leegin's Proffered Instruction on Mitigation of Damages Prejudiced Leegin, and Resulted in an Award of Damages That Is Against the Clear Weight of the Evidence.

For the reasons stated in Leegin's Motion to Exclude the Testimony of James T. Davis and Leegin's Motion and Renewed Motion for Judgment as a Matter of Law, the Court should not have admitted Davis's testimony. Expert testimony requires a proper methodology applied to correct facts.[3] Where an expert intentionally fails to consider undisputed facts that are clearly relevant to the proper calculation of damages, the result is inherently unreliable.[4] Under such

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[3] Fed. R. Evid. 702; *Daubert v. Merrell Dow Pharms., Inc.*, 509 U.S. 579, 597 (1993); *Seatrax, Inc. v. Sonbeck Int'l, Inc.*, 200 F.3d 358, 371-72 (5th Cir. 2000).

[4] *Marcel v. Placid Oil Co.*, 11 F.3d 563, 567-68 (5th Cir. 1994) (affirming the exclusion of proffered testimony because of serious flaws in the expert's data); *Chavez v. Ill. State Police*, 251 F.3d 612, 643-45 (7th Cir. 2001) (absent reliable underlying data, statistics cannot establish the opinion advanced); *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1055-56, 1057 (8th Cir. 2000) (testimony which does not consider and is not "tied to" all the relevant the facts is mere speculation).

circumstances, the error could be described either as a failure of methodology or a failure to use the correct facts. In either case, the result cannot support a verdict, especially a verdict so obviously out of proportion to any realistic loss under the circumstances. The Court's admission of Davis's testimony prejudiced Leegin's substantial rights and led to a verdict that necessarily is based upon impermissible speculation and guesswork.

The prejudice from Davis's testimony was amplified by the Court's refusal to provide Leegin's proposed instruction regarding mitigation to the jury. The Court provided a lengthy instruction to the jury that fully addressed the issue of a failure to mitigate damages.[5] The Court's instruction, however, did not provide any guidance to the jury regarding how to address evidence of actual mitigation—namely, the undisputed evidence from the Plaintiff's own witness, Smith, establishing that Plaintiff had, at least in part, already succeeded in its efforts to mitigate damages, and was continuing those successful efforts into the foreseeable future. For the reasons stated in Leegin's Motion and Renewed Motion for Judgment as a Matter of Law, the Court's denial of this instruction prejudiced Leegin. In light of Davis's testimony that he was aware of the requirement that a lost profits damages model must account for mitigation, but that he had not done so, the Court's failure to provide Leegin's proposed mitigation instruction suggested to the jury that Davis's failure to address mitigation was somehow justified. Without an appropriate instruction, the jury was unable to understand this fundamental flaw in Plaintiff's damages model.

The Court's admission of Davis's flawed opinion and denial of Leegin's requested instruction clearly prejudiced Leegin. *See Lehrman*, 464 F.2d at 46-48. The result was a patently unfair windfall for Plaintiff that is devoid of evidentiary support. Because of the multiple flaws in Davis's analysis, there is an overwhelming basis to believe that the damages assessed by the jury are wrong.

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[5] Court's Jury Instructions, pp. 8-9.

III. CONCLUSION

Because of prejudicial errors relating to the questions of both liability and damages, the Court should grant a new trial under Fed. R. Civ. P. 59(e).

Respectfully submitted,

Dated: June 30, 2004

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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing document was served on the parties listed below, by first-class mail, on this 30th day of June, 2004.

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