IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MASSACHUSETTS

NATCHITOCHES PARISH HOSPITAL SERVICE DISTRICT and JM SMITH CORPORATION d/b/a SMITH DRUG COMPANY on behalf of themselves and all others similarly situated, Plaintiffs, v. TYCO INTERNATIONAL, LTD.; TYCO INTERNATIONAL (US) INC.; TYCO HEALTHCARE GROUP LP; THE KENDALL HEALTHCARE PRODUCTS COMPANY, Defendants.	§	Civil Action No. 05-12024 PBS **JURY TRIAL DEMANDED**

TYCO INTERNATIONAL (US) INC., TYCO HEALTHCARE GROUP LP, AND THE KENDALL HEALTHCARE PRODUCTS COMPANY'S REPLY MEMORANDUM IN SUPPORT OF DEFENDANTS' MOTION FOR SUMMARY JUDGMENT

[REDACTED VERSION]

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I. INTRODUCTION

Plaintiffs do not dispute that all of the challenged conduct in this case involves Covidien selling its product at prices that are *above* its costs. This fact alone entitles Covidien to summary judgment under *Barry Wright Corp. v. ITT Grinnell Corp.*, 724 F.2d 227 (1st Cir. 1983) and Supreme Court precedent. D.I. 267, Covidien's Opening Brief ("Cov. Br.") at 9-10.

Plaintiffs' argument is that this "pricing jurisprudence" is "irrelevant" because they are "not challeng[ing] *any* discounts." According to Plaintiffs, this is an exclusive dealing case and "exclusive dealing" standards apply. Plaintiffs' argument is nothing more than a transparent attempt to recast the facts pled in their complaint and the theory of their expert to avoid the fatal pricing jurisprudence. This is a pricing case. Plaintiffs do not challenge any non-pricing aspects of Covidien's contracts. Indeed, the theory of Plaintiffs' case is that Covidien's market share discounts – *i.e.,* low prices – harm competition by excluding rivals. The overwhelming majority of courts that have considered the issue of market share or loyalty discount agreements have held that they should be analyzed under the cost-based test set forth in the "pricing jurisprudence."

Even if "exclusive dealing" law is applied in this case, Covidien is entitled to summary judgment. There is no genuine dispute about the key facts, including that the terms of Covidien's contracts do not *require* customers to purchase Covidien product, the contracts are short-term, Covidien's share of the market for sharps containers has declined while competitors' market shares have increased, and GPOs are not the only distribution channel for sharps containers. These facts establish Covidien's entitlement to summary judgment even under exclusive dealing standards. Plaintiffs' arguments are all contrary to well-established law.

Tellingly, Plaintiffs ignore *Allied Orthopedic Appliances, Inc. v. Tyco Health Care Group L.P.*, Case No. 2:05-cv-06419-MRP-AJW (C.D. Cal. July 9, 2008) (Cov. Br. at Ex. GGG), which is fatal to their case. *Allied* involved a challenge to the same type of "market-share

discount agreements" and "sole-source GPO contracts" at issue here. The court found – under the very exclusive dealing standards Plaintiffs insist the Court apply here – that Covidien was entitled to summary judgment. Among other relevant findings, *Allied* found that Covidien's contracts are not unlawful because "[t]hey do not contractually obligate hospitals to buy any [Covidien] sensors at all" and "the only direct consequence for a hospital that fails to meet its compliance level is potentially being charged the price that reflects its actual tier level of purchases." *Allied Orthopedic Appliances, Inc. v. Tyco Health Care Group L.P.*, Case No. 2:05-cv-06419-MRP-AJW, at 7 (C.D. Cal. July 9, 2008) (Cov. Br. at Ex. GGG). These considerations apply with equal force here.

Finally, this case should be dismissed due to Plaintiffs' inability to prove damages. Plaintiffs' experts admit that they did not calculate a crucial input into Plaintiffs' damages. Plaintiffs' response, which primarily attempts to dissuade the Court from considering this argument on the merits, fails to fulfill its burden of establishing the adequacy of its damages.

II. ARGUMENT

A. Covidien Is Entitled To Summary Judgment Because It Sold Its Products Through Non-Exclusive Discount Programs At Above-Cost Prices

The First Circuit's decision in *Barry Wright* and recent Supreme Court precedent hold that above-cost prices do not violate the antitrust laws. Cov. Br. at 8-10. Plaintiffs do not dispute that all of Covidien's prices were above its costs. Nor do Plaintiffs appear to dispute the legal principle that a plaintiff may prevail in a case predicated on alleged anticompetitive discounts only if the discounted prices were below-cost. Indeed, Plaintiffs do not even mention, let alone address, *any* of the Supreme Court cases. Cov. Br. at 9-10.[1]

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[1] *See, e.g.*, *Pacific Bell Tel. Co. v. Linkline Commc'ns, Inc.*, 129 S. Ct. 1109, 1120 (2009) (emphasizing that "[t]o avoid chilling aggressive price competition," courts must reject antitrust claims that challenge a defendant's discounts unless "the prices complained of are below an appropriate measure of its rival's costs.") (citing *Brooke Group Ltd. v. Brown & Williamson Tobacco Corp.*, 509 U.S. 209, 222-23 (1993)).

Plaintiffs' principal argument is that the pricing jurisprudence is inapplicable because they "do not challenge *any* discounts." Plaintiffs' Opposition Brief ("Opp. Br.") at 2. Not true. Plaintiffs' core claim is that customers will not buy from rivals because of the market share *discounts* Covidien offers through its contracts. The allegations in Plaintiffs' expert report illustrate this point. *E.g.*, Elhauge Reply Report ¶ 3 (Donato Reply Decl. Ex. A) ("[T]he ***entire theory of harm in this case*** . . . is that [Covidien]'s conduct has ***raised prices*** . . . [Covidien's] ***pricing thus reflects penalties*** . . ." (emphasis added)); Elhauge Report (Chan Decl. Ex. 3) at ¶ 128 [redacted] (emphasis added)); *id.* at ¶ 143 ("The GPO brokered agreements generally required buyers to purchase a certain share of their sharps containers from [Covidien] to obtain ***the best price***." (emphasis added)).

Plaintiffs cannot change the fundamental nature of the conduct they challenge by merely slapping their preferred label on it. *Cf. Royal v. Leading Edge Prods, Inc.*, 833 F.2d 1, 5 (1st Cir. 1987) ("Though 'that which we call a rose by any other name would smell as sweet,' we must parse causes of action as they are, not as the pleader might fondly wish they were.") (quoting W. Shakespeare, *Romeo and Juliet*, Act II, Sc. ii (1595)); *Miara v. First Allmerica Fin. Life Ins. Co.*, 379 F. Supp.2d 20, 68 (D. Mass. 2005) (same principle).

1. *Barry Wright* and the Supreme Court's Pricing Jurisprudence Govern

Because this case is fundamentally about Covidien's market share discounts, it should be analyzed under *Barry Wright* and the Supreme Court's pricing jurisprudence. Cov. Br. at 7-10. Indeed, the majority of courts addressing this issue have held that alleged anticompetitive discounts should be analyzed under the cost-based test set forth by

the Supreme Court in *Brooke Group*,[2] *even if* those discounts are awarded as part of a market share discount program like Covidien's. *See, e.g.*, *NicSand, Inc. v. 3M Co.*, 507 F.3d 442, 451-52 (6th Cir. 2007) (analyzing loyalty discounts under a predatory pricing standard and holding that if the discounts "are not predatory, any losses flowing from them cannot be said to stem from an *anticompetitive* aspect of defendant's conduct") (emphasis in original); *Virgin Atl. Airways Ltd. v. British Airways PLC*, 257 F.3d 256, 266-69 (2d Cir. 2001) (applying predatory pricing analysis to defendant's incentive programs giving commissions or discounts to travel agents who met specified sales thresholds); *Concord Boat Corp. v. Brunswick Corp.*, 207 F.3d 1039, 1060-63 (8th Cir. 2000) (applying the *Brooke Group* cost-based analysis to defendant's market share discount program to determine that it did not violate antitrust laws); *J.B.D.L. Corp. v. Wyeth-Ayerst Labs., Inc.*, No. 1:01-CV-704, 2005 WL 1396940 (S.D. Ohio June 13, 2005) (holding that "the approach adopted by the Eighth Circuit in *Concord Boat* is correct," and granting summary judgment with respect to defendant's market-share rebates); *United States v. AMR Corp.*, 140 F. Supp. 2d 1141, 1193 (D. Kan 2001) (rejecting plaintiff's attempt to "circumvent the high standards for proof of a predatory pricing claim by semantic sleight of hand" and applying below-cost rules to an incentive program).[3]

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[2] Echoing *Barry Wright*, *Brooke Group* states that "a plaintiff seeking to establish competitive injury resulting from a rival's low prices must prove that the prices . . . are below . . . its rival's costs." *Brooke Group*, 509 U.S. at 222.

[3] Most courts have held (and most legal scholars agree) that *Brooke Group*'s predatory pricing standards also apply to bundled discounts. *See, e.g.*, *Cascade Health Solutions v. Peacehealth*, 515 F.3d 883, 903-11 (9th Cir. 2008) (rejecting *LePage's* and holding that bundled discounts are analyzed under the *Brooke Group* predatory pricing analysis); *see also* Herbert J. Hovenkamp, *Discounts and Exclusions, U. Iowa Legal Studies Research Paper No. 05-18*, 16 (Aug. 2005) (Donato Reply Decl. Ex. B) ("A safe harbor test for bundling, or 'coercion,' based on price-cost relationships is essential to analyzing claims of package discounts because . . . only an effective price that is 'below cost' can exclude the equally efficient rival."); Antitrust Modernization Commission, *Report and Recommendations*, April 2007, at Part I.C, 99 (Donato Reply Decl. Ex. C) (recommending that plaintiffs in bundled discount cases be required to prove below cost pricing).

The Eighth Circuit's decision in *Concord Boat* is especially probative. In that case, the defendant offered a contract with tiered "market share" discounts to boat builders based on what percentage of their total boat engine purchases were from the defendant. *Concord Boat*, 207 F.3d at 1044 (80% purchase requirement for maximum discount). There, as here, "none of the programs restricted the ability of builders and dealers to purchase engines from other engine manufacturers" or "obligated boat builders and dealers to purchase engines from [the defendant]." *Id.* at 1045. The Eighth Circuit noted that *Brooke Group* and other Supreme Court decisions "illustrate the general rule that above cost discounting is not anticompetitive." *Id.* at 1062. The court expressly noted that these market share arrangements "were not exclusive dealing contracts." *Id.* at 1063 ("[C]ustomers were not required either to purchase 100% from [defendant] or to refrain from purchasing from competitors in order to receive the discount."). As a result, the Eight Circuit upheld the district court's grant of summary judgment in favor of the defendants. The Court should reach the same result here.

Notably, the cost-based analysis of market share discounts that is applied by most courts is also favored by leading antitrust experts. *See, e.g.*, Herbert J. Hovenkamp, *Discounts and Exclusions, U. Iowa Legal Studies Research Paper No. 05-18*, 6 (Aug. 2005) (Donato Reply Decl. Ex. B) ("[W]hen a discount is offered on a single product (whether a quantity or market share discount) the discount should be lawful if the price after all discounts are taken into account exceeds the defendant's marginal cost or average variable cost."); Daniel A. Crane, "Multiproduct Discounting: A Myth of Nonprice Predation," 72 U. Chi. L. Rev. 27, FN 6 and 48 (Winter 2005) (Donato Reply Decl. Ex. D) ("Above-cost effective prices in the competitive market (after reallocation of discounts from the other markets) should be a safe harbor for any multiproduct firm. Any other legal rule will discourage discounting to the detriment of

consumers."). The rationale for requiring below-cost prices to establish anticompetitive harm due to market share/loyalty discounts is simple. Even when a discount is conditioned on the buyer purchasing *100 percent* of his needs from the seller (which is not the case here), an equally efficient rival can still compete as long as the discounted price is above cost. Herbert J. Hovenkamp, *The Law of Exclusionary Pricing, U. Iowa Legal Studies Research Paper No. 05-34*, 10-12 (Jan. 2006), (Donato Reply Decl. Ex. E).

Since the undisputed evidence shows that Plaintiffs cannot prove Covidien's market share discounts lowered its prices below any measure of its costs (Cov. Br. at 11), Plaintiffs' claims fail as a matter of law under *Barry Wright* and the other cases discussed above.

2. Plaintiffs Have No Authority For Their Position That Exclusive Dealing Standards Apply To Covidien's Discount Programs

Plaintiffs ignore the overwhelming authority applying a cost-based standard to market share discounts and instead rely on: (i) a misinterpretation of *Barry Wright*; and (ii) a handful of cases that do not support their argument.

Plaintiffs argue *Barry Wright* supports their position that an exclusive dealing standard (rather than a below-cost standard) applies. Nothing could be further from the truth. As Plaintiffs point out, in *Barry Wright* the plaintiff challenged three aspects of the defendant's conduct as "exclusionary:" "[1] its offer of special discounts … [2] its insistence on a long-term large-volume contract, and [3] its inclusion of the special non-cancellation clause." 724 F.2d at 230. The first part of the court's opinion addressed aspect [1] – whether the special discounts were "exclusionary" – by applying a cost-based test. Because the discounts were all above cost, they were upheld as not "exclusionary."

Plaintiffs hinge their argument on the fact that there was a second section in *Barry Wright*, which addressed [2] and [3] of the plaintiff's exclusionary claim – contract duration and

terminability – by applying exclusive dealing standards. *Id.* at 236-37. Plaintiffs argue that if Covidien's interpretation were correct, the court "would have ended all analysis with the conclusion that the discounts were above cost." Opp. Br. at 3. Plaintiffs, however, misunderstand the decision. What they fail to acknowledge is that there were two sections of the opinion precisely because there were two types of "exclusionary" conduct at issue – pricing-related and nonpricing-related – and each required a separate analytical framework. The first section was conclusive of whether the *discounts* were anticompetitive. The second section was conclusive as to the non-price terms of the agreements – duration and cancellation. *Barry Wright* thus stands for the proposition that: (i) price-related claims will be *independently* assessed under a cost-based test; and (ii) non-price related exclusionary claims will be *independently* analyzed under an exclusive dealing test.

This is fatal to Plaintiffs' case because the conduct they are challenging as "exclusionary," despite a self-serving and transparent effort to repackage it, revolves *entirely* around Covidien's discounts. In fact, under Plaintiffs' theory of the case, foreclosure arises from allegedly punitive pricing and not from some non-price related contractual provision.[4] Accordingly, under *Barry Wright* the test is whether Covidien's discounts are below cost.[5]

The other cases on which Plaintiffs rely also do not support applying exclusive dealing

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[4] Even Plaintiffs' argument that the contracts are not terminable is not, like *Barry Wright*, based on a non-price term of the contract. Instead, it focuses on the "pricing penalties" (*i.e.*, higher prices) that result from cancellation.

[5] Nor do Covidien's agreements constitute, as Plaintiffs argue (*see* Opp. Br. at 5), "requirements contracts" that *Barry Wright* suggests would also be subject to challenge under exclusive dealing standards. *Barry Wright*, 724 F.2d at 237 (noting that a "true requirements contract" might be an improper exclusive deal because such a contract "flatly eliminates the buyer from the market"). It is well-established that a "requirements contract" is a contract that "*obligated* the buyer to take *all* of its requirements of a given good from the seller." 11 Areeda & Hovenkamp, Antitrust Law, §1800a1 (2nd ed. 2005) (emphasis added); *see also Bacou-Dalloz USA, Inc. v. Continental Polymers, Inc.*, No. CA 00-404-T, 2005 WL 615752, at *10 (D.R.I. Mar. 4, 2005) ("'[R]equirements' contracts commonly are understood to mean that a manufacturer will purchase *all* of the specified material that it uses from the vendor with which it contracts.") (emphasis in original). Under the Covidien contracts at issue here, however, customers are not required to purchase anything from Covidien, much less *all* of their requirements.

standards to single-product discount programs. Indeed, none of the cases cited by Plaintiffs involve agreements with *discounts* conditioned on minimum levels of purchase. For example, in *FTC v. Brown Shoe*, 384 U.S. 316 (1966), at issue were "Franchise Agreements" that *required* retail shoe store operators to buy shoes only from Brown Shoe Company. *Id.* at 318. Thus, *Brown Shoe* concerned a true exclusive deal (*i.e.*, one that requires buyers to purchase only the products of the seller); not, as here, a deal that merely gives customers discounts if they choose to purchase certain amounts of product. Similarly, the contract in *Standard Fashion v. Magrane-Houston*, 258 U.S. 346, 362 (1922) "required the purchaser not to deal in goods of competitors of the seller" and did not condition low prices on purchasing certain minimum levels.

United States. v. Microsoft, 253 F.3d 34 (D.C. Cir. 2001) also does not support applying exclusive dealing standards to market share discount agreements. To the extent *Microsoft* applied an exclusive dealing analysis, it involved contracts entirely unlike and distinguishable from the ones challenged here. *See, e.g., id.* at 68 (addressing agreement with AOL in which "Microsoft puts the AOL icon . . . 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"). *Microsoft* simply did not involve the types of contracts at issue here, under which Covidien's customers could choose to earn discounts by purchasing certain percentages of Covidien product.[6]

Of all the cases Plaintiffs cite, the Third Circuit's opinion in *LePage's v. 3M*, 324 F.3d 141 (3d Cir. 2003) is the only one that involved discounts conditioned on minimum levels of

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[6] Plaintiffs' reliance on *Stop & Shop Supermarket v. Blue Cross*, 373 F.3d 57 (1st Cir. 2004) is equally misplaced. The agreements at issue there required Blue Cross to give all its business to one group of pharmacies for three years and not to deal with other pharmacies. 373 F.3d at 65. This sort of arrangement is not present here, and thus does not support applying exclusive dealing standards to Covidien's contracts.

purchase. But *LePage's* provides no support for Plaintiffs' theory. The contracts at issue in *LePage's* involved only bundled rebates across numerous different product lines and types, not single-product sales of the kind at issue here.[7] *Id.* at 154 ("3M's rebate programs offered discounts to certain customers conditioned on purchases spanning six of 3M's diverse product lines."). Indeed, the court stressed what it believed were the specific aspects of *bundled* rebates in justifying applying exclusive dealing standards rather than predatory pricing law. *Id.* at 155.

In addition, *LePage's* has been repeatedly criticized and rejected by courts and legal scholars. *See, e.g., J.B.D.L. Corp.*, 2005 WL 1396940 at *12-13 ("[A]bsent persuasive authority that the Sixth Circuit would follow *LePage's* and agree with its conclusions, this Court is not persuaded."); *Cascade Health Solutions v. PeaceHealth*, 515 F.3d 883, 897-903 (9th Cir. 2007) (declining to follow *LePages*); 3 Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶749d (3d ed. 2008) (Donato Reply Decl. Ex. F) (criticizing *LePage's*); Joanna Warren, *LePage's v. 3M: An Antitrust Analysis of Loyalty Rebates*, 79 N.Y.U. L. Rev. 1605, 1606 (Donato Reply Decl. Ex. G) ("LePage's was poorly reasoned and has created confusion over what types of conduct by firms possessing high degrees of market share will be found to be predatory and exclusionary rather than legitimate competition on the merits."); Antitrust Modernization Commission Report at 94-100 (Donato Reply Decl. Ex. C) (criticizing *LePage's* on several grounds, including because "[t]he lack of clear standards . . . in *LePage's v. 3M*, may discourage conduct that is procompetitive or competitively neutral and thus may actually harm consumer welfare"); Daniel A. Crane, "Multiproduct Discounting: A Myth of Nonprice Predation," 72 U. Chi. L. Rev. 27, FN 6 and 48 (Winter 2005) (Donato Reply Decl. Ex. D) ("The

[7] While Plaintiffs' complaint makes allegations of "bundling" here, as noted in Covidien's opening brief (Cov. Br. at 6, fn 3), Plaintiffs have dropped those claims. Plaintiffs do not dispute that the only remaining claims in this case concern single-product discounts.

court refers to 3M's conduct as 'exclusionary' fifty-two times, without ever giving a precise definition of that word's legal meaning. The closest we get is an explanation that there are forms of exclusionary conduct other than predatory pricing, which is accurate, but no more helpful than defining murder by saying that homicides other than garroting can constitute the crime.").

The cases Plaintiffs cite do not stand for the proposition that discount programs like Covidien's should be analyzed under exclusive dealing law rather than a cost-based approach. Plaintiffs' claims should be analyzed under the pricing standards articulated in *Barry Wright* and various Supreme Court decisions. Since Plaintiffs do not dispute that Covidien's prices were above cost, summary judgment should be granted.[8]

B. Covidien is Entitled to Summary Judgment Even If Exclusive Dealing Standards Were Applied

Even if Plaintiffs' pricing claims were analyzed under "exclusive dealing" standards, summary judgment should still be granted. The threshold issue under an exclusive dealing claim is whether the alleged contracts amount to truly "exclusive" deals that preclude competition. Cov. Br. at 12. If Plaintiffs cannot prove the contracts are actually "exclusive," then the contracts are deemed lawful. *Id.* Even if Plaintiffs can show exclusivity, they must also establish that the contracts substantially foreclosed the relevant market and harmed competition. *Id.* While Plaintiffs attempt to manufacture a dispute over some of these facts, a close examination of the basis for their assertions reveals no *genuine* dispute exists and Plaintiffs cannot satisfy their burden.[9]

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[8] Plaintiffs' argument that this Court has prejudged the merits of this summary judgment motion against Covidien (which Plaintiffs describe as "law of the case") is simply wrong. *See* Opp. Br. at 11-12. The statements of this court on which Plaintiffs rely came in the context of the Court merely characterizing Plaintiffs' allegations (without adopting them or finding they were true) (*see Natchitoches Parish Hosp. Serv. Dist. v. Tyco Int'l, Ltd.*, 247 F.R.D. 253, 256 (D. Mass. 2008) (the alleged facts are only "presumed true for purposes of ruling on this motion")), and were made at an earlier stage in the case (*see id.*, issued January 29, 2008, and D.I. 169, issued August 29, 2008).

[9] This is especially true in light of the fact that Plaintiffs rely almost exclusively on *statements made by their expert*

1. Covidien's Contracts Do Not Require Exclusive Dealing

An exclusive dealing contract is when a company is required to purchase all its inputs from a single supplier. Cov. Br. at 12 (citing cases). None of Covidien's discounts or contracts require customers to buy all its sharps containers from Covidien:

- Under the terms of the hospital contracts, hospitals are free to buy from a competitor at any time. The only consequence for not meeting a market share threshold is the loss of a pricing discount. *See* Cov. Br. at 4-5.

- Under the terms of the sole-source GPO contracts, hospital members are not required to purchase *anything* from Covidien – the hospital simply has the option of buying products at pre-negotiated, lower prices. *See* Cov. Br. 5; Covidien's Statement of Material Facts ("SOF") Nos. 34-37.

Id. at 13. The terms of the agreements are fatal to Plaintiffs' claims.

Nonetheless, Plaintiffs contend that customers do not have meaningful purchasing freedom because if they switch from Covidien they will face pricing "penalties" so dire that no customer will actually choose to purchase from a competitor. However, Plaintiffs have cited *no* authority for the proposition that losing a single-product discount for future purchases constitutes an "exclusive dealing" agreement. Indeed, *Barry Wright* indicates the opposite is true. The plaintiff in *Barry Wright* had argued the "noncancellation" clauses in the defendants' agreements amounted to a "powerful economic incentive" or "penalty" that made the agreements exclusionary. 724 F.2d at 238-39. The noncancellation clause required the plaintiff to pay the entire price of the yearly order, *e.g.*, $4.3 million. *Id.* The court rejected the plaintiff's attempt to use the economic "penalty" of this clause to "transform otherwise lawful purchase agreements

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– as opposed to actual evidence – to attempt to show a genuine dispute of fact. *E.g.*, Plaintiffs' Response to SOF No. 33 (disputing that GPO contracts were terminable at will on grounds that "externality problems incentivize[d]" buyers to remain in these contracts); *id.* at No. 39 (disputing that Natchitoches was not prevented from buying from competitors on grounds that "economic factors" identified by Professor Elhauge "either prevent or penalize such purchases"); *see also id.* at Nos. 4-6, 28-32, 34, 37, 45-47. Professor Elhauge's theoretical economic arguments and legal conclusions, however, do not constitute "facts" showing a genuine dispute. *See, e.g.*, *Hayes v. Douglas Dynamics, Inc.*, 8 F.3d 88, 92 (1st Cir. 1993) ("We are not willing to allow the reliance on a bare ultimate expert conclusion to become a free pass to trial every time that a conflict of fact is based on expert testimony.").

into unlawful, exclusionary ones." *Id.*; *see also In re Apollo Air Passenger Computer Reservation Sys.*, 720 F. Supp. 1068, 1076 (S.D.N.Y. 1989) (rejecting argument that an otherwise lawful liquidated damages provision was "exclusionary"). The Court should apply the same rationale here and reject Plaintiffs' argument.

Notably, Plaintiffs ignore *Allied*, a case nearly identical to this one. In *Allied*, the court addressed allegations of anticompetitive harm based on Covidien "market-share agreements" and "sole-source agreements" (the same types of agreements at issue here) in the market for pulse oximetry sensors. Applying the exclusive dealing standards Plaintiffs urge here, the court found that "[Covidien's] market-share agreements do not create an unreasonable restraint on competition" because "[t]hey do not contractually obligate hospitals to buy any [Covidien] sensors at all" and "the only direct consequence for a hospital that fails to meet its compliance level is potentially being charged the price that reflects its actual tier level of purchases." *Id.* at 7 (internal quotations omitted).

The *Allied* court rejected the argument made by the plaintiff's expert – identical to that made by Plaintiffs here – that the loss of discounts amounted to the imposition of a "penalty price" and eliminated customers' purchasing freedom: "regardless of whether [Covidien's] discounts represent a penalty price or involve kickbacks to hospitals, they do not 'force' hospitals to do anything." *Id.* at 9 (noting that "[p]articipation in the market-share program is voluntary and can be ended at any time, and hospitals are thus free to switch to more competitively priced [alternatives]").[10]

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[10] The *Allied* court noted that it found an article by Professor Elhauge (that argued the same theory of harm he advances in the present case) to be unpersuasive, "highly theoretical," and contrary to prevailing wisdom. *Id.* at 10, n.10 ("Nor is Plaintiffs' case aided by their citation to Professor Einer Elhauge, *Loyalty Discounts and Naked Exclusion*, [citation omitted]. Professor Elhauge's article, which appears to depart from much of the current literature, argues that loyalty discounts such as market-share arrangements always (or almost always) have anticompetitive effects.").

The *Allied* court similarly found sole-source GPO contracts were not anticompetitive because they "do not require GPO member hospitals to purchase any or all of their oximetry supplies from [Covidien]." *Id.* at 12. In responding to the plaintiff's allegation that the sole-source agreements were restrictive because GPO member hospitals would be forced to "forfeit access to pricing discounts" (*i.e.*, the equivalent of Plaintiffs' claim here that GPO members would incur "pricing penalties"), the *Allied* court stated that the critical fact was "the element of free choice: members of a GPO that have sole-source contracts with [Covidien] can choose not to utilize it at all." *Id.* at 12-13 (additionally noting that, as here, "some hospitals belong to more than one GPO and may have the alternative of purchasing other oximetry brands under an alternative GPO contract").

All of these bases for granting summary judgment in *Allied* are equally applicable here. As if that was not enough, the testimony of Plaintiff Natchitoches' own witness, Stephen Crowder, fundamentally undermines Plaintiffs' argument that customers do not have purchasing freedom. *See, e.g.*, SOF 39 (testifying that [redacted]; SOF 40 (testifying that [redacted]; SOF 42 (testifying that [redacted][11]

Accordingly, even if the Court applies the exclusive dealing standards urged by Plaintiffs, summary judgment is warranted on the grounds Covidien's contracts are not "exclusive."

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11 Plaintiffs response to Mr. Crowder's testimony is that [redacted] Opp. Br. at 5, n.5. But, even accepting that rationale, his testimony [redacted]

2. Covidien's Contracts Have Not Substantially Foreclosed The Market

Even if Covidien's contracts are deemed true exclusive dealing agreements, which they are not, the contracts are not anticompetitive for additional reasons: (1) they do not substantially foreclose competition; (2) the contracts are short term and terminable at will; (3) GPOs are not the only distribution channel for sharps containers; and (4) the evidence (testimony from BD and Stericycle and Covidien's declining market share) shows that competition for sharps containers is thriving. Cov. Br. at 14-18.

Short-Term, Terminable Contracts. Plaintiffs do not dispute that the terms of the accused GPO contracts provide for termination without cause on 90 days. Nor do Plaintiffs dispute that under the terms of the discounting contracts, a hospital may forego the discount and switch to another supplier and terminate the contract. Nonetheless, Plaintiffs' contend the contracts are not terminable at will on the basis that they are only terminable "upon payment of a significant penalty." Opp. Br. at 8; Plaintiffs' Response to SOF 33. But, again, the factual basis for that statement is merely the alleged "pricing penalties" (*i.e.*, higher prices) that would result.

Plaintiffs also argue that the "hospital commitment contracts were not terminable at all" because they do not contain termination clauses. Opp. Br. at 8. To the contrary, the absence of a termination clause shows that these contracts were terminable at will, especially because the contracts did not *require* hospitals to do anything. Indeed, the leading antitrust law treatise concludes that a market share discount agreement, by its nature, "presents a contract of 'zero' duration." 3 Areeda & Hovenkamp, *Antitrust Law* 2008 Supp. ¶ 749b at 149 (Cov. Br. at Ex. FFF). A Covidien customer who no longer wanted to purchase at a "committed" level would suffer no consequences and simply pay prices appropriate for the level of purchases made. *See, e.g.*, *Allied* at 7 (Cov. Br. at Ex. GGG) (rejecting plaintiff's argument that price incentives render market share contracts not terminable at will and finding that "the fact that [Covidien's] sensor

pricing is dependent on commitment level does not suggest coercion or an unreasonable restraint"); *cf. also Barry Wright*, 724 F.2d at 238-39 (rejecting argument that contract clause is anticompetitive due to large cancellation penalty).[12]

Alternative Distribution Channels. Plaintiffs do not dispute that there are multiple distribution channels for sharps containers. *See* Opp. Br. at 9-10. Nor do they dispute that their expert stated that approximately [redacted] of Tyco's sharps container sales are made outside of the GPO channel. *See* Cov. Br. 5, SOF 37; Plaintiffs' Response to SOF 37. Instead, Plaintiffs argue that this fact is irrelevant because, as a matter of law, competitors are legally entitled to access to the most efficient distribution channel. *Id.* at 10.

The overwhelming body of case law (which Plaintiffs ignore), however, establishes that there is no requirement under the antitrust laws that competitors have access to "the most efficient" distribution channel. Cov. Br. at 16 (citing cases).[13] In fact, the law is exactly the opposite: as long as an alternative distribution channel exists, regardless of whether it is purportedly less efficient, even a company's complete domination of one distribution channel does not violate the antitrust laws. *See, e.g., id.; Omega*, 127 F.3d at 1163 ("Competitors are free to sell directly, to develop alternative distributors, or to compete for the services of the

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12 Plaintiffs argue that antitrust law does not consider a contract terminable "if exercising a termination right requires suffering a financial penalty," citing *U.S. Healthcare v. Healthsource*, 986 F.2d 589, 596 (1st Cir. 1993). Opp. Br. at 9. *Healthsource*, however, merely noted that if "a reimbursement penalty" had to be paid to terminate the contract at issue, it might have made it more difficult for the plaintiff to compete. *Healthsource*, 986 F.2d at 596 (further noting that "[n]ormally an exclusivity clause terminable on 30 days' notice would be close to a *de minimus* constraint"). Moreover, Plaintiffs here cite no evidence that any such "reimbursement penalty" would have to be paid; instead, Plaintiffs attempt to equate the loss of discounts with "penalties." Plaintiffs have cited nothing that would suggest a loss of discounts should be treated as a "penalty."

13 Plaintiffs argue that the cases Covidien cited for the proposition that alternative distribution channels show lack of foreclosure were "misleading[]" because they concerned market definition, not foreclosure. Cov. Br. at 16; Opp. Br. at 9. That is simply not true. For example, *Omega Envtl., Inc. v. Gilbarco, Inc.*, 127 F.3d 1157 (9th Cir. 1997) found that "undisputed evidence of potential alternative sources of distribution . . . eliminate substantially any foreclosure effect [defendant]'s policy might have." *Id.* at 1163 ("Contrary to plaintiffs' contention, these alternatives are relevant to assessing market foreclosure.").

existing distributors. Antitrust laws require no more."); *Roy B. Taylor Sales, Inc. v. Hollymatic Corp.*, 28 F.3d 1379, 1383 (5th Cir. 1994) ("Alternative distributors did not have to be robust to compete; they merely had to exist.").[14]

Competition is Flourishing. Plaintiffs also do not dispute that competitors BD and Stericycle have experienced substantial sales growth and that Covidien's market share has declined. SOF 2, 4, 6, 9-13; *see also* Opp. Br. at 10. Instead, Plaintiffs again argue that these facts are irrelevant to an antitrust inquiry. Opp. Br. at 10-11. While these factors alone may not be dispositive, they are significant factors that, when combined with the other undisputed facts, conclusively establish lack of anticompetitive harm here. *See* Cov. Br. at 17 (citing cases holding no foreclosure where defendant's market share declined).

C. Covidien Is Independently Entitled To Summary Judgment Because Plaintiffs' Lack Proof Of A Critical Element Of Damages

Plaintiffs' case should also be dismissed because they cannot, as an element of their antitrust claims, prove damages. As demonstrated in our opening brief, Plaintiffs have utterly failed to determine an essential input into their damages calculations. Cov. Br. at 18-20. Plaintiffs' main response to this fatal defect is to insist that this Court simply ignore it on specious procedural grounds. They invite this Court into reversible legal error by asking that this case go to trial in the absence of a sustainable damages element.

1. Plaintiffs' Efforts To Dissuade The Court From Considering The Merits Of This Challenge Are Baseless

Plaintiffs' procedural objections to summary judgment on this issue are

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[14] *Microsoft* and *LePage's*, which Plaintiffs cite for the contrary proposition (Opp. Br. at 10), merely hold that foreclosure can be found if the *only* viable method of distribution is cut off. *Microsoft*, 253 F.3d at 64 ("[A]lthough Microsoft did not bar its rivals from all means of distribution, it did bar them from the cost-efficient ones."); *LePage's*, 324 F.3d at 160 ("3M's exclusionary conduct cut LePage's off from key retail pipelines necessary to permit it to compete profitably."). Plaintiffs here do not, nor could they, allege that GPOs are the *only* viable distribution methods sharps containers; indeed, the undisputed evidence establishes otherwise. *E.g.*, SOF 29, 36-37.

wholly misplaced. Plaintiffs' principal argument that Covidien purportedly waived, or is judicially estopped, from raising this fatal defect (Opp. Br. at 12-16) is wrong on the facts and the law. The factual basis for this argument is that Covidien made the exact same challenge it makes now in a Daubert motion seeking to exclude Dr. Singer, then subsequently withdrew that motion in an agreement with Plaintiffs. *Id.* The *Daubert* motion, however, raised a fundamentally different issue: the overall "fit" and validity of the NEIO damages model used by Plaintiffs' expert, Dr. Hal Singer. *See* D.I. 179. It is that critique that Covidien agreed to save for trial, if one occurs. Covidien seeks summary judgment on a completely different and non-methodological claim that Plaintiffs cannot provide an essential input into their own damages formula to generate any damages estimates on which a jury could reasonably rely. *See* Cov. Br. at 18-20. That is not the argument that Covidien had advanced in its Singer *Daubert* motion, and thus its agreement to withdraw that motion is wholly irrelevant here.

Plaintiffs' legal objections are equally deficient. Plaintiffs appear to argue that Covidien's challenge should have been, or can only be, raised in a *Daubert* motion. *See* Opp. Br. at 13 ("[Covidien's] summary judgment arguments regarding damages are unquestionably within the realm of a *Daubert* challenge."). That is simply wrong. Courts routinely grant summary judgment in antitrust cases where a plaintiff has not provided proof of a necessary element of its damages. *See, e.g.*, *City of Vernon v. S. Cal. Edison Co.*, 955 F.2d 1361, 1373 (9th Cir. 1992) (summary judgment appropriate where "the serious flaws in the only damage study which could be proffered to the jury placed [the plaintiff] in the position of having no proper proof of damages at all") (citing numerous cases with the same reasoning); *In re Mun. Bond Reporting Antitrust Litig.*, 672 F.2d 436, 443 (5th Cir. 1982) (holding that summary judgment was proper where plaintiff failed to establish a triable issue regarding the 'fact of injury' or 'cause

of injury' elements of damages); *Package Shop, Inc. v. Anheuser-Busch, Inc.*, 675 F. Supp. 894, 951-52 (D.N.J. 1987) (summary judgment granted where expert's computation of damages was flawed and lacked a foundation). Whether Plaintiffs are missing an essential element of their damages proof is simply not appropriate for "consider[ation] by the jury during cross examination *at trial*" as Plaintiffs argue. Opp. Br. at 15 (emphasis in original). If Plaintiffs' claims fail as a matter of law, it would not be proper to have the case heard by a jury. Accordingly, all of Plaintiffs' arguments about waiver, judicial estoppel, and *Daubert* are simply irrelevant.

2. Plaintiffs Cannot Satisfy The Burden Of Establishing the Ability To Prove Damages

Plaintiffs' remaining comments about the purported validity of their overall damages methodology ("the NEIO model") simply miss the point. The question of whether the NEIO is valid is not the issue here. Indeed, purely for summary judgment purposes, the Court may assume the NEIO model is a reliable method of calculating antitrust damages. The issue presented is that Plaintiffs are unable to supply, let alone prove, an essential input into their model: the amount of foreclosure allegedly experienced by rivals as a result of the challenged contracts (*i.e.*, the impact of the contracts on rivals' market shares). This input is required for Plaintiffs to present a non-speculative damages amount to the jury.

Plaintiffs fail to say anything at all in response to the issue Covidien has actually raised. Dr. Singer's damages model depends on two inputs that he obtains from Professor Elhauge: one is the "overall foreclosure share" (*i.e.*, the total portion of the market foreclosed by Covidien's challenged conduct in each year of the class period); the other is the amount of foreclosure allegedly experienced by Covidien's rivals. *See* Elhauge deposition exhibits (Chan Decl. Ex. 47) and Singer damages tables (Donato Reply Decl. Ex. H). It is the *latter* input that Plaintiffs'

experts failed to determine and on which Covidien's summary judgment argument is based. Cov. Br. at 19 (the input at issue is "the amount of foreclosure allegedly suffered *by Covidien's rivals*, or – put differently – the impact of the challenged practices on *rivals' market shares*") (emphasis added). Plaintiffs' opposition brief focuses only on the overall foreclosure share (Opp. Br. at 16-20), which is not at issue. With respect to the element that is actually at issue, the alleged impact on rivals' market shares, Professor Elhauge's testimony could not be clearer: "[W]hat I haven't done, which is the relevant damages question, is quantify the difference between rival shares in the actual world and the but-for world." *Daubert* Hearing Tr. at 106:7-14 (SOF 55). Indeed, when asked whether his calculations were meant to be "a precise quantification of the impact of those share discounts on rivals," Professor Elhauge's response was to the point: "It's not meant to be a precise quantification of the amount of impact." *Daubert* Hearing Tr. 95:25-96:9 (Donato Reply Decl. Ex. I). In other words, Professor Elhauge has made clear that he has disavowed the second input Singer relies on as a precise quantification of the amount of foreclosure suffered by Covidien's rivals.

Plaintiffs' assertion that this fatal omission should be ignored because Dr. Singer "performed an independent audit" of Professor Elhauge's market foreclosure estimates is also completely off-point. This "independent audit" was limited to conducting a purely mechanical check on whether the calculations were done correctly. Singer Dep. at 49:15-17 (Chan Decl. Ex. 8) (testifying that with respect to his "audit" of Professor Elhauge's work, "[b]asically any of the inputs that I was relying on, I wanted to make sure there were no calculation errors"). The dispositive fact is the admission that he performed no "independent audit" of Professor Elhauge's methods. *E.g.*, Singer Depo. at 118:12-119:4 (SOF 54) ("I have not been asked, nor

have I formed an independent opinion as to whether Professor Elhauge's calculation of the differential in rival penetration was the appropriate analysis.").

Plaintiffs' claim that "Dr. Singer did, in fact, independently and precisely translate the "'foreclosure share' into the but-for market" is equally unavailing. Opp. Br. at 18. Dr. Singer's report establishes otherwise. He states that he calculated rivals' but-for market share simply by multiplying two inputs he received from Professor Elhauge, the "overall foreclosure share" and the "amount of rivals' foreclosure." Singer Report at ¶58 (Chan Decl. Ex. 6) ("I multipl[ied] the increase in rival penetration from the foreclosed to the non-foreclosed market by the overall foreclosure estimate."). The accuracy of that final calculation is dependent on the accuracy of the two variables that went into it. Dr. Singer never "independently and precisely" determined the accuracy of the second variable, the amount of rivals' foreclosure. *E.g.*, Singer Depo. at 63:11-64:21 (SOF 54) (testifying that he "turn[ed] over . . . the role of estimating the magnitude of foreclosure to Professor Elhauge" and that he was "not asked to prove foreclosure," only to "convert that foreclosure, assuming that it occurred . . . into a but-for price").

Plaintiffs failed to determine a crucial input for their damages case, and thus are left with damages claims that are nothing more than pure speculation. Summary judgment is appropriate under such circumstances. Cov. Br. at 18-20.

III. CONCLUSION

For these reasons, Covidien respectfully requests that summary judgment be entered in Covidien's favor on all of Plaintiffs' claims.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that the foregoing was filed through the ECF system will be sent electronically to the registered participants as identified on the Notice of Electronic Filing (NEF) and copies will be sent to those indicated as non-registered participants on September 15, 2009.

/s/ *James Donato*