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of the

ANTITRUST LAW SECTION

January 25, 2007
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Introductory Remarks

MS. GOTTS: Good morning, if I can ask everyone to get a seat. We want to start on time because we have a full program.

My name is Ilene Gotts and I am the Chair of the Antitrust Law Section of the New York State Bar Association, and this is our Annual Meeting.

As I said, we have a full day planned, and I'm going to turn it over in a minute to the Program Chair, but we will have a full program in the morning.

Right before we break at lunch we will have a representative of the New York Bar Foundation come and speak for just a few minutes about some of the good programs they have going on.

We will then break for lunch, and then after lunch have another session. Then, hopefully, we will see many of you tonight at the dinner, which is at the University Club. It's the first year we are moving it there.

I'd now like to introduce our Program Chair, who will be the Chair of the Section next year, or starting this evening: Saul Morgenstern. He is a partner at Kaye Scholer.

Saul?

MR. MORGENSTERN: Thanks, Ilene.

We wouldn't be here today if it weren't for the immense amount of work that Ilene has done. And I would like to just quickly thank Ilene for what she's done this past year for the Section. We'll say more about that tonight at the dinner.

Let me add my welcome to today's program. We have a program today that will cover, I think, a number of bases in antitrust, very interesting topics. We'll start this morning with our first program, which is the Annual Review of Antitrust Law, which will be delivered by Molly Boast.

Molly is a partner at Debevoise and Plimpton. She is a well-recognized expert in antitrust and a truly versatile lawyer and counselor. She served in the Bureau of Competition at the FTC from 1999 to 2001, first as Senior Deputy Director then as Director. She led the Commission's successful litigation challenges, for example, to the BP/ARCO and Heinz/Beech-Nut mergers, among other matters. Ms. Boast oversaw several significant litigation challenges to patent settlement agreements in the pharmaceutical industry, and she continues to this day. She also served as the agency's representative to the joint European Union/FTC/Department of Justice Mergers Working Group. In 1993, she presented the argument on extraterritorial application of the antitrust laws before the United States Supreme Court in *Hartford Fire v. State of California*.

In 1992, in a nod to her diverse capabilities, she was appointed Special Assistant United States Attorney for the Independent Counsel Investigation of Banca Nazionale del Lavoro, otherwise known as the "Iraqgate" scandal at the U.S. Department of Justice.

Since returning to private practice at Debevoise, she has represented pharma companies, credit card companies, entertainment companies and others in price fixing investigations and in litigation. She's assisted companies in merger matters in connection with FTC investigations and proceedings, and coordinated international antitrust investigations and transactions.

She is a frequent speaker and writer on antitrust subjects.

Please welcome Molly Boast.

(Applause.)

Annual Review of Antitrust Developments

MS. BOAST: Well, I'll add my welcome to that, and thank you very much, Saul, for the unbelievably overgenerous, flattering and mostly untrue introduction.

The real hero of this morning's presentation, besides the litigants in the trenches and in our government agencies, is my colleague and advisee, Rosa Castello, sitting in the second row, who has prepared the written materials you have in your handout and also the Power Point, and helped me make some judgment calls about what we should focus on this year.

We've labeled this "Greatest Hits," and we actually spent some time but ultimately abandoned the effort to try to key our choices of what might be of interest to counselors in this field to the "*Rolling Stone*'s 500 Greatest Albums of All Time." But we thought you would find our sense of humor pretty strained, so we gave it up.

In thinking about greatest hits this year, I should make the observation that, although there were a number of decisions—and all the appellate level decisions are covered in the written handout—there weren't that many cases that we felt really advanced the ball.

So what we are covering today are the few we thought were actually important, a few unusual cases—whether they are really important or not remains to be seen—a couple of cases that just had funky facts, and some highlights of the agencies' output.

Let's turn first to the case law, then. We had three Supreme Court decisions in the antitrust field this year, and I don't propose to discuss all of them. I believe the Robinson-Patman decision, the *Volvo Trucks* case was discussed last year. We'll touch briefly on the *Dagher* case, which also, I believe, has been discussed in the past.

I don't want to rerun all the facts because people are probably pretty familiar with them. This involved a joint venture between Texaco and Shell in which they pooled their downstream resources to form a company called Equilon. They retained both the Texaco and Shell brands and priced similarly across the company and then were sued by service station owners for price fixing.

After the district court had granted summary judgment, the Ninth Circuit, in its usual wisdom, reversed.

The Supreme Court gave us a very clear statement in a very simple, straightforward opinion that joint ventures are presumptively to be treated under the Rule of Reason and overruled the Ninth Circuit.

The most interesting of this trio of Supreme Court cases last year, of course, was *Illinois Tool Works*, a tying case. In this case Illinois Tool was a company that sold patented print heads and had an alleged tie in the purchase of unpatented ink. The plaintiff in this case had developed the same ink and was challenging this arrangement. The issue was whether there was a presumption of market power arising from Illinois Tool's patent in the print head. The district court had granted summary judgment for defendants and then the court of appeals reversed.

Again, we finally got a clear statement from the Supreme Court that the patent does not necessarily confer market power and the presumption under which some courts, at least, have labored was now abandoned.

The decision is definitely worth more attention than we can give it here today. We'll discuss a couple of the cases that followed *Illinois Tool Wooks* to see what's happened with the decision, since it's been out for several months. But it basically puts the burden on the plaintiff to prove market power in the tying product in all these patent cases. The real question, I think, will be how much one can read into this decision outside the patent context.

The Court was essentially abandoning its own precedents in this area. How did it do this? This is the part of the decision that's really interesting. First of all, it went back to its own cases and said, "Well, all along, we have really been talking about this as though it were a Rule of Reason approach."

Secondly, it noted that after the Supreme Court had decided *Jefferson Parish*, Congress had gone back and amended the Patent Code to eliminate the presumption in the patent misuse context, and said this certainly invites a re-appraisal of the per se rule.

Third, it went through some of the academic and economic literature, and they all pointed to a Rule of Reason approach.

Finally, the Court noted that the FTC and the Department of Justice in the Intellectual Property Guidelines also stated clearly they did not believe a patent should necessarily be assumed to confer market power, and that a traditional Rule of Reason approach to market power should apply.

The Seventh Circuit decided a case after *Illinois Tool Works* that is not particularly interesting for its facts. It involved a property listing service to which realtors had access if they were members of certain National Board of Realtors–recognized organizations. And again, the defendants won this case on a summary judgment motion in the district court.

In this case, the court of appeals affirmed the district court, noting that under Seventh Circuit precedents, the Rule of Reason analysis had been incorporated long ago, and since in this particular case there was only one participant in the tied market, there couldn't be tying. It is a little bit bizarre. There was a discussion about whether there were effects on potential competition, but it didn't lead anywhere.

Our friend Judge Wood, known to many in this room, wrote a concurring opinion in which she makes, I think, the correct observation, that perhaps the court is getting a little bit ahead of the Supreme Court's decision in *Illinois Tool Works* because that case didn't expressly abandon per se treatment outside the patent context. She didn't disagree with the final analysis since there was only one competitor.

The second case that applied *Illinois Tool Works* was one with funky facts. It involved a type of soybean that had been developed by Monsanto. Monsanto licensed this technology, and sold these patented seeds but allowed growers to grow one crop. But of course, how could they control their intellectual property rights if people could just go out and sell their patented seeds? So they had a no re-plant policy. There were also license agreements that required, at least for a certain period of years, use of an herbicide that Monsanto also had manufactured called Roundup. And this gave rise to a tying claim.

The court of appeals, again, affirmed the summary judgment that had been granted by the lower court, and said that the case was a straightforward application of the patent misuse doctrine and therefore the *Illinois Tool Works* rule applied.

Moving away from the tying cases, there were several decisions on standing this year. This is one of the areas where we concluded that it was not worth dragging you through all of the decisions because they weren't particularly—they were intuitively obvious standing issues, and they were not going to advance our learning that much.

The principal one of interest in my view is a case out of the Eleventh Circuit, *Gulf States Reorganization v. Nucor Corp*. This case arose in the bankruptcy context. Gulf States had filed for bankruptcy and was selling its assets. Nucor had 85 percent of the market in this particular product, and instead of actually bidding for the assets itself, it funded a bid by a group that had been put together called Park. Park won the bid, I should say. Another bidder sued, claiming, of course, that this was really Nucor with its 85 percent market share getting these assets in the market. Nucor ended up selling the assets and not holding them for itself. It justified its position by saying it was really buying these assets just to make money.

The district court found that the challenger, this other bidding group, lacked standing. The court of appeals reversed, saying that the injury to the bidding group was inseparable from the injury to competition because it intended to enter the market and compete with Nucor by virtue of the fact that Nucor sold the assets. Nucor denied consumers the benefit of the competitive entry.

In the only really fun language we could find in the cases this year, one of the judges said he was "concurring in part and, perhaps, dissenting," being unable to parse the majority decision. He believed that Nucor's justification—that it was selling the assets so it was "no harm, no foul"—really affected a different market and had no role in the Rule of Reason analysis. He believed that the company alleged a straightforward antitrust violation that Nucor was protecting its monopoly by precluding a competitor from acquiring these assets. I think the one thing you can say with certainty about a decision like this is that strange things happen in bankruptcy court when antitrust issues arise, as we have seen on many occasions.

This was an interesting case that I think is worth discussion since so many of the antitrust practitioners in New York are litigators as opposed to regulatory lawyers. This case involves a court struggling with how to treat inferences that could be drawn where there is actually direct evidence of conspiracy as part of the litigation. It doesn't really lend itself to simple treatment in this kind of presentation, but it does raise some interesting questions in an area where, at least as the court describes the precedents, there is mixed or little guidance.

In this particular case, the parties were competing service centers in the aluminum industry. The plaintiff had some quotations or statements made by one of the distributors saying that the distributor and others would source their metals from other mills if the mills sold to Champagne, the plaintiff here. The district court had granted summary judgment, saying that the plaintiff's theory didn't make economic sense. The court of appeals went into a discussion of how to deal with the fact that there was direct evidence of this distributor's statement. But it was incomplete. It was insufficient to prove the conspiracy because it didn't tell you who was involved. It didn't identify the parties. Therefore some circumstantial evidence was also going to be required.

The court went on to look through the precedents and said that some courts, when there's been direct evidence, have not required an economic justification or rationale after direct evidence was introduced; this was sufficient to get the case to the jury.

But in a situation where you couldn't really prove the conspiracy based on the direct evidence, what do you do? So the court finally punted. This court went to the next step and decided that the conspiracy was economically rational and then remanded the case to the lower court to determine whether taking the direct, the circumstantial evidence together created a genuine issue of material fact.

So it doesn't give us, again, clear guidance for the future. The one thing I do feel about this case is I'm not sure they were really reading the precedents properly. But clearly there was some concern that the bar was set too high by the district court in the summary judgment decision.

There was not that much of interest in the Second Circuit this year. We thought that one case worth spending a little bit of time on was the case that involved lumber distribution and termination of one of the distributors in favor of an exclusive distributor. The terminated distributor, of course, sued.

The court said this was really a "one monopoly rent" case. The vertical arrangement provided no monopolistic benefit to Doman, the monopolist, that it didn't already enjoy, so there was no harm to competition.

One of the other things we looked for were cases where we might be able to discern some divergence of views between circuits so we could see if there were cases that might be heading for the Supreme Court. I'm not sure this one will qualify, but you may remember last year—those of you who were here—we discussed the Second Circuit's decision arising out of the tobacco Master Settlement Agreement, *Freedom Holdings v. Spitzer*.

This is the Sixth Circuit's run at the same sort of bundle of issues. Just to refresh everybody's recollection a little bit, under the Master Settlement Agreement, states were required to adopt certain complementary legislation, basically to encourage participation by non-signatories and to prevent the principal participants in the settlement from being competitively harmed.

So in Kentucky an escrow statute was enacted that required manufacturers that weren't main signatories to the Master Settlement Agreement either to join it or to deposit money based on their cigarette sales into an escrow account which would later go back to them under certain circumstances.

The competitive harm alleged in this case was that one of these non-participating manufacturers asserted that the whole scheme encouraged participating tobacco manufacturers to keep their prices high because that would decrease their market share and therefore decrease their contributions, while at the same time, the nonparticipating manufacturers, who were paying into this escrow fund, didn't ultimately see the same reduction in their payment obligations. And the issue was one of preemption. The district court declined to hold that the Sherman Act preempted the Kentucky Escrow Statute. It relied on its own earlier preemption decision case, a case called *McNeilus Truck*, which held that state law must actually authorize or require behavior that is prescribed by the antitrust laws before preemption can apply. It specifically addressed the Second Circuit's decision in *Freedom Holdings v. Spitzer*, but rejected it because the threshold used in that decision was too low. The Second Circuit had said the complementary legislation need only allow or permit the proscribed conduct before preemption was appropriate.

Our friend 3M continues to litigate based on its exclusive arrangements. This is sort of an interesting case because of the analytical approach the court used. Again, not to our economist friends, I'm assuming this is the result of some clever economic testimony. This involved a product, an automobile abrasive product in which the plaintiff had a 67 percent market share and 3M was the only other meaningful competitor. The purchasers of this product tended to enter year-long contracts and switched buyers only at the end of those contract terms. So 3M came in with a multi-year exclusive discounting program and ultimately NicSand went out of business. That's, of course, what gave rise to the suit.

The interesting discussion is the court of appeals saying that you can operate on the assumption that retailers wouldn't insist on exclusive arrangements if they weren't going to gain from them somehow. But the problem with that assumption, the majority said, is that the retailers could fall prey to collective action problems, where the retailers are making assumptions about what other retailers might do. So they might incorrectly assume that other retailers would or would not act or would or would not obtain benefits they might obtain, without, of course, having the conversation with them, and behave accordingly.

Therefore the issue, ultimately, really was a standing issue. But it was this analytical discussion that was interesting. The majority said that NicSand, the now-out-of-business competitor, had standing because it stood as a proxy for all competitors due to the fact that now only 3M was in the market.

The dissent framed this issue around the collective action analysis, saying that the fact that retailers signed these longer term contracts and got better prices showed that they had sufficient bargaining authority and there was no reason to try to interpolate the notion there was a collective action problem operating.

Another decision in which there is the potential circuit split—although I'm not sure the Supreme Court would have much more to say on this point—involves monopoly leveraging. Again, this was a relatively unremarkable case in some ways. It involved a patent held by Abbott for a product that is also used in combination with another product. The plaintiff had a complicated theory about how pricing in one market was allowing the defendant to price in the second market through monopoly leveraging. This case was decided on a motion to dismiss by the district court which granted the motion. The court of appeals affirmed and expressly stated that it was joining the

Federal Circuit in rejecting the Ninth Circuit's approach in the *Kodak* case because there is no freestanding theory of monopoly leveraging.

I included this case. It doesn't really tell us anything about antitrust law. It just happens to be a favorite topic of mine, as Saul noted in his introductory comments. This was a decision under the Hatch-Waxman Act actually, in a situation in which Mylan had been approved to sell a generic version of the Proctor & Gamble product, and then Proctor & Gamble launched an authorized generic product. Under the Hatch-Waxman Act the Court said Mylan had no claim because there was nothing in the statute that precluded the launch of an authorized generic during the 180-day exclusivity period.

This is a very hot topic at the FTC right now. As you may have read in March, the FTC announced they would do a study of the long- and short-term effects of authorized generics. There's a lot of discussion within the industry, I think, about this topic because there are many who believe that it's not in the branded company's interests, for a variety of reasons, to launch an authorized generic. But at the same time, they are free to do so.

As recently as a few weeks ago, Commissioner Leibowitz was heard suggesting that legislation should be enacted to prohibit the launch of authorized generics during the exclusivity period. This is the kind of issue that I could imagine being quite controversial even within the Commission because of the obvious argument that it is just more competition and that, if there is no prohibition on it today, why shouldn't the consumers get the benefit of competition during the exclusivity period?

In one of the few cases that I actually found really interesting, we have this—be careful what you wish for—an extended, elaborate and fascinating discussion of the interplay between arbitration law and antitrust law. This involved an arbitration provision in Comcast's agreements with its subscribers. Comcast sued on antitrust grounds and moved to compel arbitration on grounds of retroactivity that are not particularly important to our discussion. When the case reached the First Circuit, the Court got around the retroactivity problem and then had to confront the main issue which was: Did this arbitration clause contravene a fundamental federal antitrust policy because there were provisions that shortened the statute of limitations, precluded treble damages, precluded the recovery of attorneys' fees and precluded class treatment?

The questions were framed as whether each of these points should be decided by the court in the first instance or could be decided by the arbitral forum. The First Circuit went through each of these issues separately.

First of all, it concluded that the statute of limitations really was a factual question and could be decided by the arbitral forum and therefore spent no time on it.

But when it got into the discussion about the bar on attorneys' fees and treble damages, it concluded that these terms did indeed contravene federal antitrust law and, therefore, raised a question of arbitrability that the court itself could decide. But looking at the arbitration contract itself, the court noted there was a savings clause that said if the law would require that these provisions not be enforceable, then they would be severed. Therefore, treble damages were available and attorneys' fees were available.

Similarly, when it reached the discussion of class treatment, the court concluded that the deterrent effect of precluding class treatment in this area was so strong that there was a question of arbitrability. It said the complexity of these kinds of cases and the risks involved in litigating them discourage individuals from pursuing the claims and that the costs to attorneys for taking on these cases made them even less appealing. Therefore class treatment was appropriate.

So what to do with the arbitration provision since the agreement, again, by its own terms, allowed a severance of clauses that were not enforceable? The court allowed the arbitration to proceed as a class arbitration. So at the end of the day, what Comcast got out of this clause was an arbitration on a class-wide basis involving attorneys' fees and treble damages with the statute of limitations to be decided in the arbitral forum. The case raises a question about whether you could ever really draft an arbitration clause that would allow you to deal with a simplified version of antitrust claims.

The *Stolt-Nielsen* case is one we have talked about before, but it happens to be one of my favorite so I thought we should finish the story of *Stolt-Nielsen*. This was a fascinating situation in which Stolt-Nielsen had applied for leniency based on price-fixing activity. They had a conditional leniency agreement with the Antitrust Division. In subsequent investigations, the government found that Stolt-Nielsen had not withdrawn the conspiracy in accordance with the government's expectations and therefore withdrew from the contract and prepared to indict the company.

Stolt-Nielsen went to court and got the district court to issue an injunction against the indictment because it said there had been no determination that there had, in fact, been a breach of the contract between the government and Stolt-Nielsen, that is, the conditional leniency agreement.

The case went up to the Third Circuit, which I think reached the right conclusion, and said the district court didn't have the authority to prevent the government from indicting. There were many special rights that attached to the defendant at this stage, and the argument that there was a contractual right or a contractual obligation that

the Antitrust Division held was something that could be raised either in an application to dismiss the indictment or in a criminal trial itself.

We have at this point four cases pending, in one fashion or another, in the Supreme Court. So in a little bit of a preview for some of the things that, no doubt, will be discussed next year, oral argument has already been heard on the *Twombly* case, which arises out of the Second Circuit and raises an important question about what allegations are sufficient to withstand a motion to dismiss in the conspiracy context. The Second Circuit essentially said, "We are not going to rely or make the analysis turn on allegations about plus factors at this stage." This is contrary to what I think a lot of people have felt for a long time. Whether it is the right rule of law, I'm not so sure. It is definitely symptomatic of the Second Circuit's extreme distaste for motions to dismiss.

The second case on which argument has been heard is the *Weyerhaeuser* case, which raises a predatory bidding claim, whatever that is. The Court has been asked to decide whether the same standards apply to predatory bidding as apply to predatory pricing. Here, again, we are beneficiaries of the Ninth Circuit, which came up with its own test, and which will now be under review by the Supreme Court.

More recently, the Court granted *certiorari* in the IPO market allocation case where the issue for the Court will be implied immunity. In this particular instance, the other product of the Second Circuit, with the Second Circuit starting to sound a lot like the Ninth Circuit, the district court had said that implied immunity was appropriate because the SEC either permitted or regulated the IPO process. The Second Circuit thought that standard was too broad and vacated and remanded on a much narrower standard. The United States, in its own brief to the Supreme Court, disagreed with both standards. It thought that the district court standard was too broad and the Second Circuit standard, interestingly enough, was too narrow. The brief goes through a very interesting discussion of the standard as set forth here on the slide and how it might operate under certain settings.

And finally, the Court also recently agreed to hear a vertical minimum resale price case. Again, the facts here are not all that interesting, but the defendant, Leegin, lost this case in a jury trial. On appeal, *Leegin* challenged the application of the per se rule and use of it in the jury instructions. But the court of appeals said, "Dr. Miles is still out there; we are not in a position to abandon that."

So, again, the United States filed a brief in which it takes the position that the Court's precedents, as we saw when we started out with the *Dagher* case and as we saw with the *Illinois Tool* case, we've increasingly moved toward the Rule of Reason as the appropriate approach. That ought to be the case in vertical resale price cases because the actual effects can be either pro/or anti-competitive. And only the Rule of Reason allows us to determine that.

Let's move to some of what the government did in 2006. This slide stands here for two purposes. One is to remind everyone, as you probably already know, the FTC, the Commission overturned the ALJ's decision in the *Rambus* case, finding that Rambus's conduct violated the FTC Act.

Rambus has been discussed in this room many times, but it involved an alleged failure by Rambus to disclose to the standard-setting organization, of which it was a member for a time, that it had a patent that would be infringed if a certain standard were adopted. That standard was, in fact, adopted and Rambus began collecting royalties.

The second reason I included this was to talk about the approach to standard-setting that this particular organization uses, which is called the RAND approach: Reasonable and Non-Discriminatory royalty terms. So the notion is if the disclosures are properly made in the standard-setting process, the group can come up with a royalty provision that won't unlevel the playing field for everyone who is going to be incorporating the standard in its products.

One other interesting thing about the Commission's decision here is that they reached their conclusion by finding deception under the FTC Act, which seems an odd place to park this case. But in any event, this is a case I actually started when I was at the FTC, so I'm quite happy with the result.

In contrast to the RAND approach that the *Rambus* case reflects, the Department of Justice issued a business review letter giving clearance to another standard-setting organization called VITA. This involved what they referred to as ex-ante licensing. VITA is, again, operating in the high-tech sphere and had developed standards that include patented technology. Its approach is different, and it was this approach that was up for review in the business review context.

VITA required patent holders to disclose their most restrictive licensing terms if their standard were to be selected, so that everyone knows what would be the maximum, the highest price, of whatever the terms will be. The government said this disclosure would decrease the chances of ambush later on. There are also many protections built into this process that I didn't set forth here but that are described in the business review letter itself. It also observed that this system creates incentives for patent holders to come in with terms that are essentially competitive because they presumably would like to have their standard selected.

Quite recently, Deputy Assistant Attorney General Masoudi gave a speech in which he goes through this en-

tire standard-setting area and makes the observation that you shouldn't assume that, if you do or do not comply to the letter with the VITA approach, you're on one side or the other of the law. I didn't read this as threatening. It was really intended, I think, to say, "There are many ways to go about this."

This next case was just a lot of fun to read. The very short complaint by the FTC in this consent motion was an invitation to collude in a case involving a company called Valassis and another company called News America. They make freestanding newspaper inserts.

They had been in a price war, and so Valassis made a company announcement of how it was going to deal with this and set forth very deliberately: "I'm going to take my customer base and I'm going to keep it. And people who stick with me will get the benefit of this kind of pricing," very elaborately laid out. Valassis then said, "We are going to be paying attention to what our competitor, News America, does." And basically, in almost these words, the statement said: "If News America goes after our customers, we'll return to competing them into the ground." This case serves as a reminder that our services are still needed.

I included the Maytag and Whirlpool merger in here not because it was so remarkable but just because, looking back on my own experience in the government and with mergers since then, I think we are at the point where the kinds of arguments that didn't used to have traction seem to have traction, at least in certain markets today. One is that there are foreign manufacturers that have capacity and shipping costs, even for relatively bulky things like appliances, have become sufficiently low and certainly manufacturing costs are lower, that imports are now a real threat in certain markets, a real competitive threat.

Secondly, the government noted that there are buyers out there—these products are not sold directly to consumers by the manufacturers—that have very substantial bargaining power. Again, an argument that Wal-Mart has buyer power was the flavor of the day in the late '90s and early part of this century and was never really acknowledged by the government, but seems to be today.

Finally, there were a number of publications by the government this year. The one that I think is most important doesn't lend itself to really fast treatment here. The Department of Justice issued guidelines on how to obtain the benefits of cooperation if you're not the "first in" under the leniency program. It goes through a very detailed discussion of what the rewards would be, mostly various adjustments to the Sentencing Guidelines. DOJ makes it very clear that this is just—they can't give you bright-line rules the way they can with first-in policy because what they are concerned about is the proportional value of the cooperation that you might offer. And that proportionality means: What did they get on the first round? What have they gotten through independent sources?

So DOJ will have to assess cooperation in the context of the state of their investigation at the time, and whether there is really something new being offered. Suppose you were the person who came in on day two, when somebody else had gotten in on day one, and you've done everything that the first applicant had and you would still advance the investigation.

I think DOJ wants to keep the incentives out there, first of all, for cooperation in this area. And secondly are concerned that firms are holding back, because why should they stand up if they are going to be twelve hours late and get nothing for it? But this document is definitely worth a read and is something to keep in mind in counseling your clients.

And the FTC, of course, published its non-enforcement, but interesting, discussion of Noerr-Pennington, a favorite topic of the former Chairman's. And the Commission did a pretty good job, I think, at least from their perspective, in isolating the areas where they think Noerr arguments have been made inappropriately. They clearly carve out the political arena because they don't want to get involved there.

We also had the DOJ's merger review process amendments, which are similar to but not the same as those published by the FTC earlier. The agencies published an interesting commentary on the Horizontal Merger Guidelines which doesn't tell us all that much, but certainly is an educational tool for thinking about where certain arguments might and might not work.

The last thing I wanted to touch on was the tentative recommendations of the Antitrust Modernization Committee. These recommendations were published earlier this month and are preliminary. But the chances that they'll change in significant respects, with a few exceptions, are not high. So they are worth a little review, bearing in mind the Commission has neither enforcement authority nor legislative authority. It is simply a set of recommendations to Congress.

The tentative recommendations show a consensus among the commissioners that fundamental merger policy is where it should be, and that there be no change in Section 7 of the Clayton Act. They conclude the courts are managing to grope their way through Section 2 analysis and, therefore, there should be no fundamental change there. They conclude that the states' role in both merger and non-merger matters should remain unchanged, and that the treble damages remedy should remain intact and the availability of attorneys' fees should remain intact.

Where there also seems to be consensus for change is in repealing the Robinson-Patman Act and in repealing

Illinois Brick and replacing it with a scheme that would, first of all, try to get all of the cases into federal court and then limit the damages to the measure of damages available to the direct purchasers but provide—since all parties theoretically would be in one forum—for an allocation between direct and indirect purchasers in that court.

The third thing I thought was of interest, and I think it is probably a compromise, is whether dual enforcement between the Department of Justice and the Federal Trade Commission should continue. I think the compromise here is that in the merger area, the AMC would suggest that the Commission has to litigate its cases in federal court rather than obtaining a preliminary injunction in federal court and then returning to the administrative court for a full adjudication of the merger. That would have the practical effect of creating the same standard for preliminary injunctions for the FTC and DOJ, which is probably not what the law is today.

Where there seems to be a division that remains to be sorted out, and I'm not even sure how important this is, is there's a clear divide on the role of efficiency in merger analysis, notwithstanding an overall consensus that merger enforcement is where it should be.

There are many places in this set of recommendations where there are Supremacy Clause issues, where there are suggestions that the states should be positioned one way or another or not. I don't know how a federal Congress does that.

And finally, there are many places where the AMC opines on how they'd like the courts to treat something. For example, one of the recommendations under consideration is that during the time awaiting the hoped-for repeal of the Robinson-Patman Act, courts should require a showing of injury to competition that parallels that which we see in the Rule of Reason cases. The AMC, besides the fact that this Commission can't enforce the laws or make the laws, can't tell the courts what to do. So it is a wishful thinking sort of approach. It is an interesting set of questions, and if you know any of the personalities involved, their specific positions on anything that's in controversy are set out in the footnotes.

That was all I had for this morning. Any questions comments or hopefully discussion among you?

Well, thank you very much then.

(Applause.)

MR. MORGENSTERN: Thank you, Molly. And we now have a break before the next session, which is actually scheduled to start at 10:00, so you can have coffee and phone calls. We'll see you back here.

Robinson-Patman Litigation and Counseling After *Volvo*: New Plaintiffs' Burdens or Business as Usual?

MR. MORGENSTERN: Welcome back to our unprecedented ahead-of-schedule program.

In today's environment of large power buyers and the ever-increasing adoption of suppliers and multi-faceted approaches to marketing and distribution products and services, it is more essential than ever that practitioners remain vigilant to a host of counseling and litigation issues, including those raised by the RP Act, as recently interpreted by the Court in *Volvo Trucks against Reeder-Simco*. It is not often that we see Robinson-Patman cases of that size make it to the Supreme Court. We are quite interested in following that along.

This panel will discuss the implications with *Volvo* including whether the Court has significantly modified the injury-to-competition requirement for establishing liability, the nature of economic evidence required to establish whether an alleged purchaser should properly be considered a power buyer, what new defenses may have been created, and what impact the decision will have on the continued vitality of the now famous *Morton's Salt* inference.

The discussion will also address related issues as loyalty programs, slotting allowances, and the interplay between the RP Act and the Sherman Act.

Our panel, litigators who represent plaintiffs and defendants in RP cases, an economist and an inside counsel from Wal-Mart, will use a hypothetical to explore the practical business and legal considerations presented by the case, including the use of M&AP programs and the implementation of suggested retail price policies in connection with Internet sales.

Our panelists are as follows:

Panel Co-chair and Moderator Larry Fox is Co-chair of McDermott Will and Emery's Distribution and Practices Strategy Group and Chair of the Antitrust and Competition Practice Group of the firm's New York office. He represents clients in investigations, litigations and trials commenced by private plaintiffs as well as federal and state antitrust authorities. His litigation and counseling practice focuses primarily in the areas of antitrust, distribution, e-commerce and intellectual property. And he's been involved in a number of nationwide antitrust class actions and distribution and advised clients of distribution areas throughout the years. He has written extensively on antitrust and speaks frequently for both the Antitrust Law Section of the ABA and this Association.

One of my first antitrust cases 25 years ago was against Larry and one of my more recent cartel cases was with Larry on my side. I learned something from him both times. I suspect you will today.

The panel is co-chaired by Barry Brett of Troutman Sanders and Richard Steuer of Mayer Brown Rowe & Maw. Barry is the Practice Group Leader of Troutman Sanders' national and international antitrust practice and past Chair of this Section. He concentrates on antitrust and trade regulation, product distribution, pricing, dealer termination and patent issues. He has represented domestic and foreign clients in such diverse businesses as theater, popular music, pharmaceutical, cosmetic products, computers, paints and chemicals, labor unions, retailing, food manufacturing and distribution, and ball bearings. I could go on.

Richard specializes in antitrust litigation, counseling and M&A at Mayer Brown. He's written a book, dozens of articles and lectures frequently and is regularly quoted in the press. He has served as Chair of the Trade Regulation Committee of the Association of the Bar of the City of New York, Secretary of the ABA Section of Antitrust Law, Editorial Chair of the *Antitrust Magazine*. He is currently a Section Delegate at the ABA House of Delegates, has taught antitrust at NYU and St. John's, and is a member of the Advisory Board of Antitrust and Regulation of the Court.

Jeff Kessler is at Dewey Ballantine in New York. He's the Co-chair of the firm's Litigation Department and one of its leading antitrust lawyers. His concentration is in antitrust, sports law, IP and other complex litigation. He's a leading expert in international antitrust law, has litigated some of the more complex antitrust and sports and IP cases, including *McNeil against the NFL*, which led to the establishment of free agency. Whether you like that or not depends on your perspective on football. Jeff is currently Adjunct Professor of Columbia University Law School and has written and lectured extensively on international trade and U.S. antitrust law, and he has recently published a new edition of leading treatise in that area. He was previously Co-editor-in-Chief of *State Antitrust Practice and Statutes* and formerly a member of the Council, Co-chairman of the Publications Committee and Chairman of the International Antitrust Law Committee of the ABA, and a member of the ABA's NAFTA Tri-National Committee.

Howard Kitt is Vice President and senior advisor of CRA International. He specializes in antitrust and trade regulations matters. He was the founding Chair of NERA's US Antitrust, Trade Regulation, and Healthcare Group as well as its Global Antitrust and Competition Policy practice through 2004. He's prepared studies on the nature of product and geographic markets and their relevance to Sherman and Clayton Act litigation and analyzed the competitive impact of mergers and acquisitions, including pricing and trade practices, industry structure and performance. These studies and analyses have been undertaken for a wide range of consumer goods and industrial equipment suppliers.

And finally, certainly not least, Paula Martucci is Director of Merchandise Compliance of Wal-Mart Stores, Inc., putting these principles in practice on the ground every single day. She's responsible for regulatory compliance in areas of product development, packaging, competition and consumer protection. She joined the Wal-Mart Legal Department in 1996, managed litigation, counseled on a broad range of merchandise, operating and operational matters. Before joining Wal-Mart, she served as a prosecutor and practiced law with firms in Dallas and Topeka, Kansas. She's a member of the Editorial Board of the ABA Antitrust Section's *Practice and Statutes*, Fourth edition. It will come out in 2009, and she recently served as Vice Chair of the Section's RP Act Committee.

Please welcome this illustrious panel.

(Applause.)

MR. FOX: Good morning.

Last year two highly significant events occurred involving the Robinson-Patman Act which may have profound implication for the future enforcement of the Act and certainly has raised significant issues affecting all practitioners and counselors who must advise clients regarding the requirements of the Act.

First, the Antitrust Modernization Commission recommended that the Robinson-Patman Act be repealed in its entirety. Second, the Supreme Court issued its decision in *Volvo Trucks* [*North*] *America v. Reeder-Simco* [*GMC*], in which Judge Ginsburg, writing for the Court in a 7-2 opinion, reversed the Eighth Circuit Court of Appeals' affirmance of the district court's $1.3 million verdict on behalf of Reeder, a Volvo truck dealer and the Robinson-Patman plaintiff in that case.

In doing so, the Court may have imposed upon plaintiffs significantly new burdens in satisfying the injury-to-competition requirement in a secondary line-injury claim under Section 2(a) of the Act. Today's panel, utilizing a hypothetical problem, will address the range of legal, strategic and practical implications of the *Volvo* decision.

Before introducing the panel, I will briefly provide a very brief sketch of the Act, its requirements, the views expressed about it before the Antitrust Modernization Commission and the Commission's ultimate recommendation to repeal the Act. Finally, I will provide a brief description of the *Volvo* decision and some of the provocative questions that it raises.

First, with respect to the Act, as you know, it was passed in 1936 as an amendment to Section 2 of the Clayton Act. One of the Act's express purposes was the protection of small retailers against price favoritism shown by manufacturers to large chain buyers where the discrimination might substantially lessen competition. In sum, Section 2(a) of the Act prohibits discriminatory pricing among competing buyers of goods seeking to sell those goods to the same customer.

In essence, to establish a prima facie case of liability a plaintiff must show that

1) a seller charged different prices to two buyers
2) in connection with one sale at least that was an interstate commerce
3) of commodities—not services—that
4) were of like-grade and -quality, and—and this is the important injury-to-competition requirement or prima facie case—this discriminatory sale must have the effect of substantially lessening competition—might
5) have the effect of substantially lessening competition, or—there's a big "or" there—injure, destroy or prevent competition with a person who grants the discrimination—that's called primary line injury, where the competing—a competitor of the discriminating seller is injured, that's primary line injury, or the person who receives the benefit of the discrimination, the favored buyer. That's competition between the customers of the discriminating seller, that's called secondary line injury, and that's the kind that was involved in the *Volvo* case.

   This last component is the component called injury-to-competition. It has generated the most intense litigation involving the Robinson-Patman Act and was the central question in the *Volvo* case.

The controversy regarding proof of injury to competition in a secondary-line case often involves one of the following issues:

1) When is an inference of injury to competition permitted under the Supreme Court's 1948 *Morton Salt* decision?
2) When and how is such an inference rebutted?
3) Whether it is sufficient for a plaintiff to allege that it has been injured in its competition with

the favored buyer. Is that sufficient? Or must a plaintiff, as part of its prima facie case, establish and plead that indeed the discrimination had an anticompetitive effect on interbrand competition in a market as a whole?

And the circuits are divided on this.

The Act itself, let's talk about the history and where we are with the Act as far as its characterization. I think that there is no single antitrust law that, since its inception, has been more controversial and, indeed, maligned than the Robinson-Patman Act. If one was to survey the literature—including the testimony before the Modernization Commission, of all the antitrust practitioners, government agencies, academicians and economists—and wrap it into one statement that most of them have expressed about the Act, this hypothetical statement would sound something like this: The Act is a confusing tangle of inconsistent and often incomprehensible regulations that thwarts, rather than promotes, consumer welfare.

Indeed, since its adoption, the Act—there have been efforts to repeal it. It has consistently been criticized widespread. Yet, efforts in the past have been unsuccessful in re-appealing it or reforming it.

Last year, the Antitrust Modernization Commission decided in May to recommend that the Congress repeal the Act in its entirety. In doing so, this was the finding of the Modernization Commission, and I quote, "The Robinson-Patman Act is likely to harm competition and consumer welfare by prohibiting or discouraging price discrimination that lowers prices to consumers; protecting competitors rather than competition; and increasing costs of doing business, and thereby likely raising prices to consumers in a variety of ways."

On January 2007, the AMC circulated its "Executive Summary" and its "Tentative Recommendations" and maintained the recommendation to repeal the Act in its entirety.

With a Democratic Congress and grassroots appeal, with the desire to protect small business from large buyers, it is certainly an open question as to whether the Act will find a receptive congressional audience sufficient to repeal the Act. So it is imperative, and I think we will see that it will be part of everyday life for a counselor and practitioner to remain extremely vigilant regarding the requirements of the Act.

So despite the relative abandonment of enforcement of the Act by the federal antitrust agencies, the report of the Act's imminent demise, I think, indeed, is premature. In fact, there were 41 federal cases last year dealing with the Robinson-Patman Act. That's an increase over 2005. Thirty-three of those decisions were in the district court and eight were in the courts of appeals, including the Second, the Fifth, the Sixth, the Seventh, the Eighth, Ninth, Tenth and the Eleventh.

I note for you: There is a decision that was rendered last month by the Second Circuit in *E&L Consulting Limited v. Domain Industries*, 206 U.S. appeal Lexis 30842. I can give you the cite. But the notable thing about it is that it affirms a dismissal, 12(b)(6) dismissal of a Sherman Act and Robinson-Patman 2(a) claim, never mentioning *Volvo* and never mentioning *Twombly*, within the Second Circuit and dismissing on 12(b)(6) Sherman and Robinson-Patman, saying there were inadequate allegations of injury to competition. And among the allegations in the complaint was that the activities of the defendant would raise prices to consumers and reduce available supply to consumers, affecting the market. That wasn't sufficient for the Second Circuit.

So I think, within the Second Circuit, there is a real question as to how vital *Twombly* is, and I think they clearly recognize that the Supreme Court was concerned about that decision.

Moreover, the Act continues to be a real concern for counselors responsible for assisting clients to comply with the Act's requirements. The fact that counselors are concerned about this is proven by a footnote in the Modernization Committee's report. It reported that companies that provide programs for CLE credit reported that the highest attendance of all instruction are those regarding the Robinson-Patman Act and how to comply with it.

Let me give you a brief thumbnail of the *Volvo* case and Rich Steuer will give you additional information concerning it during his presentation.

First, what did the case involve? The case involved special-order, heavy-duty trucks purchased through customer-specific competitive bidding. This is not a case where you had sales from inventory and discriminatory sales between two competing purchasers. The plaintiff, Reeder, was a Volvo dealer that bid in competition with other, typically non-Volvo, dealers to sell to truck-fleet owners. Reeder claimed that Volvo was seeking to eliminate it as a dealer by granting larger concessions to other Volvo dealers in connection with their bids to supply customers, notably, when they were not competing with Reeder, the plaintiff.

The Court, reversing the Eighth Circuit's award for Reeder, held that Reeder had not established a Robinson-Patman violation, finding insufficient evidence of competitive injury. Specifically, Reeder was not bidding in competition with other Volvo dealers for specific customers in head-to-head competition. The Court noted that Reeder alleged only two instances where it bid against another Volvo dealer. And in those instances, Volvo had a policy and followed the policy of essentially following equal pricing treatment where there was head-to-head

competition. Where Volvo had deviated slightly, there was basically potential damage to Reeder of $30,000 on the sale of 12 trucks.

The Court said that differential was not of a magnitude sufficient to affect substantially competition between Reeder and the favored dealer.

In explaining its decision, the Court noted that the favored purchasers were not alleged to have market power. And that those favored buyers bore no resemblance to the chain operators that gave rise to the Act.

In addition, the Court's opinion acknowledged that the original purpose of the Act was to protect small retailers from powerful buyers, but the court said we should resist any interpretation of the Act which provides more protection to competitors than the stimulation of competition.

And the Court admonished against adopting any interpretations of the Act that were not consistent with the broader principles underlying the antitrust laws. What were these broader principles? It cited to their 1977 decision in *Continental TV*, stating that the purposes underlying the antitrust laws were to foster interbrand competition. Now, that's important since, essentially, the Robinson-Patman Act is an intrabrand restraint. Now, they are basically saying, "We can't interpret the Act if it's inconsistent with the general purposes of the Act, which is to foster interbrand competition."

So this decision raises a series of very significant, provocative questions that will affect litigators and counselors.

For example, has the decision essentially de facto repealed the Act by erecting barriers that, in reality, are an insurmountable burden for plaintiffs to establish competitive injury? Must a plaintiff establish that the favored purchaser was a "power buyer" with market power as a prerequisite for utilizing the *Morton Salt* inference for proving competitive injury in a secondary line injury case?

What is a power buyer? How does one measure the power? At what stage of the litigation must it be alleged and ultimately proven? Does *Volvo* mean that a supplier may freely price and discriminate among its customers, so long as it has a significant number of customers and each of them possesses a very low market share? This and others will be among the issues discussed by our panelists.

First, Rich Steuer will provide a detailed explanation of the *Volvo* decision and his views on its implications for counselors and litigators and how he believes it does change the landscape.

Then Jeff Kessler will present his views, which is a contrary view to Richard, pretty much business as usual.

Then Barry Brett will introduce the first stage of our hypothetical problem and some or all of our participants will comment on the issues raised in the hypothetical at each stage of the fact pattern.

Then Paula will play, throughout, the role of President and General Counsel of our hypothetical company and will discuss the practical everyday legal and counseling question that the problems arise: How does this play out in the real world? How does one counsel a client?

And finally Howard Kitt, our resident economist, will discuss what are the statistical methods to be used to establish competitive injury in a bidding situation. And how does one prove a discrimination sufficient to establish anticompetitive injury in the post-*Volvo* market?

We will be taking questions and answers. I'd appreciate if people would write their questions down. At the end, we can read those questions.

Now, I'm pleased to present Richard.

MR. STEUER: When I started out in the antitrust field, one of the first matters I was given to work on was a Fair Trade case that was left over because the Act had already been repealed. And I said, "Oh, no, please don't let me start my career having to learn about a repealed law." Well, I suspect there are a lot of young lawyers at the antitrust bar today who are saying to themselves, "Please don't put me on a Robinson-Patman case."

I agree with Larry. I don't think the predictions of the Act's demise are fair, but it's amazing how every time those of us who deal with distribution regularly think the law has reached a state of equipoise, things change. The ground is moving under us with things like the Internet. And now one can't ignore what may be on the horizon with the *Leegin* case, which may mean that we are in a world where you can have resale price maintenance. We will get into that as we discuss this.

What I do want to talk about today is largely the *Volvo* case, and that is going to be the vehicle for our going through a hypothetical, which will open this up to a range of distribution issues.

Volvo really raises two questions that we will be looking at. The one that everybody anticipated *Volvo* was going to address, the one that was front and center: First, may a supplier offer one dealer better prices than another dealer when those dealers bid against each other and only one of them can win the bid and make the sale? The question that's come up over and over again is: Can both of them be purchasers for purposes of meeting the statu-

tory requirements if only one of them is actually going to buy the goods and resell them, because they are bidding against one another? That's the easy question.

The second question is: Does the Robinson-Patman Act still prohibit anything that is not also prohibited by the Sherman Act? Or does the Court's decision basically say that you must have what amounts to a Sherman Act violation today to have a Robinson-Patman Act violation because of injury to competition? And as we'll see, *Volvo*, at the very least, leaves the answer to that question in some doubt.

It is important to understand that, prior to *Volvo*, there were really two views on both of these issues. There were two views on whether both bidders could be purchasers. One view among the courts was that, in bidding contests, only one company is going to emerge as a purchaser because only one will win the bid and then buy the goods that are resold. The other school of thought was that if the loser makes any purchases from the supplier, it is a purchaser, even though in this one instance where it loses the bid because it has been discriminated against, it is not a purchaser. That does not mean it is not a purchaser for purposes of the statute.

The second debate within the courts is what's necessary to show injury to competition under the Robinson-Patman Act. One school of thought was that injury to a single competitor that is material suffices to meet this requirement. The other is that after the Supreme Court decided *Brooke Group*, which was a primary line case, not a secondary line case that under the same reasoning applying to secondary line cases, there must be injury to market-wide competition.

An example of the first school of thought was one court that said that there is a critical distinction between the prima facie elements of the Sherman Act, where there is a need to adequately allege an actual adverse effect on competition as a whole in the relevant market, and the Robinson-Patman Act, where a plaintiff need not similarly allege injury to competition. Other courts applying *Brooke Group* said that, no, there must be injury to competition.

The courts in the first camp said if you apply *Brooke Group*, that would, in effect, make the *Morton Salt* inference invalid. So that's one of the things we are going to be examining today: What, if anything, is left of *Morton Salt* after *Volvo*?

Now, the facts of *Volvo* were more than a little bit unique. As we often encounter in analyzing cases, it's not your typical case that the Court always chooses to make the law. So we struggle because 90 percent of the situations in which we need to give advice don't look very much like *Volvo*.

First of all, these were custom-made trucks. The trucks weren't manufactured until the order was placed, until someone won the bid. These weren't coming out of inventory. This was the kind of situation in which there could only be one seller because this was done on a custom-made basis. Most of what we deal with today is not in the realm of custom-made goods.

Second, this was a bidding situation. This wasn't a situation where somebody had a storefront and waited for customers to walk in the door and you didn't know who the customers might be or who you're competing against. When you are operating a store, you know you're in competition with a lot of other stores. But continuity is needed, as in a bidding situation, where you can track who is doing the bidding and what the bids are.

There were exclusive territories in that each of these dealers had its own area of responsibility in which it operated. That is not the same as in many situations where we have people who are either in the same location or location doesn't matter very much. We are in the world of the Internet now; but nobody buys a custom-made truck over the Internet.

Next, even though there were these exclusive territories, there were no territorial restrictions, which meant the dealers theoretically could compete against one another. Occasionally, the Volvo dealers did, but they were spaced far enough apart that it was really quite a rare occurrence. But theoretically, it was possible. So you didn't have the situation that you sometimes have in a Robinson-Patman analysis that you don't have competing purchasers because each one is in its own silo, each one is in its territory and can't go against the others. Here, they could compete against each other, at least in theory.

There was evidence that Volvo had too many dealers and that led to favoritism in pricing. We talk about power buyers, and of course, the initial example from the 1930s with A&P was that all the decisions to favor one customer over another were precipitated by the power of the buyer. Here, it was a little bit different in that the evidence showed that Volvo thought it had too many dealers. Although in another world, it might just fire the ones it didn't like, it was facing state franchise law that made it impossible to simply terminate dealers for no reason. So what it did, instead, was decide to discriminate against some. At least, those were the facts of record. Again, this is not your typical situation as far as a motivation for why a supplier would favor one customer over another.

As I mentioned, there was almost no head-to-head bidding here, even though it was theoretically possible. What happened at the trial is that the jury awarded half a million dollars under the Arkansas Franchise Act and also recovery of 1.3 million under the Robinson-Patman Act.

The court of appeals affirmed, finding that the losing bidder did qualify as a "purchaser" even though it obviously didn't buy the custom-made trucks that would be delivered on that bid, but it bought other trucks that it then resold when it was bidding against non-Volvo dealers. The dissent thought this was a flawed analysis and that you cannot piggyback a non-purchaser transaction—that is, when it was the losing bidder—onto purchaser transactions and say you have competing purchasers. The dissent said, in this type of situation, there's only going to be one purchaser.

The Supreme Court reversed 7-2, with Justices Stevens and Thomas dissenting. The majority criticized the plaintiff in the case, saying that the plaintiff only looked for instances in which it was disfavored. It didn't look for instances in which it was favored. There was no statistical analysis whether plaintiff was favored on average as compared to other dealers.

Now, whatever else you may think about *Volvo* and however we come out in terms of what it means for injury competition, this is pretty spot-on in terms of what the rule is going to be in terms of what you need to show for injury. And whether it is injury just to the plaintiff or injury to the market as a whole, the point is this: The discrimination has to be discrimination on average. You can't just pick and choose those instances in which a plaintiff was disfavored if in many other instances it was favored. If you're favored on odd days of the month and disfavored on even days, you can't just pick the ones in which you paid a higher price and say, "Well, I've got a Robinson-Patman case."

The Court said the hallmark of competitive injury under Robinson-Patman is diversion of sales of disfavored purchasers to favored purchasers, and under *Morton Salt* this may be inferred from a significant price discrimination over a substantial period of time. Now, that's pretty standard textbook Robinson-Patman analysis. Remember, of course, that *Morton Salt* was not a private damages case under Section 4 of the Clayton Act. It was an FTC Act case under Section 5 of the FTC Act. So that's something to bear in mind right there.

But the *Morton Salt* inference certainly is something that the court pointed to and did not criticize—that injury to the plaintiff may be inferred from a significant price increase over a substantial period of time. Now it is an inference, which means it is rebuttable. Let's not forget that. And we'll see that that's important.

The majority said the plaintiff failed to show competition with favored dealers for the same customer on the facts. It criticized the plaintiff, saying there was no systematic study, and you cannot draw the inference of injury to either the plaintiff or competition, presumably, from a "mix-and-match, manipulable set of evidence." You can't cherry-pick. The Court then declined to reach the issue of the application of the Act of competitive bidding for custom-made products. In other words, what seemed like that easy question: Are they both purchasers? The Court skipped over that one. Instead, the Court held that the head-to-head competition in this case between the allegedly favored and disfavored purchaser was not sufficiently substantial, nor was the magnitude of the alleged discrimination sufficiently substantial. In other words, the Court hit two items there, using the word "substantial" both times. The first one is: Was the amount of competition substantial? Are there only two instances where they bid against each other? So that was not substantial. And was the magnitude of the discrimination substantial? In one instance, there was no discrimination. In the other, it was both *de minimus* and after the fact. So what one can take away from this is there are really two buttons to press in terms of substantiality: Is it substantial competition and is it substantial discrimination if there is substantial competition?

Plus, then the Court said—and here is the part we will be focusing on quite a bit: The Court held there was not a showing of injury to market-wide, interbrand competition, which is the primary concern of the antitrust laws, because there was no evidence that any favored purchaser possessed market power.

Now, where we may have some disagreement is the import of this coda onto the end of the opinion. As I see it, this is not dictum. This is an alternate holding. What the Court said in the opinion is: Even if the Act's text could be construed in the manner urged by Reeder and embraced by the court of appeals, we would resist interpretation here, orders of protection of competitors and competition. So if, in fact, this is an alternate holding, what the Court is saying is: Well, even if Reeder is right about that first part on the discrimination, still, it hasn't proved market-wide impact. The Court cited *Brooke Group*, which requires market-wide competitive injury, and held that it would decline to extend Robinson-Patman's governance to cases in which there was no injury to interbrand competition, and price discrimination actually might foster interbrand competition. In other words, what the Court perceived is that the supplier here may have been favoring one dealer in order to make that dealer more competitive against other brands. And that's a good thing.

The effect of this is to limit liability in secondary line cases to instances where the favored purchaser: 1) poses market power, and we will talk more this morning about what exactly that means; and 2) gets favorable pricing that does not foster interbrand competition.

These cases may be rare. I think that is one of the things that we will find out as the case law unfolds post-*Volvo*. But how many cases will there be where the favored purchaser does have market power, is some kind of power buyer, and gets favorable pricing that's not fostering interbrand competition when you balance everything out?

There was a dissent. The dissent said, "Hey, it looks like what the majority is doing here is saying, absent head-to-head bidding, there can't be competitive injury." That may very well be what happened.

The dissent also pointed out that it is unclear whether the majority opinion applies to sales from inventory. This is terribly important because most of what everyone deals with is competition among people who are selling out of inventory, not bidding for customers. What the dissent said is: This is for Congress to decide. The majority has re-written the Act and that's just improper.

A few things we come away with: It seems price discrimination is defensible for failure to cause the requisite injuries to competition if it promotes competition against other brands—interbrand competition—even if it injures the ability of a particular dealer of one brand to compete.

Morton Salt applies to injury under Robinson-Patman, but does it apply to injury under Section 4 of the Clayton Act? This, I think, is one of the least clear aspects of the Court's analysis. Is the Court saying that this substantial injury to interbrand competition is an element of the Robinson-Patman Act—that you can rebut the *Morton Salt* inference by showing that this actually fosters interbrand competition? Or is it really saying, "Well, once we do the Robinson-Patman analysis, now in a private case you have to do a Section 4 Clayton Act analysis, and there you surely have to show impact to market-wide competition and specifically to interbrand competition."

You could argue both sides of that one. The analysis in the opinion, I find, doesn't really make an effort to draw this distinction and explain what the basis is, but you could read it either way.

Plaintiffs are required to prove that they were disfavored overall on average in comparison with other competing purchasers. In other words, the no cherry-picking rule. I think this one is pretty clear.

Under Robinson-Patman, discrimination must be substantial and substantially affect competition between favored and disfavored purchasers. This is the takeaway, again, from the Court's use of the word "substantial" in these two different ways.

What's the practical effect? The real question that most of us need to face every day is: What do you tell dealers bidding against each other? Obviously, *Volvo* is going to have an impact in litigation on cases that have already happened, but what a lot of what folks need to do day-to-day is counsel on how not to become the test case. And I suspect that a lot of the counseling—and that's a lot of what we'll talk about this morning—is going to be somewhat cautious until the courts have had a chance to spin out exactly what the effect of *Volvo* is. On custom-made goods, Volvo obviously offers a lot of guidance, more than it does on inventory, but again, it is not that often we are going to be dealing with the arcane world of custom-made goods and competitive bidding for them.

There is also another area we will touch on, which is when the supplier is asked to make a bid to somebody downstream and that bid may result in its favoring that buyer over another. This is a somewhat different bidding situation. *Volvo* doesn't teach us very much about it, but it is something that comes up under Robinson-Patman as well, and it's important to understand there's more involved than just the kind of scenario with dealers bidding against one another.

And with that, let me turn this over to Jeff, who I know has a somewhat different view of the effect of *Volvo*. And then what we're going to do is undertake to look at the hypothetical and try to apply this in more practical terms.

Thank you very much.

(Applause.)

MR. KESSLER: Good morning.

The Robinson-Patman Act is like that great villain in a B movie—every time you think he is dead, he is still there. You could shoot it; you can knife it; you can drown it; you could pass 400 reports recommending its elimination. It doesn't make any difference. And it doesn't make any difference, frankly, to anybody in this room because the bottom line is: The Act is here; the chances of Congress repealing it approach zero. I would never say zero, but they approach zero as a political matter. And *Volvo* teaches you nothing as a counselor. So we could all go home now.

But let me tell you how I get to that conclusion because, again, I think it would border on malpractice—and I will say that—to counsel a client that you can now rely upon *Volvo* as having announced some fundamental change in Robinson-Patman Act law, which means you now don't have to worry about price discrimination unless there is market power or power buying or any of the other requirements that would affect interbrand competition.

Now, does that mean that every one of those issues will not get litigated in the case? Of course they will. They'll get asserted; there will be motions to dismiss; there will be arguments on appeal. But this is litigation that will take place after the problems have happened. If you want to avoid litigation, you're not going to help yourself by relying upon any of these points as defenses.

Let me read to you something, an interesting quote. It comes actually from *Volvo*, and what the quote says is: "Cautioning against Robinson-Patman constructions that extend beyond the prohibitions of the Act and in doing so help give rise to a price uniformity and rigidity in open conflict with the purposes of other antitrust legislation."

That's the new reasoning of *Volvo?* That's the dramatic change? That's why we should change all of our counseling? That's actually a quote from *Automatic Canteen v. FTC*, a decision by the Supreme Court in 1953.

This idea that there is something new in the last section of *Volvo* that, when you are construing the Act, you should try to avoid a construction which conflicts with the broader purposes of the Sherman Act and the antitrust laws, goes back, at least, to 1953. Shortly after I graduated law school, I was just learning about antitrust, it was announced again in 1978 and 1979. These are not new concepts. None of this has ever changed the *Morton Salt* inference.

The *Morton Salt* inference applies in a secondary line case; that's when you have competition between the purchasers, or for that matter, a tertiary line case—which is still alive, by the way. In *Volvo*, they talk about tertiary line price discrimination, which is completely inconsistent with any idea of reading the Sherman Act into this.

Whether it's a secondary line case at the purchaser level or the next line, the inference remains that if you lose customers or profits to your competitor, if you can show diverted lost sales or profits, or you can show substantial discrimination between competing purchasers over time, then you get an inference of "competitive injury" as the Robinson-Patman Act uses that term, which is a "reasonable possibility" of competitive injury.

Nothing has changed. It didn't change in '53. It didn't change after *Brooke*. It didn't change after all the efforts to repeal the statute. And it certainly didn't change after *Volvo*. *Morton Salt* is quoted and cited with favor, not with criticism, not once, but three times in the *Volvo* decision.

Rich says the last part of the decision is an alternative holding. It is not an alternative holding; it is an alternative dictum. If you read the first part of the decision, before Section 4, it is a textbook description of *Morton Salt* and the inference to prove injury to competition. By the way, that's all dicta, too, because that wasn't what the decision turned on.

Section 4 is thrown in. If you read this opinion, it appears that someone who first drafted this opinion, ended it at Section 3. Read the decision and you will see that.

So where did Section 4 come from? Well, I'm not an expert on the dynamics of the Supreme Court, but it possibly came from one of two places. It either came from the clerk, who had an idea to throw out and maybe took an antitrust course one day with Easterbrook or Posner or something like that. It has nothing to do with the decision. You can't piece it together.

Rich is being kind when he says there's not a lot of analysis as to how you apply this. There isn't any analysis. It is a statement, a free-flow of ideas of basic Section 1 principles, but it has nothing to do with the opinion.

The second possibility is that there were a couple of justices who needed to move into the majority and wrote a different opinion, possibly a concurring opinion, and they pulled out a section and put it in the majority opinion in order to get some required votes. One day, 15 years from now, when somebody else releases a set of papers, the way it happened a few years ago with Justice Marshall, we'll actually know where this section came from. I doubt it came from Justice Ginsburg herself.

So what did *Volvo* hold? Well, you start out by asking: What was the question in *Volvo*? It is interesting, Rich put up two questions. The first was the question about two purchasers, and he said everyone thought the Court was going to answer that. The Court didn't reach that. The Court made very clear it was not deciding the issue as to whether the Act applies at all to competitive bid situations without two purchasers. He said that's the easy question. The easy question the Court didn't answer.

What did the Court answer? The Court answered the question it identified. If you look at what it did, it answered the following: We granted review on the federal claim to resolve the question whether a manufacturer offering its dealers different wholesale prices may be held liable for price discrimination proscribed by the Robinson-Patman Act absent a showing that the manufacturer discriminated between dealers contemporaneously competing to resell to the same retail customer. That was the question. And what that means is, in a bid situation, do you have to have discrimination between companies who were actually competing for the bid?

The real issue in *Volvo* is then how do you define competing purchasers? That's the issue that was answered. In fact, the court goes on to say in that very paragraph: Competition of that character—talking about a bid situation—ordinarily is not involved when a product is special-ordered and sold in a customer-specific competitive bidding process.

So what *Volvo* teaches is not a surprising point at all, that if you have a custom bid situation and you have retailers competing for that custom bid, what you have to do is give the same price only to those retailers who are actually bidding for that customer at that time.

What happened in *Volvo* is that it was a failure of proof. The plaintiff put in evidence that those were two instances of competition. One time the plaintiff received the identical price. No discrimination. The other time, it was given the identical price, the bid was awarded and then the winning bidder got a better price, went back to Volvo and said, "I need a little bit more, I should get a better price." But it clearly had no effect on the competition.

What is so surprising about that holding? There clearly was no impact on competition. There clearly was no discrimination in that case.

Contrast this with what the Court describes as the purposes of the Robinson-Patman Act. I find that interesting as well. If you want to talk about alternative dictum, the court talks at length about the fact that the Robinson-Patman Act came from concern over large buyers, which of course it did—and to protect competition in that circumstance. In fact, the decision talks about the fact that the Act was intended to protect independent stores competing with the A&Ps of the world.

Why is that significant? Well, first of all, the Court reaffirms where the Robinson-Patman Act comes from, concern over large buyers. That has nothing to do, by the way, with market power. We have some very good economists here, including Howard Kitt, and I'll ask Howard: "Did A&P have market power in any defined market you can think of in the 1930s in order to exercise that as a power buyer?" The answer is going to be: No. Any kind of market share analysis—

MR. KITT: I just want to know if you were implying that I was around at that time?

MR. KESSLER: No, I am not. Were you?

The point is this: There is no evidence that A&P had market power in that sense. It was a big buyer. That's all. It had a lot of sales. So it used that power to get a discount. That's what the Court was talking about. Now, the Court contrasted that with the situation here in *Volvo.* In *Volvo,* the allegedly favored purchaser was just a dealer. It had no particularly large volume of sales and, in fact, there was no evidence of price discrimination.

So what does this mean? Is *Volvo* going to dramatically change counseling? It better not if you want to keep your client safe. Is *Volvo* going to change the nature of Robinson-Patman litigation? Yes, it will make it more costly, more expensive to litigate a Robinson-Patman Act case. Is that a good thing? For lawyers, it is a good thing. It is not going to be particularly good for clients because it has injected a new level of uncertainty in a statute that is already so filled with cracks and crevices and odd doctrines that it is very difficult and expensive to litigate. So, I'm not sure that *Volvo* is a good thing at all with respect to counseling.

Finally, in the outline, I talk a little bit about one case I'm involved with, which is the *Feesers* case in the Third Circuit. My guess is that you'll get very little insight into *Volvo* from the *Feesers* case or some of the other cases that are pending. Why is that? Because I don't think it is terribly applicable. The *Feesers* case involves traditional out-of-inventory purchases and resales with undisputed evidence—because it is not disputed on appeal—of substantial price discrimination over time.

In that situation, which is exactly the *Morton Salt* inference, it's not clear to me that *Volvo* is going to have any particular impact at all. I could be surprised, but I will be very surprised if the Third Circuit goes in that direction.

Mark Twain said: The reports of his death have been greatly exaggerated. I think that's true of the Robinson-Patman Act as well. But, does the Robinson-Patman Act make sense? Is it a rationale way to interpret it in this manner?

The answer is that it depends on your objective. If your objective is pure economic efficiency in a micro-economic sense, then no, the Robinson-Patman Act makes little sense. That's what people struggle with, and that's why the courts say, "Let's be sure we don't interpret it too far out to interfere with the Sherman Act." That's where that comes into conflict.

But what the courts have also recognized, over and over again, comes back to the fact that pure economic efficiency is not what Congress meant or wanted. Congress enacted the statute because it believed it was creating a more level playing field. It did not want buyers with greater purchasing power to get advantages over their competitors. Period. Who could change that? Congress could change it. I began by saying the chances of that happening approach zero. So do I think any of this will change? No. Will we be back here ten years from now again talking about the demise of the Robinson-Patman Act? I'm sure we will be, and I don't expect any change.

Thank you.

(Applause.)

MR. STEUER: Let me make two quick points if I may. If you want to search for where that last part of the opinion came from, I think you need look no further than the arguments the government made.

In terms of *Morton Salt*, my only point really is: Can you reconcile the reliance on *Brooke Group* with the continued citation of *Morton Salt*? That's really the challenge.

MR. BRETT: I'm delighted that we have been able to clarify for everyone here where the law is now on Robinson-Patman, and how you approach counseling when each of us gets the call from our clients saying, "Gee, I've got a customer out there and I can make a sale of about $20 million, but I've got to give them a much better price than I've given to anybody else. Must I refuse that sale? Are you going to tell me I can't take the order?" And after we go through the questions about. "Well, are you meeting competition? Do you know what any of the other buyers are doing? Who else is out there?" And when that inquiry adds no clarification, and we talk about the Robinson-Patman Act and its purposes, none of us are going to be very comfortable starting to talk to the client about *Morton Salt* inferences and impact on competition and those other issues.

What we would like to do now is to use a hypothetical to provide some guidance as to day-to-day counseling in an area that all of us confront with some regularity. I think in terms of risk/reward ratios, we will ask Bernie Persky and some of his colleagues in the class action bar whether they will bring a class action Robinson-Patman Act case anymore or whether they will routinely decide it is too difficult in light of *Volvo* and other cases. I'd be interested to hear how that's being approached these days. Or is it likely much of the Robinson-Patman issues are going to still come up in a litigation context when you have an allegedly disfavored purchaser, being sued for failure to pay or going into bankruptcy, and you have a bankruptcy trustee or someone else coming in and looking for ways to raise problems? How real is the problem?

Now, to try and focus some of the counseling and issues that we have to deal with in Robinson-Patman and related matters, we have created a hypothetical which we have also gone to some great expense with graphic art to try and display to you.

MR. FOX: It is in the volume at page 113, I believe?

MR. BRETT: The hypothetical is built around a company called Moozik, which creates a new product which is a trendy music and video player. As it comes out with the product and introduces it initially, it sells only through its own stores. The stores are located in malls, high-end urban shopping centers, and in fact, at this point is selling only at the retail list price it established. It's not discounting or otherwise.

They have no competing buyers or sellers, should not be any Robinson-Patman issues, or any other resale price maintenance or any other issues. It doesn't sound like it is going to create any antitrust problems. Unless someone has a different point of view, I think all of us would be comfortable in that circumstance telling our client, "As long as it is your own stores and products, you can sell it as you see fit at whatever price you want to."

Then a year later Moozik begins to branch out. It has now established the product and gotten a lot more acceptance and it has started to sell through high-end retailers. But it is very careful in selecting the retailers through which it sells, and it has selected only those which have a history of selling at full retail prices. This is, selling through companies that have not been discounters in the past. There is a requirement imposed on each of these retailers that they build a dedicated Moozik section.

Again, it does not sound as if it is going to raise any Robinson-Patman issues since, as you see, we are selling through high-end retailers. Each of them has been required to build a separate section dedicated to the Moozik product and they have been carefully selected, again to move it along. Sounds here, again, there is no specific requirement imposed or stated that the retailers sell at the full price. Moozik is relying on the history and practice of these customers, and the requirement that they build a separate section for Moozik products does not appear to present any issues. Unless somebody sees a problem at this point, it doesn't seem to be a lot to talk about.

MR. FOX: I would just mention for counseling purposes, whenever there is an imposition on a dealer by a supplier, like building out space or a commitment of buying inventory well in excess of what would be needed for the initial sale, there is always a possibility that that relationship, which one would normally characterize as a buy/sell relationship, may indeed find itself as a franchise relationship governed by one of the state franchise statutes, and that additional activity a franchise fee. So I would just suggest that building out and those types of requirements may have implications, not necessarily the Robinson-Patman Act, but under state dealer/relations law franchise statutes.

MR. STEUER: I think the point is that this is still the surest way of ensuring a high-end aura for a product—by opening your own stores if you're the supplier, and putting obligations on independent dealers to spend money to promote the product. You don't need resale price maintenance or other kinds of restrictions if you have outright requirements that they need to build a particular facility or display and that, if they fail to meet those requirements, then action could be taken. This is very straightforward.

MR. KESSLER: I'd also note that, in this hypothetical, we have a ban on sales to Internet customers or to anyone but consumers. I think there's a widespread consensus that that's not going to be a problem in most cases. So that could also be put in as part of these restrictions.

MR. BRETT: So I think basically, to this point, everyone is going to be pretty comfortable with talking about *Colgate* and *Sylvania*, unilateral choices or vertical nonprice restraints requiring that they sell only to consumers, prohibiting sales to Internet and we are not likely to have any major issues.

MS. MARTUCCI: One thing I would say, from a practical standpoint, you need to think long and hard about putting in place a *Colgate*-type of program because it is difficult to sit there with the real salespeople and say to them, "Now, you're going to put these restrictions on your dealers and inevitably one of your dealers is going to violate them. You don't get to give them a second chance and you don't get to give them warnings. You're going to have to dump your best dealer." And regular people don't understand that. So you're going to have to really think, "Can my people execute this? Can they understand it? And can we abide by it?" And sometimes those nuances don't fit your sales team. So you really have to ask: Does this fit my structure?

MR. BRETT: I think an important point, to build on Paula's observation, what we are asking the salespeople to do in those circumstances is directly contrary to the instincts of a good salesperson who will go in and work with his customer, talk with them, tell them what the problem is and build a relationship. We are going to tell them, "You can't tell your customer you're terminating. You can't give them any warning. And you may have to cut them off without further discussion." It is absolutely significant and a great practical issue.

MS. MARTUCCI: That salesperson also, that's going to affect their commission and sales and that sort of thing. So they may not even bring it up to you for counseling.

MR. BRETT: Let's now move on. Here's where Moozik is now starting to get a little more aggressive. Moozik is expanding beyond its own stores and beyond the high-end retailers in whom it has confidence. It starts selling to chains where it can have less confidence that the chain will maintain resale prices as dictated by Moozik, and they are likely to discount. But Moozik adds to the program at this point a minimum advertised price restraint as part of a co-op advertising problem.

Here is where, I think, Paula in her dual capacity as a CEO and general counsel is going to have to be advising herself as to what the problems are, what to worry about and what the law is. I think there are some very real practical counseling issues that she will address with us.

MS. MARTUCCI: Well, in this situation, they want to have the minimum advertised price restriction on this electronics chain because, remember in the earlier scenario, we hand-selected high-end retailers that were going to invest money and build out a special display. They were going to dedicate sales associates who are going to be able to give great customer service.

So we've asked that group to put out an investment and now we are branching out to more of the Best Buy, Circuit City and electronic stores, and they are not going to be as apt to provide that high of an end service.

So we don't want to anger our high-end retailer, but we have got to expand our sales and distribution. So we need and want to be in this other group. We also know they have a history of discounting. So we want to put this minimum advertising price restriction on them and we also want to tie it to their co-op funds. I believe with the CD cases that came out, the FTC, when they looked at that, they felt it was too broad. So we are going to have to look at this. Do we try to tailor it to a specific product? Do we do it to everything we are selling to the electronics chain? Will it be sufficient? Because the way I have to tailor it is: I can only restrict my co-op money. So if they advertise with their own funds, I probably don't have a lot of say in it. So I need to look and see if this is going to be an effective tool, or if promotional analysis and different types of things might help me achieve that end.

I don't know if anyone wants to speak to the CD cases at all?

MR. STEUER: I think the main feature in the CD cases is where do you draw the line between what is advertising and what is the selling price? In most of these cases, there has been some effort to delay revelation of the actual selling price later and later. I think what really swung the FTC in those cases was the feeling that the actual selling price wasn't posted even in the store, and that consumers only found out what it was virtually when their credit card was being swiped. It wasn't quite that bad, but the idea is that there has to be a realistic line between what is an advertised price and what is a selling price. That's going to be the issue in all of those MAP cases.

MR. BRETT: I think it is important to note that all these issues that we're talking about in MAP are really RPM rather than Robinson-Patman cases in most respects. I also think it important to ask whether or not anyone is now counseling more aggressively in that area in anticipation of a change in the law based on what the Supreme Court is doing with *Leegin*. We have been making some wagers early on. Would they wager anything on the likely outcome of *Leegin* and would they do it in terms of a counseling issue today? Are you changing what you're telling your clients based on what's likely to happen?

MR. STEUER: Well, I'm not. I think we've only seen one side. The government has come down in favor of ending the per se rule on resale price maintenance. There have been some persuasive briefs, but if anyone wants to read a good explanation of the Free Rider Doctrine, Ping filed a very interesting brief, but we haven't seen the other side. There is going to be some powerful push back from consumer groups and others. I would not predict the outcome. What is really interesting is what if resale price maintenance becomes permitted? What does that do for the Robinson-Patman analyses that we have been talking about in terms of showing injury to competition where everybody has to charge the same price?

MR. KESSLER: I'm not, at the moment, prepared to wager and I would like to see the other side. What I would predict is that I think that the decision on this issue is going to be a lot closer than 7-2, and it would not surprise me at all to see a 5-4 decision in the case one way or the other. I'm not clear which way it will come out, but I think if you look back at where the Justices are and who is likely to come out different ways, it is very difficult to predict what the outcome of this case is going to be at this moment.

MR. STEUER: Even if the per se rule is abandoned, it's not likely that that's going to mean that the defendant always wins because even in the government's brief in support of Rule of Reason, they cited an article by Warren Grimes, saying, "Even the great critics of resale price maintenance have allowed that the Rule of Reason should apply."

Grimes sets forth a method of analysis to do a Rule of Reason analysis of resale price maintenance. So I think that even if the Court decides to abandon the per se rule, what we are likely to see in an opinion are instructions as to what the recipe is for conducting a Rule of Reason analysis.

MR. KESSLER: I actually think if the Court reverses and goes to Rule of Reason, what you will see is a re-explosion of resale price maintenance litigation, sort of comparable to what you had in the '70s. The reason is as follows: Right now, there are so few areas of clear antitrust counseling. So one of the things you can counsel is you can't specifically agree to fix resale prices. And, as a result of the difficulties that have arisen over 20 years of litigation in proving agreement, there really has been a dramatic reduction in terminated dealer cases over resale price claims under the *Monsanto* line. These cases have receded to a very significant extent. Now, if you now start with the Rule of Reason all over again, you're going to have counseling to companies that "now you can try resale price maintenance," and hundreds of companies will try it. The law will then be very uncertain as to what's a Rule of Reason violation in this situation. And, I predict, you will see cases all over the country brought by consumers. It will be very interesting in the vertical context as to who is being injured. You'll see all sorts of cases saying, "No, this isn't an unreasonable use of resale price maintenance." It will be good for the lawyers if it goes the other way.

MR. BRETT: Well, you certainly did not see that kind of litigation flow when the Supreme Court permitted maximum resale price maintenance after *Khan*, and one wonders whether the difficulties of proving a Rule of Reason case on either side will yield that kind of litigation.

MR. KESSLER: The only reason I think it is different is that it is very hard to figure out a maximum resale price case for anyone who is going to have the antitrust injury. Consumers, obviously, like maximum resale prices. Buyers like maximum resale prices. A competitor may not, but it is almost impossible to state an antitrust injury in that case. So that didn't surprise me. I think that if you allow minimum resale price agreements, you'll see a different result.

MR. BRETT: Maybe it will be interesting to hear Howard's discussion later on when he tells us how, as an economist, he would look to prove an anticompetitive effect on competition based on intrabrand restraints. I wonder if the same issue would not prevail if you tried to prove an effect on interbrand competition from an intrabrand restraint on minimum prices. But it will be interesting to see.

Just very, very quickly, in case anyone is not following and didn't hear the presentation earlier, *Leegin* is a case coming out of the Fifth Circuit where, for very curious reasons, the defendant tried to impose minimum resale prices and did not do it in a non-*Colgate*-permissible matter. They probably could have done everything they intended to do. The case came up through the circuit and the Supreme Court framed, because of the manner in which it had been done, as strictly an attack on Dr. Miles. The Supreme Court did something very unusual before it took the case: It stayed the mandate and the judgment in the lower court and then granted *cert.* I believe the only issue on *cert* is whether or not Dr. Miles should be reconsidered. I don't think there's anything else there. The Court can obviously do anything it wants to, but it is going to be difficult for them to duck that issue when it is finally addressed.

MR. FOX: Before we move off to *Leegin*, first of all, I think the reason you see so few of these is that the way it was implemented was so bad that you wound up with a plaintiff's verdict in this type of dealer termination case based on alleged resale price maintenance agreement. So it was a question of the evidence below that they really did have an agreement to enforce retail prices.

But one of the issues that the appellate court looked at was a distinction—and I think it is a distinction we are going to see of more and more importance—is the prima facie liability case and your proof required to meet your liability case as distinguished from what do you need to prove for antitrust injury and damages under *Clayton 4*? And once liability was established because there was an agreement, they argued below the now. The defendant said "Well, even if there is liability, there is no antitrust injury because there was no interbrand effect, and therefore, there was nothing flowing from what makes the law improper," which is an anticompetitive effect in an interbrand market.

The Fifth Circuit said no, all you had to show was he had lost profits and lost sales. That was enough. I think you may see the Supreme Court in *Leegin* talk about that distinction and say, "Even if you could establish liability, you need to then show, for damage purposes, an interbrand effect," which was insufficient in that case.

MR. BRETT: Let's go to our next slide which adds something very interesting. We have the same set of distribution issues, but what has now happened is that Moozik begins selling the product through its own Internet Web site and allows certain of its retailers to sell the players through their Web site, but only if they agree that the prices will not be shown to the consumers on the Web site until they put it into the shopping cart. That is, when the consumer decides whether or not to take the product on the Web site, there may be something on the screen saying something like "Price to be determined" or "At our aggressive price . . ." or whatever, but only after they add it to their cart and get to the checkout will they see the actual price.

This raises two areas of initial comment: Whether or not that kind of restraint on the ability of the selected dealers is appropriate. And two, whether or not there's a Robinson-Patman issue if certain of the dealers have the ability to sell on the Web site and some do not. You have some favorites and disfavorites. It is not a price discrimination. What are the problems this raises? Paula, how do you feel about it as a counselor in the first instance?

MS. MARTUCCI: Well, I would want to say that the Internet is another channel, and so I would try to distinguish that we had some good reasons for allowing certain people to be in that channel and perhaps others not. And that it wasn't a Robinson-Patman issue so much as our ability to select where we are going to sell things.

The problem is whether it comes under—when talking about Robinson-Patman, whether it comes under one of the technical requirements such as whether you allow them to sell in this channel is a form of discrimination or not on price. So that would be one of the issues that I would want to know more about.

MR. BRETT: Anybody have a problem with the imposition of the restriction against displaying the price prior to getting to the shopping cart? You're not controlling the price. It is not an RPM.

MR. STEUER: It is another example of trying to approximate in cyberspace what the rule previously was in bricks and mortar in things like the CD cases. Basically, by keeping the price—other than suggested prices—off the first screen, some suppliers try to prevent these crawlers from doing price comparisons, try to guard against free-riding, just as they would in the bricks-and-mortar world.

There is a tremendous tension that the Internet has created. On one level, if suppliers had their druthers, the Internet would be the only place to sell their products. Why do you need more than one Internet site? Everyone can Google the name of your product and find you. But the horse has left the barn on that in most areas. So the dealers in the bricks-and-mortar world have these Internet sites. So far, nobody has really pressed the issue whether allowing me as a retailer to have an Internet site is a service or facility, especially if there is some support from the supplier. But that's always been the lurking question: Is cyberspace a place or is it a method of selling?

MR. KESSLER: Yeah, I would say I don't think it is a Robinson-Patman Act issue, even under 2(d) or 2(e). I don't think it would fit into those characterizations. I think, if it is an issue, it is a Sherman Act issue. The issue is whether you're sufficiently interfering with price competition, but it is probably not per se. Looking at the Supreme Court case law in *Sharp*, where you have to have agreement on a specific price level at least to be per se illegal, there isn't a specific price level restriction here. So it would be a Rule of Reason claim and probably not a very strong one.

MR. FOX: We are coming back to the question of restricting what you can say on the Internet regarding pricing. Contrary to bricks-and-mortar situations where there is always a potential for a dialogue between the customer and the retailer about the ultimate selling price. Obviously, a supplier could recommend the suggested retail price but can't compel it other than with a *Colgate*-type doctrine. But when you're selling on the Internet, when would you preclude a retailer from displaying any price other than the actual selling price in the cart? Haven't you maybe gone the distance to preventing any price competition or negotiation between a retailer and the customer, such that the supplier now has essentially determined the resale price of its goods?

MS. MARTUCCI: But what if you had something like a pop-up that said, "Special discounts apply when it goes into your shopping cart," and you have that frequently enough that everybody knows, "Hey, I've got to at least get it into the shopping cart to see the best prices."

MR. FOX: Where is that line? Can you make reference to "Special price available. Call this number." I've been involved in situations where they actually have an 800 number or they can push a button and actually get an e-mail of what the sale price is. There are different ways. But can you go the distance and say—the only thing is, they could see what the real price is, and nothing before it could indicate that the price that they are seeing on the screen, which is the MSRP price, isn't the final price until they get to the shopping cart and find out, in fact, that there are alternates to the shopping cart.

I'll ask the other question that nobody has really raised yet: What do you think about the question of Moozik imposing these but also being a competitor as to whether these are vertical or horizontal restraints? Are they potentially raising a question of basically horizontal price fixing between themselves and their retail competitors because they have retail stores? And when do you cross the line as a supplier to distribution from a vertical to a potential horizontal restraint? How do you deal with those?

MS. MARTUCCI: Well, for the most part, the dual distribution issues, as I've been researching, says it is not a huge issue but the Internet does add another layer to that because, a lot of times, you may have geographic locations where you have your stores and they have their stores. So you know where those lines are. To me, the Internet is not always considered competing with the stores; it really takes away all the geographic boundaries. I think it would potentially raise horizontal problems depending on what kind of restraints you put on them. Then if you ended up having to get into a price war with them, if you had a policy that you'd always meet competitors' prices and they start lowering their price, and then you have to terminate them. It depends on what kind of

restrictions you put on them and how you're influencing that and whether you're going to punish them for doing it, or whether you're just suggesting they do it.

MR. BRETT: Let's move on to what's going to happen next year. Moozik has had some success. A lot more of the retail chains want to get into the product, including the big buyers, such as the club stores and the big-box sellers.

So a year later Moozik comes and starts taking on this additional volume. They begin selling their product to club stores and mass merchandisers. But as we all know, many of them will demand lower prices than their competitors among the high-end retailers. And to respond to that, Moozik doesn't give them better discounts. What they do is create some new models with lower capacity, different outer designs, and they offer these at lower prices. In addition to that, some of the club stores, who want to protect themselves against taking on inventory, negotiate to take title to the product only at the moment that it is sold to a consumer so that Moozik is shouldering the cost of carrying the inventory at the stores.

We have added a whole bunch of issues there: The requirement of the statute that the goods be of like-grade and quality in order for there to be a discrimination; and certainly there is always going to be a threshold question as to whether or not the changes made are sufficient to take them out of the requirements of like-grade and quality, particularly on commodity-like products. How different do the products have to be?

And a separate question, I think, as part of that on Robinson-Patman issue is whether or not one must make all of those models available or any requirement to make the lower-priced models available to your high-end retailers and maybe even the flip side of that: Can the mass merchandisers demand that they also get access to the higher-end product which they might very well be using as loss leaders or selling very aggressively but not taking on major inventory, but having great impact on your ability to sell to the customer? So you get some of the real day-to-day Robinson-Patman issues.

MS. MARTUCCI: I don't think that the cosmetic changes alone will get you a difference in like-grade and quality. So that one, by itself, wouldn't. The lower capacity, I think, will get you to a difference in like-grade and quality—especially if it's a music box—or if it is a DVD/VCR and one has a recorder and the other doesn't have a recorder. Those are clearly different items. Those kind of distinctions can get you there, but not cosmetic alone.

The other thing was about whether you can restrict. I think you can have either exclusive deals where you're going to sell certain models to certain of the outlets. You can do that. You would be more apt to want to make sure you had more things available to the high-end people that you started with.

Not just for the law, but one of the issues you have, you have those high-end people that invested a lot of money in this program, and they built out the stuff and hired and trained their associates to be able to sell your things. So you don't want to alienate them.

But at this point in our business model, now we have to get a lot of those Moozik players out there in the market. Eventually our technology is going to keep putting things into this pipeline and we're also going to be making more money on maintenance and add-ons. So we want to keep going back through this structure and we don't want to alienate the high-end people by the time we get down to the mass merchants.

I think you're going to want to keep these in separate channels and you're going to want different products. You may want to offer it to people upstream, but you're probably not going to want to offer it to people downstream unless they don't want to sell your product otherwise.

But you have to keep replicating your model and not alienate the people at the different stages. You want to expand your model and you need them for different types of things.

MR. BRETT: Anybody envision any kind of objective criteria that one could apply in trying to determine whether or not variations are sufficient to change a product of like-grade and quality?

MR. KESSLER: I don't think there are objective criteria. I think, as a general test, Paula is right: It has to be something which will affect consumer use and preference. That's as much guidance as you can have. Clearly, capacity, in this hypothetical, for a Moozik player, I think, would be something that would affect consumer use and preference.

The interesting thing is, though, is it can be counter-intuitive. You could increase capacity and create a different like-product and sell it at a lower price, and you would get out of the Robinson-Patman Act. So there doesn't have to be any logical connection between the change in the product and which way the price goes, which is interesting.

One point I do want to mention is the reference to passing title. This is a tricky area. Some companies have tried to form a structure in which they claim that title doesn't pass until a later point in the distribution chain, and therefore, argue that there are two purchasers at the next level because, I guess, the product just rides through to the ultimate purchaser.

I don't think that title is going to control that issue. It did come up in the *Feesers* case and it was rejected that title was the relevant test by the lower court. That issue was not raised on the appeal. But the issue, I think, has to be looked at: Who is negotiating the purchase price? And who is determining the sales quantity? And so, in an economic sense, who is the real purchaser? But just writing on a piece of paper that title is going to pass at some later time, I think can be viewed as form over substance. I think the courts will look at it economically: Where is the purchase taking place? Who bears the risk of loss? In our hypothetical, it says that the company will bear the risk of loss. I'm not sure what that means. If the products go down in a fire, who is going to pay for those products?

MS. MARTUCCI: In real life, you have a supplier who has trading cards or bread or something like that, and they are directly delivering to your store, and you sign up for the consignment agreement, and you negotiate who is going to bear that risk of loss. Something like baseball cards have a very high shrinkage. They are shoplifted all the time. If you're going to make them bear the risk of that but they also don't have control, you're giving up control and protecting your product and maintaining that risk. But if you negotiate it in such a way that you don't have a risk, I don't think you have true consignment.

MR. FOX: Right. I think there's another point that raises within the context of the Robinson-Patman Act. These are known as situations where the retailer is going to pay on scan. Essentially, they may have it in inventory but the title doesn't shift until they actually wand it at the cash register. And then it becomes a sale. The Robinson-Patman issue also involved is: If, in fact, a supplier is maintaining the cost of inventory so that the inventory cost of maintaining this is not going to be borne by the dealer, have you provided a benefit to the dealer in such a fashion to lower its purchase price so that it is cognizable either under 2(a) or potentially 2(d)? It usually comes up in 2(a). If the supplier assumes a cost for certain retailers that it doesn't assume for others, does that affect net price? And some of the recent cases say no, it's what the retailer pays the supplier. What's the net price paid? And if a supplier absorbs a cost for some and not for others, it will not be viewed within that.

MR. BRETT: How do you deal with that in light of the older cases which indicated that a difference in credit terms was clearly a difference in price for purposes of 2(a)? Isn't having to bear a cost of inventory pretty similar to that?

MR. STEUER: I think you hit exactly on the issue. I don't think it is a 2(d) or 2(e) issue because it is not in connection with resale. So it falls within the interstices of Robinson-Patman that way. But if credit differences are differences in price, then what about the time value of money? If somebody has to pay when it hits the loading dock and somebody else only pays when it hits the checkout aisle, is that a different price?

MR. BRETT: How do we advise the clients when these mass merchandisers now demand slotting allowances in exchange for shelf space? There's been a lot of discussion and FTC hearings about shelf space and whether it's more valuable and important to get the product at eye level or lower level and category captains and things that may have great value to the retailer from the point of view of the seller, but they want to get paid for doing it. Are these now going to be viewed and continue to be viewed as 2(a), 2(d) and 2(e) problems?

MR. FOX: Well, I think there's a distinction between pay-to-play and pay-to-stay. Pay to get in, often in the hearings at the FTC, what you're really paying for is the retailer's willingness to accept a new product, to assume some of the risk and costs associated with that new product. So you're not really paying for a reduced price on a per-unit basis. But it could be a 2(a) and it could be characterized as a 2(d) in the context of providing the slotting allowances on an ongoing basis that it ultimately benefits them in connection with the resale of the product. So it implicates both 2(a) and 2(d) and also arises in two contexts: One getting in and one staying.

MR. KESSLER: I think the reason that you don't see a lot of Robinson-Patman Act cases on slotting allowances is because it is very hard to translate those slotting allowances into a Section 4 injury to a competitor. Remember, most Robinson-Patman Act cases are brought by disfavored competitors. When there's an actual price reduction, you can more easily draw the injury connection than with a slotting allowance, which tends to be a lump-sum payment. And, it could be allocated over a whole multitude of products. So it might not be clear what specific product the allowance should be applied to and how it is affecting the sale. So you haven't seen a lot of RP litigation over slotting allocations.

MR. FOX: I think there are two cases in the Second Circuit, the *Tropicana* and the *High Grade* cases. One denied summary judgment and one denied a motion to dismiss relating to slotting allowances. And there was a First Circuit case about two years ago, *Hudson News Company*.

MR. STEUER: I think the FTC wrestled slotting allowances to the ground in extensive hearings in which it was really unable to come up with much of a theory for going after them on a broad basis. One stumbling block is that it's very common that there is a meeting competition defense because you have multiple suppliers bidding for the stakes.

MR. BRETT: There are some very interesting, to some of us, hearings and reports and analysis on slotting allowances that have to deal with the FTC proceedings on the issue.

MR. FOX: It was a very important portion of FTC's only Robinson-Patman case in the last couple of years, the *McCormick* case in 2000. The FTC went after McCormick for providing slotting allowances and, adding they had 95 percent market share, arguably was a primary line case, but it had a secondary line impact. But slotting allowances played an important part in that case.

MR. BRETT: Let's put up our last slide, which deals with an issue that the products have become very, very popular to the point where cruise lines, other customers want to make large purchases of these products in order to give them away as promotional items and giveaways and for other purposes. The mass merchandisers and the chains are very interested in bidding for this business, but the chains complain that they can't compete against the mass merchandisers, and they are asking for better prices. They threaten to sue unless they get the appropriate price discounts on the products. And in large measure in this circumstance, the higher-end and lower-end product with the higher capacity and lower price may be fungible from the point of view of the cruise line. They want to give away the Moozik product. They are not going to start describing all of the features.

How does Moozik, which may also want to bid for this business, try to get it directly, how does it deal with these issues now where they are competing? And, ultimately, will it matter if the sale is going to be made on products from inventory as opposed to custom-made with special indications that it's made for the particular buyers?

I think that's really going to be an issue as to how far we can take *Volvo*. Is *Volvo* going to help us in those areas?

MR. KESSLER: Well, I daresay, as a counseling matter, what I would do is say that if mass merchants and the chains are bidding for that specific cruise line, then all of them should be given the same price. But you certainly can, I think, after *Volvo*, take the position that the customers have to come to you and say yes, I'm bidding for this account and you then respond by saying here's the price you will get if you're bidding for that cruise line.

I think it would be very risky to, in effect, create the missing facts that weren't in the *Volvo* case by discriminating and relying upon Section 4 of the opinion and saying: "But okay, there is no effect on interbrand competition." I wouldn't counsel that way. I think what you have to do is take the decision where it is. You don't have to give the same prices if they are not bidding. But if they are bidding, you offer the same prices. That becomes your policy, which was the policy that Volvo had, which the Court held was lawful.

MR. BRETT: What if they are bidding from inventory and come in and say, "I don't want a special price for this customer but it is a competitor, I think I want to bid for the account against so-and-so."

MR. KESSLER: I think you have to let your customers know that, as a matter of policy, that special pricing might be available but they have to come and ask for that. You're in a functional availability defense of the RP Act, which is that if the chains didn't know that you were giving it to the mass merchandisers, it is not functionally available to them.

MS. MARTUCCI: Well, I think you have a couple of issues. One, because it is in inventory then, it is a purchase that already took place. So you may not have a contemporaneous sale. It can be it is last year's color or some other model. So if the electronic chain now is coming in and saying, "I want to bid on these also but I don't have it in inventory," as the supplier, I want to know, "Do I have it in inventory or can I manufacture it and give them that same price? Or what's the best I could do?" But they are not contemporaneous sales even though they are trying to compete for the same customer. So you want to be very fact-specific and treat them as fairly as you can. But it is not the exact same transaction.

MR. STEUER: There is also a nice issue if the customer specifically wants one model and not the other, whether you have to make that model available to everybody who wants to bid. Certainly, if GM sells Chevrolets to a lot of dealers, some of whom also carry Cadillac, it is pretty clear those are different lines and you don't have to make Cadillacs available to everybody who carries Chevys. But within lines, if it is a matter of a little more capacity or less or a different size, is that a service or facility where, if somebody has the line, you've got to give them all of the models? That's a very fuzzy area.

MR. BRETT: Can we refuse to give one customer an opportunity to bid or opportunity to get access to special pricing for it?

MR. STEUER: And obviously as a business matter, it is a horrible choice to discriminate among customers that you expect to be out there bidding your products. On the other hand, that was the whole premise of *Volvo*: They hated the plaintiff.

MR. BRETT: Do we solve the problem or can we solve the problem for Moozik if you make all of the special orders customer-specific and you agree, probably at very little incremental cost, to put the ultimate customer name on it, the cruise line or otherwise, so that it is a distinct product and it's not saleable in the stores? Would that do it?

MR. STEUER: Now you have a custom-made good, so you're back to the issue that *Volvo* ducks: How many purchasers are you going to have when only one of them actually purchases this custom-made model that's going to go to the cruise line?

MR. FOX: I would like to hear Howard tell me how you're going to make a judgment as to whether or not any of these bidders have sufficient power to be viewed as a power buyer in the context of *Volvo*? How do you measure and evaluate power?

MR. KITT: I'm glad you asked me that question. Finally. I now know what it is like to be an Affirmative Action member of a panel.

The problem, and I promise I will get to your question, the basic problem with an economist looking at the Robinson-Patman Act, and we can put aside all the ideology, it begins with the fact that, at least as far as I am concerned, the Act was, in effect, a regulatory statute being shoehorned into antitrust policy. As Jeff said, the purpose was to protect small business and that was always its purpose. And that's okay. We can do the cost/benefit analysis and decide whether or not small business is worth protecting, whether there are externalities, all the things that economists and policymakers can do. But when we try to put this into a competitive context, we end up with a series of disconnects. Let me talk about them, in effect, one by one. It really has to do with basic definitions of terms.

First of all, to an economist, price discrimination only occurs when prices don't reflect costs. Or in other words, when a seller is earning a different margin on sales to otherwise similarly situated customers. It is not a difference in price. And a difference in price is neither necessary nor sufficient because if you're charging the same price to people, two of whom have different costs of service, it is just as much a discrimination. The whole question of like-grade and quality, functional interchangeability or as Jeff said—I'm sorry I forgot the phrase that you used about consumer preference?

MR. KESSLER: I don't remember it.

MR. KITT: But it was brilliant. It has to do with demand and elasticities. It has to do with the ability of the customer to turn to other sources of supply.

What about competition? What does competition mean? Well, there's a noun form and there's a verb form. The noun form is what economists generally describe as a situation where prices are equal to marginal costs, all sellers are price-takers, are infinitely elastic, people can sell all they want at a given price. They are pure price-takers.

Now, in a verb sense, that's in many ways where competition has ceased because there isn't the striving that you would expect to see if you looked at "competition" as a verb.

Essentially, the way in which competition takes place, more often than not, has to do with the creation and destruction of discriminations. Whether the discriminations have to do with price, whether they have to do with terms and conditions. How do you, as a competitor, make an inroad into a store which has not carried your brand? Either you have to provide them a superior product, or a better price, or better terms and conditions.

What is so sacrosanct about price to warrant a specific statute talking about price discrimination? Yes, there are those sections that talk about credit terms, and as Richard pointed out, the time value of money. All of those things reflect costs to the purchaser.

The Supreme Court long ago, even though it didn't overrule it, said there really isn't any distinction between price and nonprice restraints. They all affect, in effect, price. They all change the costs of doing business. So whether it is—I mean, free riding, I think, is a perfect example of that. When you prevent, via customer restrictions or territorial restriction, when you prevent someone from cream-skimming another person's service, you have increased the former's cost of doing business because now the former has to go out and spend more money than before when free-riding was still a possibility.

So whether you raise the price or you force additional costs on the purchaser, you end up in the same place.

So what do we mean, then, when we talk about anticompetitive effects or competitive effects generally? Well, to the economist, it can be summarized very succinctly as: A situation where the demand curve facing the supplier has become less elastic at the given price, which is a high-falutin' way of saying: The beneficiary, after everything has worked itself through, faces a less elastic demand curve. As a result, he will raise price, reduce output, a reduction in consumer welfare.

That's, in a nutshell, what an anticompetitive effect is. So the question to be asked, coming now to Larry's point, how do we determine whether or not there are anticompetitive effects on the assumption that that's what we are being asked to do? I really don't have the competence to decide whether Richard or Jeff is right on the decision—although I do know why I was seated between them.

But a very shorthand way of doing it, and I don't have all that much time, the way in which analysis takes place under the Merger Guidelines is really good enough. What are the questions that the Merger Guidelines ask? They ask in the first place: Will there be the possibility of a unilateral exercise of market power after the merger? A merger takes a competitor out of play. An acquisition takes a competitor out of play. Price discrimination arguably puts someone at a competitive disadvantage.

The second question that the guidelines asks is whether it will facilitate coordinated effects. Is this price discrimination, in other words, in aid of either establishing or maintaining a conspiracy, which will have the effect of changing the elasticity of demand facing the partners to the conspiracy?

What does that mean from the point of view of price discrimination? Well, we are talking about interbrand competition. How do we determine interbrand competition? How do we do it in a merger matter? We need to do it by defining relevant markets in order, at the very beginning, to calculate HHIs and see whether there is an unacceptable increase or, at least, a presumptively unacceptable increase in concentration following the merger.

And all of the elasticity tests, all of the econometric analysis that is used to determine which products compete with which products are germane here. Has the requirement for competition versus competitor been written out of antitrust price discrimination? No, I don't think so. I mentioned conspiracy as one.

Let's talk about inner interbrand competition for just a second. Few markets are homogeneous. That has been recognized in the Guidelines through the analysis of close substitutes. If a merger, even though there is in some broad sense interbrand competition, if the merger takes out of play one who is a very close substitute to the acquirer, the elasticity of demand facing the acquirer can change and the acquirer will acquire some power over price.

Why are they close substitutes and why aren't others? They may be particularly advantageously located. Their brands may be viewed as interchangeable. There are a whole bunch of things that everybody does in context of a Hard-Scott-Rodino filing that can be done here. It's not, in effect, an Economists' and Lawyers' Relief Act.

There are benchmarks and there are tests that can be applied. But the basic problem for the economist is that—heretofore at least—let's assume with Jeff that the world really hasn't changed all that much, there isn't a whole hell of a lot for an economist to do. We can get involved, I suppose, in arcane questions of whether or not—we can do cost justification, but in that area, the problem with it as it is now defined is that you have to justify all of the costs, and you have to do it precisely. That's very rare in the real world. It's not the way business people make judgments. What happens if you've justified 90 percent of the price differential and you're only left with 10 percent that's unjustified? Is that the portion you should be looking at for purposes of determining anticompetitive effect? Or is it all or nothing? I don't know the answer to that.

But we can do the cost justification. We can look at that and decide whether certain costs should be taken into account. We can measure damages—if damages are defined as the lost business, the business lost or the profits lost by the disfavored purchaser in secondary line cases. We can do that. And attorneys can counsel people in that respect.

As for meeting competition, let me, in fact, end on this note. So far as I am concerned as an economist, absent conspiracy, every punitively discriminatory price is generated by a competitive circumstance. What was the issue in A&P, going back to that case? A&P could take it in-house. A&P said, "I'll buy it from you or simply produce more private label products," among other things. Why would a rational profit-maximizing supplier lower price if that supplier didn't have to? It's always to meet competition of some sort. It's always to meet diversion of some sort. So higher or lower prices, in some sense, to an economist, always reflect some competitive response. Except as I mentioned for conspiracy.

So where are we? If the law hasn't changed, then we're in a hothouse world. We are in a world in which the traditional laws and principles of economic analysis really don't apply because it is very difficult for an economist to talk about competition the way competition has been defined in previous Robinson-Patman cases. If it has changed, it hasn't repealed the Robinson-Patman Act, but it does require an empirical analysis of competitive effects.

MR. BRETT: Howard, let me comment on something. Dick pointed out the significance of the absence of market power on the injury-of-competition issue. Is there any prospect, from the point of view as an economist in determining whether or not there's an injury to competition? Also, Richard, from a legal point of view, can you take a quick look and say there is no market power, it is an atomistic market here. So there is virtually no prospect of market power, there's no prospect of injury to competition based on those facts alone, and therefore, whether it is a Section 1 or Robinson-Patman context, there's not likely to be the requisite injury to competition?

MR. KITT: I think the answer was two-fold from the economist's standpoint.

One, technically, every firm that does not face a horizontal demand curve has market power if you define market power as having some influence over price and quantity. The question is: How much? And that, I think, can be addressed in the same way that it's addressed in merger analysis. I mean, will there be—merger analyses talks about small but significant nontransitory changes in price. One can ask the question here: Will this practice result in, after everything has worked through, some change in the pre-existing price level that will work to the detriment of consumers? And if the answer is no, it seems to me you're home free.

MR. FOX: Are there any questions that any of you would like to pass up or just ask from the floor?

AUDIENCE MEMBER: What would happen if Moozik decided to adopt a software digital rights management strategy to differentiate the products? So they'd be giving out the same player, same capacity everywhere but they had installed software keys so some could only play country and western music. Others could play music that was released more than six months ago. Some would be able to play music released within the last three months. To make it more interesting, they pre-install certain artists recordings on those devices and other artists would be told, "You don't have a large enough audience, but if you want to pay us, we can install your music on some," and come up with a custom view.

MR. FOX: My view is that is a substantial difference that would affect consumer demand, and that would differentiate the product. To me, the issue is: Are there different demands? If one is just rock and one is country, and those are two consumer groups, and you can't alter the configurations so the actual mechanics, although they are the same, the product is, to my mind, a differentiated product.

MR. BRETT: One more question.

AUDIENCE MEMBER: Howard, do you have a view as to how the Rule of Reason issue should be structured in the event the Supreme Court decides in *Leegin* that a requirement that an agreement to maintain pricing above a certain level is no longer per se?

MR. KITT: Yes, and I think it really has to begin with a Merger Guidelines–type market analysis. The question is: What alternatives are there, not just to consumers by the way, but to purchasers as well? Because arguably—I mean, think of a dealer termination case where someone is terminated for carrying the same brand as someone else and picks up a different brand. Arguably, interbrand competition has been aided by that. So unless you define the market, you define the competitive space, and once you do that, it seems to me that you very easily apply the standard sorts of competitive analyses that are used.

MR. FOX: Thank you to the panelists.

(Applause.)

Section Business Meeting, Election of Officers and Members of the Executive Committee

MR. MORGENSTERN: Thank you all for that. That was really an excellent panel.

If you could sit tight for a few minutes, I'm going to bring Ilene Gotts up, and she will preside over our Annual Section Meeting, which has a little bit of business and a little bit of information.

MS. GOTTS: Meg, I would ask that Meg give the Nominations Committee report.

MS. GIFFORD: Good morning, everyone. I would ask all of the people present who are members of the Section to give me your attention for a minute or two. And by the way, I hope you are actually all members of the Section. And if you're not, we can sign you up immediately.

This is the "Annual Report" of the Nominating Committee. As usual, there is a long list of names of individuals who are currently serving on the Executive Committee of the Section who are being renominated for another two-year term. With the agreement of our outgoing and incoming chairs, if I can dispense with the reading of all of those names, that will make all of us happier. And I will identify the names of individuals whom the committee is nominating for election to a two-year term to the Executive Committee for the first time. They are not current members:

Brendan Dowd of O'Melveny and Myers; Marjorie Han of Henry Schein, Inc.; Jonathan Jacobson of Wilson Sonsini Goodrich and Rosati; Elai Katz of Cahill Gordon and Reindel, although he has been a diligent attendee of the Executive Committee meetings for some time now; Michael Naughton of Simpson Thatcher and Bartlett; Wesley Powell of Hunton and Williams; Patrick Rao of Carrier Corporation; Harry Robins of Morgan Lewis and Bockius; Eileen Simon of MasterCard Worldwide; and Robert Trenchard of WilmerHale.

If I may have a motion from a member of the Section to elect them?

AUDIENCE MEMBER: So moved.

MS. GOTTS: And a second?

AUDIENCE MEMBER: Second.

MS. GIFFORD: All in favor?

AUDIENCE: Aye.

MS. GIFFORD: Our last piece of business, the Committee nominates the following members of the Executive Committee for election to one-year terms in the offices that I will identify: Saul Morgenstern as Chair; Stacey Mahoney as Vice-Chair; and Paul Braunsdorf as Secretary. If I could have a motion and a second?

AUDIENCE MEMBER: Aye.

MALE SPEAKER: So moved.

MALE SPEAKER: Second.

MS. GIFFORD: All in favor?

AUDIENCE MEMBER: Thank you very much.

(Adjourned for lunch.)

Joint Venture Litigation and Counseling After *Dagher* and *Polygram*: New Joint Venture Jurisprudence?

MR. MORGENSTERN: Our next program today is on joint venture litigation and counseling after *Dagher* and *Polygram*, two more significant cases in this area in the last couple of years.

Joint ventures and other collaborations among competitors raise a number of issues that require careful thought. Both inside corporate counsel and outside antitrust counsel should be aware of the important counseling litigation issues raised by the Supreme Court decision in *Dagher* and the earlier court of appeals decision, *Polygram Holding against FTC*, which we like to call the *Three Tenors* case, just because it sounds better.

Our second act for today brings together a distinguished panel of practitioners, a government enforcer and an economist to explore these issues in the context of another hypothetical that they have constructed to facilitate a real-world—okay, a simulated-real-world, to be more precise—understanding of these issues. They will explore the practical legal considerations presented by the *Dagher* and *Three Tenors* decisions with respect to the formulation and implementation of their hypothetical joint venture.

If you've been wondering whether the *Dagher* Court's analysis differs significantly from the D.C.'s circuit in the *Three Tenors* and what the significance is inside or outside the joint venture, what are the defenses and justifications for restraints in the context of a joint venture, and what economic issues concerning partial integration and market power of joint ventures, this is the place to find out.

Our panel Co-chair and Moderator is Eamon O'Kelly of Dewey Ballantine here in New York City, where he specializes in antitrust and general commercial litigation. He represents clients in investigations by the FTC and DOJ, by the state attorneys general. Eamon came to the law after a career in banking, where he learned many valuable lessons about how businesses really operate, and he's used that since becoming a lawyer. I know because we have often worked together. He is uniquely capable of guiding today's discussion on the practical effects of these interesting legal developments.

Our panel Co-chair James Yoon, who has opted not to sit up here, deserves to be mentioned for all the work he has put into helping get this going. He is an assistant Attorney General in the State of New York Attorney General's Office. He investigates and prosecutors a wide variety of antitrust matters, including state review of mergers and acquisitions.

Lauren Albert, sitting in the middle, is a partner at Axinn, Veltrop and Harkrider here in New York, and she regularly represents clients in mergers, assisting them in analyzing the antitrust issues implicated by their business plans and obtaining government consent to execute them where necessary. She most recently represented GHI, defeating the City of New York's attempt to enjoin its merger with HIP, and also represents clients in antitrust litigation as well as intellectual property and commercial litigation.

Dr. Vandy Howell is a Vice President at Cornerstone Research, where she provides consulting and testifying expert services in antitrust, intellectual property and breach of contract cases as well as in labor markets. Her expertise extends to class certification issues. She has conducted economic and policy analyses for the Federal Reserve Board and at the Department of Labor. She also has taught industrial organization at the University of California at Berkeley.

Finally, certainly not least, we have Tara Koslov here from the Federal Trade Commission, where she is the Attorney Advisor to Pamela Jones Harbour, specializing in antitrust and policy competition matters. Ms. Koslov previously served for several years as Attorney Adviser to Commissioner Sheila Anthony. She began her FTC career 10 years ago as a staff attorney in the Bureau of Competition in Mergers II, where she focused on cases in high technology markets. Before that, she was in private practice in the D.C. office of Vinson and Elkins.

Please welcome this illustrious panel.

(Applause.)

MR. O'KELLY: Good afternoon, everybody.

As Saul mentioned, the template through which we are going to be looking at the state of antitrust law as it relates to joint ventures will be two recent significant decisions: The *Three Tenors* case, which was decided in 2005 by the District of Columbia Court of Appeals, and the more recent *Texaco v. Dagher* decision as handed down by the Supreme Court in February of 2006.

I think it's fair to say, based upon the amount of commentary that has followed both of these two decisions, the *Three Tenors* case is certainly the more controversial. It has generated an enormous amount of writing both in favor of and against the reasoning of the D.C. Court of Appeals and ultimately of the Federal Trade Commission. And the *Dagher* case, in many regards, has been less controversial, but I think it is very important in counseling clients going forward that we look at both of these cases because they both deal with many of the same issues, but

come out in different places because of nuanced differences between the justices, and the way justices saw those issues.

Both of them purported to deal with so-called ancillary restraints in the operation of a joint venture. As you'll see, both courts ultimately saw the application of that doctrine quite differently in the circumstances of those cases.

Let me tell you at the outset how we intend to use our panel this afternoon and we'll get on with the program. First of all, we'll discuss those two cases in some detail. We will start with the *Three Tenors* case. I will give a very brief synopsis of the facts and the holdings of the case and then the members of the panel will weigh in. Then we'll proceed onto *Dagher*, and then we'll discuss what Saul characterized as a simulated-real-world hypothetical where we'll try and bring elements that were involved in both of those cases together. And the panelists will tease out how those elements might play out in litigation or investigation. And then finally at the end, I would like to leave some time for questions from members of the audience.

It's our goal today to keep this interactive and pretty informal so we can have as animated a discussion as possible. If any of you have questions that you absolutely feel cannot wait until the end and you have to interject, feel free. But we would prefer if we could keep the questions until the end.

So first of all, let me talk very briefly about the *Three Tenors* case, given its proper caption, *Polygram Holding, Inc. against Federal Trade Commission*, 416 F.3d 29, decided by the D.C. Circuit in 2005.

The basic facts of the case were that the Three Tenors, Pavarotti, Carreras and Placido Domingo, put on spectacular concerts around the soccer World Cup finals of 1990, 1994, 1998.

Polygram released a recording of the 1990 concert and it became one of the biggest, if not the biggest or best-selling, classical concert recordings of all time. The concert in 1994 was equally successful, and the recording of the concert was almost as successful as the 1990 recording. The Three Tenors switched labels between 1990 and 1994, and the 1994 album was distributed by Warner.

In 1997 with the Three Tenors proposing to do a third concert—in soccer parlance, I guess they were going for a hat trick—Polygram and Warner came together and agreed to a joint venture for distributing the recording of the 1998 concert.

The basic terms of the deal were that while Warner had the overall rights, it licensed the non-U.S. rights to Polygram. So therefore Warner would distribute the recording in the United States, and Polygram would distribute it elsewhere in the world.

In 1998, several months before the concert took place, Warner and Polygram got back together and agreed ultimately to a side agreement whereby there would be a 10-week moratorium around the time of the release of the new recording, a 10-week moratorium on distribution and promotion of the 1990 and 1994 CDs. The rights to those two CDs continued to be held by Polygram and Warner and respectively for the 1994 concert.

The FTC heard about this agreement and issued a complaint and eventually the matter was tried before an FTC administrative law judge. The ALJ found that the agreement to have the moratorium on promotion and distribution of 1994 and 1990 CDs was unlawful. The full Commission affirmed the order of the ALJ, and the defendants, in turn, appealed to the District of Columbia Court of Appeals, which upheld the Federal Trade Commission.

On appeal, the defendants raised four objections and only two of them were germane to what we are looking at today. First, they pointed out that they had presented an argument that the moratorium agreement on discounting was an ancillary restraint to the joint venture, which the FTC had not challenged, and that the purpose of the ancillary restraint was to preclude free-riding by either one of the two joint venturers on the promotion efforts surrounding the 1998 recording.

The defendants argued that the Commission should not have summarily rejected this argument as they did.

Second, the defendants argued that the FTC was required to prove that the restraint actually harmed competition before the Commission could have required the defendants to offer a pro-competitive justification in the first place.

And as I mentioned there were two other arguments. One was that there was insufficient evidence to support the Commission's conclusion and one attacked the structure of the remedy.

The D.C. Circuit devoted most of its analysis of the case to the question of whether the Federal Trade Commission had employed the correct mode of analysis. The court noted that in cases such as *NCAA v. Board of Regents* the Supreme Court had indicated that it was moving away from the old rigid dichotomy between per se legal rule and the Rule of Reason.

And in the view of the D.C. Circuit, the way that Section 1 conduct should now be evaluated by the court was along a continuum. The closer you got to the type of conduct that was heretofore condemned as per se unlawful, the more quick-look analysis that you can apply, the further away you got from that, the more closer you got to the old Rule of Reason–type situation, then you needed to do a more detailed analysis.

So the court concluded in this part of its analysis that, rather than focusing on whether to apply the old per se

rule or the old Rule of Reason, courts should make an inquiry, meet for the case, looking to the circumstances, details and scope of the restraint in order to answer what the court says is the ultimate question in any Section 1 case, whether the challenge restraint enhances competition.

Having set that template, the court quickly concluded that the Federal Trade Commission had indeed created an inquiry that was meet for the case, looking to the circumstances and so forth of the case. The analysis the Commission had used was to ask first whether the restraint was inherently suspect. And if it found that it was, without having to prove the harm to competition, the FTC then required the defendants to justify the restraint.

The court said that it had no difficulty in concluding that the type of arrangement was indeed inherently suspect. It was an agreement between two competitors, not to give discounts on two products that, in the court's view, competed most directly with the product sold by those same two entities through a joint venture. Therefore it was only a hair's breadth removed from price fixing.

Having concluded that the restraint was inherently suspect, then the court found that the justification proffered by Warner and Polygram, the elimination of free-riding, was really pretextual and that the so-called free-riding that was to be eliminated was nothing more than actual competition.

Having then decided that the mode of analysis and application of the analysis by the Commission was appropriate, the court upheld the Commission's decision.

That's the infamous *Three Tenors* case. And now I'll turn to the panel.

Lauren, if you don't mind, I'll start with you. Did you find the D.C. Circuit's analysis persuasive?

MS. ALBERT: No, I was quite troubled by it. It's troubling both as an antitrust practitioner in advising your clients; we have this long body of law, *Brooke Group*, *NCAA* and *Addyson Pipe* going back to 1898 telling us how to do things and then we have this D.C. Circuit telling us very differently. So what are we supposed to advise our clients? Ever since *Addyson Pipe*, going back to 1899 and more recent cases, they have upheld that any restraint ancillary to achieving the legitimate efficiencies of joint venture should be analyzed under the Rule of Reason.

In the *Three Tenors* case, however, the court found a restraint which traditionally has been considered ancillary, one that is related to achieving legitimate efficiencies to be a negative restraint and, as such, per se unlawful. The problem is they skipped the Rule of Reason analysis. If you skip the Rule of Reason analysis, you can't decide whether the restraint is anticompetitive, whether it actually causes consumer harm. You're not testing whether the anticompetitive effects of the restraint outweigh any alleged procompetitive justifications.

So even if, as the court found in *Three Tenors*, justification is purely pretextual, it still may not harm competition. If it doesn't, why should it be condemned under the antitrust laws? Let me explain the analysis in a little more detail.

First, the court said the restraint on products outside the joint venture—that is, the parties agree to temporarily diminish the promotion of *Three Tenors I* and *II* and the court said that's inherently suspect.

Therefore, rather than finding the restraint is ancillary and then embarking on the Rule of Reason analysis as is traditionally done, the court said, "Let's see their justification. Let's see if I buy this. If I don't buy it, that's it. You're condemned."

The defendants put forth what's commonly put forth in any joint venture analysis: That the restraint on the promotion of the *Three Tenors I* and *II* prevented free-riding on the promotional effort of *Three Tenors III*, the promotional efforts the joint venture was going to do.

Despite numerous cases finding such justification is legitimate and ancillary, including the D.C. circuit's own *Rothery Storage* decision, the *Three Tenors* court rejected it because it involved products outside the joint venture. The court found, because it was products outside the joint venture, that all this was an attempt to eliminate competition against the joint venture.

There's no basis for this inside/outside distinction. No court, other than *Dagher*, which we'll get to in a minute, has ever really made this distinction. Regardless of whether the products are outside the joint venture, if they can affect the output of the joint venture, courts have consistently upheld such restraints as reasonable or, at least, have gone through the Rule of Reason analysis to determine whether [they are] reasonable.

The court, the D.C. Circuit, said, "Because we are not buying your justification for the free-riding argument, it is condemned." There is no analysis whatsoever of the anticompetitive effects of the restraint.

That's an important step to skip. Had they done the proper analysis, it is extremely unlikely it would have failed under the Rule of Reason. That is, that it would have found to be anticompetitive. The reason I can make such a strong statement is by thinking about what the market definition would have been. It's very likely the market would have included many, many other classical recordings. In that properly defined market, it is highly unlikely, it is very unlikely that *Three Tenors I* and *II* would have had market power. Absent market power, how could the restraint have anticompetitive effects?

As a result of this decision, we are left with a black-and-white dichotomy. If you put all the products that are related to—if you put all the products outside the joint venture under the umbrella of the joint venture, then there's a good chance you're going to be condemned. But if you throw them all in, as we see in *Dagher*, you're okay. So you're at risk when your client insists, "I'm not putting all the products in joint venture. We have other business reasons we want to keep them out." You're at risk despite a lot of laws on joint ventures, that if you get sued in the D.C. Circuit, it will be condemned as per se law.

MR. O'KELLY: Thanks. Tara, not to put you on the spot to defend the FTC's position in this, or for that matter defend the D.C. Circuit's ruling. If I may impose on you?

MS. KOSLOV: I'm not sure I can exactly do that in terms of representing the Commission because I do need to issue the standard disclaimer that my views today are my own and do not reflect the views of the Commission or any specific Commissioner, including the Commissioner for whom I work.

Having said that, it is a little bit more fun to represent something when you have a circuit court position backing you up. So I will do my best.

I do agree with Lauren that practitioners–lawyers, generally, and antitrust practitioners, specifically—really do benefit from having a framework for analysis. Particularly in this area that we are dealing with the continuum of conduct as reflected by *CDA* and a bunch of other decisions going back. It is easier to counsel businesses when you have a framework and it's easier to evaluate risks.

From an agency perspective it is easier to determine how you want to spend your proportionate resources. We too benefit from a framework that is generally accepted so we can pick and choose our cases appropriately.

The framework here, if you look at the ultimate goal of antitrust law, we want to focus on the nature of the conduct and look at it in terms of the economic and factual realities of a specific marketplace, which is where, I think, Lauren was going. But on the flip side, you do need an efficient way to grapple with the fact that you can't possibly do a full-blown analysis of every single type of practice out there. There is a significant body of case law that identifies certain practices as harmful to competition and there needs to be a way to strike that balance. The D.C. Circuit agreed with the Commission. It is consistent with precedent, including *CDA* as well as other cases. I'll talk about this a little bit more later, but I don't think the case turned entirely on the inside/outside distinction. But I'll get to that in a minute.

The point is to benefit from the many years of experience in predicting what are the types of conduct likely to harm competition. There is a great quote from the D.C. Circuit, that when you're dealing with conduct that has a close family resemblance between the suspect practice and another practice that already stands convicted in the Court of Consumer Welfare, do you really need to go through the full Rule of Reason analysis if you can draw those sorts of parallels?

The other important thing is that under the inherently suspect framework the analysis does not end once something has been classified as inherently suspect. The defendant still does get to come back and articulate a reason why, in this case, in this market, under these facts, those presumptions should not apply; the burden should then shift back to the plaintiff, either a private plaintiff or the government, to put forth the more elaborate analysis.

And it bears noting that the plaintiff ultimately does bear the ultimate burden of persuasion. So in the end, it does come back there. So I don't think it's fair to say that things are cut off and the defendant never really gets an opportunity to put more issues in play.

If the defendant does put forth cognizable and plausible justifications, the plaintiff is going to have to jump through more hoops under the inherently suspect framework.

One issue I wanted to flag is this concept of "cognizable and plausible." I hadn't really focused on this but when I looked at the documents again, I think the Commission's opinion did a little bit better job than the D.C. Circuit opinion in separating those two concepts. I agree it might be a little fuzzier in the circuit opinion. If you're interested in teasing this out a little bit, look at the decision written by the Commission versus the D.C. Circuit. As I think of it, "cognizable" is a legal determination. Is it the type of argument that goes to the fundamental goals of antitrust law where you're trying to promote competition, enhance efficiency and promote consumer welfare? As opposed to something "plausible," which is more of a factual determination.

Another quote from the D.C. Circuit opinion that resonated with me on that point was: "If the only way a new product can be properly introduced is to restrain legitimate competition of older products, then one must seriously wonder whether consumers are generally benefited by the new product."

I think in terms of cognizable—the D.C. Circuit did go along with that concept. Ancillarity, as Lauren indicated, is critical to the workability of Section 1 analysis.

The language of Section 1 itself is extraordinarily terse, as we all know. What makes it workable is this long line of jurisprudence and the ancillary concept is a big part of that; it provides a basis for making the sort of efficiencies justifications that let you say that not every agreement between competitors is going to be condemned out-

right. But it does need to be reasonably necessary. That's the phrase that we keep coming back to. There has to be a nexus so the challenged restraint is either augmenting or otherwise supporting the goals of the underlying integration of the JV.

Free-riding is a perfectly legitimate justification in many cases, and I certainly don't think that either the Commission or the D.C. Circuit was trying to eliminate free-riding as a defense. But here, the spillover effect from the moratorium agreement, the agreement not to advertise the first two products, that would have happened regardless of whether Warner and Polygram had entered into this very limited marketing joint venture. The way the Commission and the D.C. Circuit characterized it, this was normal marketplace competition in this market. The interplay between new releases and catalog products, they always affected each other. Companies routinely planned their marketing strategies based on that interplay and you just couldn't argue this was really true free-riding in the term that concept is usually meant.

There was also an interesting timing issue which the Commission decision characterized as not dispositive but relevant. The joint venture predated the moratorium by three months. So they formed the joint venture, and three months later, they came up with the moratorium as a side agreement. The fate of the moratorium changed over time as the parties tried to figure out, are we really going to abide by this moratorium? Are we going to back off it? There was a fair amount of give and take.

Throughout that time, however, the parties never altered their commitment to the JV in terms of the level of resources they were putting into it or their marketing strategies. Which, in my mind, makes it extremely hard to argue that the parties needed the moratorium in order to ensure their full commitment to the venture, because it just did not play out that way.

The final point I wanted to make, and this is just sort of a practical reality point from my perspective as someone who as been at the Commission for ten years. The Commission went one step further. It went beyond the cognizability problem and did a fuller analysis of plausibility—whether, under the facts of this specific market, these justifications actually made sense.

The D.C. Circuit, as indicated, stopped. They stopped at that point and didn't go further. Interestingly, I spoke to one of my friends who attended the D.C. Circuit oral argument and she emphasized to me that the judges were pretty aggressive in their questioning of the parties on the underlying factual scenario, the plausibility, and I believe it was Judge Ginsburg who asked the parties at some point during their argument, "All right, forget about the ancillarity framework issue for a moment and let's just look at the facts. If I decide this case based on the facts, you lose, right?"

And my friend's sense was that the parties basically conceded that under these facts, yeah, they probably were going to lose. The reason, just to tie this up, the reason I think that's relevant is, in my experience at the Commission, rarely, if ever, do we bring cases where we would be able to stop at just the cognizability prong. We always assume that the parties are going to come back with something cognizable and plausible, and that the plausibility issue is, in fact, is going to come back to us.

The Commission staff is always prepared to go to court to litigate a full case. We don't tend to invest our resources in bringing cases that are that borderline. We want to bring the right cases. I think this case was one of those. I think in this case this was conduct that needed to be condemned and would have been condemned either as it was or under a full Rule of Reason analysis.

But again, that's just my experience based on my time at the Commission.

MR. O'KELLY: Vandy, you've read the case; do you have opening positions on this? As an economist, do you have anything special to bring here?

DR. HOWELL: So I read the *Three Ts* and I should say that I struggled with this case. And I also struggled with how to summarize the point of view about the case in five minutes. So I'm going to try, but it is complicated.

I should say my first reaction, and I think this is true for most economists, the first reaction to the ruling in *Three Tenors* is disbelief. I mean, it is literally just—what? How did that happen? I don't understand that. And the reason is market power. So forgetting which standard, whether it's per se or Rule of Reason, I think there's a general smell test of market power that is distressing here. And when you read the cases, the problem is that your concern about this isn't addressed because there really was no meaningful discussion about market power.

I will say that in the discussions about free-riding and about harm, implicit was a belief that these three recordings are substitutes, and that the degree to which they substitute for each other is much more meaningful than other recordings that are in stores. While it was not proven and there was not direct discussion about it, it was implicit in some of the assumptions or the lines of reasoning that have been taken in the case.

So I would say it really stretches the imagination for most people to think that the Three Ts' recordings of 1990, 1994 and 1998 would either be in a stand-alone market or would somehow, through brand, possess enough market power that some minimal restraint in how they were priced would impact consumers in a negative way.

Additionally, I think there is evidence in the case that substitution for another product was important, but it wasn't discussed directly. So when there was discussion

about the promotional activities that happened between the *Three Tenors* CDs and, in particular, the court thought it was very important that there were promotional activities that the 1990 *Three Tenors* album took against the 1994 release of the competing album.

Additionally, the court found it persuasive that, when Warner released the 1994 album, Warner was not deterred in doing its marketing knowing that the *Three Ts I* would be marketed against it.

The thing is, when you look at the Warner marketing documents, they say that they are really concerned about many kinds of alternative products, and that their marketing efforts were meant to distinguish them from many, many other kinds of alternative products.

So it is implicit, I think, in this one document—and I did not see all of the documents in the case because that kind of analysis was not done here—but I think, even at this, it was clear there was a lot of competition around this, other than these three.

So that's one thing. I think most economists have a general belief that the authorities should not get involved in how pricing happens when the market has the ability to discipline those behaviors itself. So that was my first reaction.

My second reaction is that I am sympathetic to the idea that Rule of Reason—a full-blown market analysis for every type of conduct—is, from a policy perspective, not always inappropriate. It would be difficult and I could imagine the world being better off in certain cases where you do not go through that level of analysis.

So the question, I think, in this case is: Is this behavior of the type that should get this kind of quick look or essentially per se ruling, or is it something that should have had full Rule of Reason? I think that it's my belief that there should have been more investigation and that the decision was too cursory.

That's for two reasons. I know that Tara said that the FTC did and the district court did think a lot about the facts beyond this cognizable dismissal of the free-riding argument. But that's not how it reads. How it reads is that the court decided that, because both the FTC and the district court decided that because the agreement about price was outside the original joint venture agreement, that (A) it was, as a matter of law, separate. That they were "separate" products and (B) it was not persuasive. That it was not about the joint venture; rather it was about raising the price of the other product.

So I think that, as an economist, the distinction about whether the agreement happened a month before the joint venture, in the contract of the joint venture, or as an agreement after the joint venture, doesn't matter because the joint venture is an agreement, and the agreement is an agreement. They are both agreements among competitors. So separate from the law, which you're interested in, is whether this culmination of agreements would be procompetitive or anticompetitive. That would be the lens I would want to take to it.

Secondly, I have a concern because the remedy in the case forbid Polygram from entering into any kind of similar price agreements or lack of discounting agreements or marketing agreements with competitors in the future. It worries me because I do think, whether one believes the free-riding argument in this case, I do think there are legitimate free-riding arguments in the world and that there are legitimate potential free-riding arguments that could be important in joint ventures Polygram might face where they really would need to, within the joint venture, make a decision to jointly market a set of products.

An example I thought of was: Just imagine there are two artists and they compete. And they compete in the sense that they both sing the same kind of songs. And right now, they are under different labels and they sell their products separately. There is a discussion about, "Hey, should they record something together? Wouldn't that be great? The market would love that." The parties say for a variety of reasons—especially, let's say, maintaining the value of their own brand—that they don't want to put these two together to do a recording unless they can do some sort of deal around how the joint marketing would happen because they don't want to pull away from the value of their existing brand. I can imagine, especially in the context where there's competition from other products, that a restrained joint marketing effort including this additional product would benefit consumers. So I wouldn't want to a summary rule that would not allow them to do something like that.

My final reaction is that the economics in this case are extremely complicated and the main reason is that, with these albums, they are both complements and substitutes. There was a lot of discussion in the case about the fact that, with a new album like the *Three Tenors III* CD, advertising is done for it that brings people into the store. They could be more likely, potentially, to buy the *Three Tenors II* CD, instead of *III*. They might buy both. The fact is that if the *Three Tenors III* CD did well, because the *Three Tenors II* CD is a complement, it might be expected to cost people more in the future to buy the *Three Tenors II* CD due to increases in demand.

Because the economics are complicated, a quick look did not allow either side to really think fully and clearly about the competitive effects of the behavior. That's why I think, as an economist, the case is not satisfying. It would take that kind of work to understand what the real impact of the behavior was.

So in short, I think that I would have been more satisfied to see more thinking about it, and my gut feeling

is that, while it is important to restrain certain kinds of behavior that—I mean, particularly the remedy in this case has the potential to harm, and I find that a little bit disturbing.

MR. O'KELLY: Lauren, did you want to take a minute to react to anything that Vandy said?

MS. ALBERT: Well, my thoughts in hearing Vandy speak, when she's saying it in economic-speak, my instinct is in a legal analysis. I'm saying, "Why isn't this Rule of Reason? We have had a hundred years of doing Rule of Reason. We should do Rule of Reason. Everybody gets Rule of Reason. It is not fair." She explained in economic-speak just because the economics are so complicated you really should have done it to come to a logical resolution.

MR. O'KELLY: Tara, can I ask you to address two points quickly? One, the last one that Vandy made, which is: Does the remedy itself in this case have the potential to harm competition in the future? And two, I don't want to jump the gun on the inside/outside issue raised earlier, but if the joint venture in this case had brought the *Three Tenors I* and *II* albums into the joint venture, would that have immunized them from scrutiny by the FTC? And if so, would that give them inside/outside distinction?

MS. KOSLOV: Sure. Let me take that second point first, the inside/outside distinction. I think if you go back to the Commission opinion, certainly the Commission did not intend to draw a strict inside/outside distinction. They went to great lengths to emphasize they were not drawing that distinction. They cited examples, including *Rothery* and *Coke*, where the Commission or courts had accepted forms of integration where restrictions on products outside the joint venture were legitimately ancillary.

The point that the Commission and the court emphasized was that the—it depends on the level of integration. Again, along these lines of the continuum, you have to look at the level of integration in the joint venture and that's how you determine how far you can reach to the other products.

One interesting parallel here that I was thinking about is—I don't know if anyone in this audience follows healthcare antitrust in particular, but some of the debate going on with clinical integration among joint ventures of physicians and trying to figure out what level of integration among physicians enables them to get together and jointly set their prices and contract with managed care plans. So if you're looking for some insight into the way the Commission is thinking about that inside/outside level of integration, that's an additional source for some insight.

As far as the remedy goes, I do recall that in the Commission opinion and I believe also in the D.C. Circuit opinion, there was an emphasis on the fact that yes, there are other transactions that these very companies might wish to be involved in where the order might restrain them in some way, but the Commission and the court ultimately believed this was the appropriate balance in terms of trying to draw the line in what they were and were not going to be allowed to do in the future. I think if you had a situation where they did decide to include the products, fully include them into the joint venture so they were integrated, I don't think that would run afoul of the remedy. I think they would be able to do that.

I think that the Commission actually anticipated there would be situations, given the realities in this marketplace and this interplay between new releases and catalog sales, where it probably would come up again. That was why they felt they needed to have something, but certainly believed there was room for procompetitive JVs among these parties going forward.

I think ultimately what it comes down to is: Businesses make a ton of business decisions every day. Our whole economy is premised on a lot of joint activity that goes on out there and every day you make choices, and each choice bears a certain level of risk. I think the message here is that you can minimize your risks by fully integrating. Sometimes that's not going to make sense from a business perspective, and that's when you have to figure out what level of integration justifies what level of ancillarity.

DR. HOWELL: I did have one thought about the inside/outside distinction. From a theoretical perspective, it feels to me like why should there be a distinction? They are both agreements. Economists are in a nice position to think that way because, often, we are thinking in ways that aren't applying to the real world.

It strikes me that the one upside, in a sense, of the distinction between inside/outside is that if it is inside the terms of visibility to the authorities when there is a look at what's happening, then it is happening at one time. To the extent that the parties can consider the impact of their behavior and consider the degree to which they will be agreeing and have that be visible at one time so it is looked at one time, I can see a policy benefit potentially in efficiencies.

MR. O'KELLY: The inside/outside, Vandy, is a good opportunity to segue into our discussion of the next case that's part of our template for today. That's the case that was captioned in the Ninth Circuit *Dagher v. Saudi Refining* and in the Supreme Court *Texaco* against *Dagher*. The facts in this case are pretty straightforward. In 1998 Texaco and Shell Oil, who had been direct competitors in oil and gasoline markets, had agreed to combine all of their refining and marketing in the western United States, west of the Rockies, into a joint venture by the name of Equilon. The terms of the joint venture were that Shell and Texaco pooled all of their resources and agreed to

share equally in the risks and the profits of the joint venture.

Most significantly for the litigation which followed, they decided to keep the Texaco—to retain both Texaco and Shell brands because there was a value associated with those brands and also, there was evidence that each of those brands had its own brand-loyal customers. However, Equilon would have a free hand in setting the prices of gasoline products sold under those two brands.

The Federal Trade Commission and four attorneys general in the western states investigated the joint venture and eventually entered into a consent decree with Texaco and Shell, where after some divestiture of assets, the formation of a joint venture was approved by the FTC and the attorneys general.

Once the joint venture was up and running, a class of something like 23,000 Texaco and Shell service station operators in the western states sued, alleging that the price-setting mechanism within the Equilon joint venture was per se unlawful price fixing. The district court held that the Rule of Reason should be applied to the analysis and because the class had affirmatively foresworn any kind of Rule of Reason claim, granted the motion to dismiss by the defendants.

The Ninth Circuit disagreed. It reversed the district court. It characterized the arguments being put forward by the defendants as a request for an exception to be carved out from the per se rule against price fixing and remanded the case to the district court with a strong hint that the district court should find the agreement, the arrangement, per se unlawful.

An important part of the Ninth Circuit's analysis was the way that it had applied the ancillary restraints doctrine. It held that the price setting mechanism within Equilon was not ancillary to the legitimate procompetitive purposes of the joint venture, such as the synergies, efficiencies, so forth, and held that those benefits could have been achieved by less restrictive means than having Equilon set prices for the Texaco- and Shell-branded gasoline products.

The Supreme Court reversed the Ninth Circuit. The Court summarily rejected the idea that the per se rule should apply and, indeed, the Court went on to say that the challenged behavior shouldn't be subject to the Sherman Act at all. It characterized the price setting as being the merely internal pricing decisions of Equilon and its legitimate joint venture. And the fact that Equilon chose to sell gasoline products under two different brands that, in the eyes of consumers, appeared to be competing was neither here nor there.

The Court also took a bash at the way in which the Ninth Circuit had applied the ancillary restraints doctrine. The Court said that the ancillary restraints doctrine only applies to restrictions that are outside of the joint venture restrictions that, in essence, are ancillary to the operation of the joint venture, and simply had no application here, where the challenged conduct was inside the joint venture.

Tara, you got beat up by the other two members of the panel last time around. Do you want to take the lead this time? I know the FTC put in an *amicus* brief favoring the defendant's position in this case.

MS. KOSLOV: We did. There was an *amicus* brief filed by the FTC and DOJ signed on to that. Subsequently, I don't have that much to add because the Court largely adopted the analysis that was set forth in the *amicus* brief.

I think the key point from the government's perspective was the ancillary restraints doctrine itself presumes that you are applying it to a restraint that is eliminating competition in some way. But here, competition was eliminated by the formation of the joint venture which underwent elaborate review by the Commission. The merger shop that looks at all the petroleum deals did a full-blown investigation, second requests, consent agreement where they looked at specific market concentration and specific market products. The whole shebang.

So the agreement couldn't possibly be ancillary because there was no longer competition. There were no longer two entities, just the one entity. So I think that was the overriding theme of the Commission's brief.

One interesting point—I could tee up something that I was thinking about as I was going through this, a theme that was really emphasized in the government's brief, in particular coming from the DOJ side, the DOJ being the agency that's charged with criminal cartel enforcement. The brief emphasized that DOJ has a very strong interest in maintaining a relatively bright line of some conduct that is truly hard-core conduct.

There are two reasons they would have that interest. One would be, as a litigation matter, the DOJ likes to be able to go in and summarily condemn certain hard-core cartel activity without having to go through an elaborate Rule of Reason analysis. But there is also the deterrent effect, the idea that businesses derive useful guidance from these sorts of cases. If you chill legitimate conduct, which the government certainly believed was the case here, that claiming that this conduct was per se unlawful would chill very legitimate conduct of a joint venture, that would go too far the other way because you have all these integrated joint ventures out there making day-to-day business decisions on the ground of how to run their operation. If all of a sudden, they have to second-guess every decision and worry about whether they are going to be opened up to per se liability all over again, that's probably not an effective way to provide guidance to businesses.

That does raise an interesting question with *Three Tenors*. Under *Three Tenors*, because you have this inherently suspect framework and the burden does shift in some sense back to the defendant, you certainly could argue that that framework also has a chilling effect on procompetitive conduct. I think we would certainly argue that the conduct in *Three Tenors* deserves to be chilled because it did not have any redeeming procompetitive applications. The parties made it clear the only reason they were engaging in this moratorium was because they were so sure the third *Three Tenors* recording was going to be so much worse than the first two they knew no one would buy it unless the prices were all the same and they could somehow restrict the discounting of the first two. So that should be chilled. Clearly, one could argue that the question of the chilling effect does get a little bit more blurry after *Dagher*.

MR. O'KELLY: Lauren, very few people had anything positive to say about the Ninth Circuit's decision in *Dagher*. They say that a good advocate can always argue two sides of any issue. Can you weigh in with anything positive to say?

MS. ALBERT: Yeah, I feel I have to give a disclaimer: This is the second time I've been on a panel where I'm defending the Ninth Circuit's analysis of *Dagher*. It is not necessarily my own views, but I'm an actress playing a role here.

In *Dagher*, we are seeing the flip side of an in-and-out economy. In *Three Tenors*, the restraint of all products outside the joint venture was condemned as per se unlawful and bypassed the Rule of Reason test. In *Dagher*, the restraint involves activity within the joint venture. Because one of the purposes of the joint venture was to market the Shell- and Texaco-branded gasoline, any restraints relating to those sales is activity within the core of the joint venture. And as much, according to the Court, activity within the joint venture is per se lawful. In other words, whatever you do within the joint venture is unassailable. You don't look at it under the Rule of Reason, per se test or anything in between.

Again, as in *Three Tenors*, we are giving the ancillary restraints test. The Court said, "We don't have to get into it because the restraint at issue was within the joint venture." Such inside/outside dichotomy is misplaced here just like it was in *Three Tenors*.

Never before has the Supreme Court made such a distinction. Instead, the Supreme Court, as well as lower courts, always applied the ancillary restraints test regardless of whether restraint was inside or outside the joint venture.

The Court did make a pass at the ancillary restraints test, but then misapplied it. The Court said, "Even if we were to invoke the ancillary restraints doctrine, we find the pricing policy at issue here is clearly ancillary."

But a conclusion that the restraint is ancillary doesn't mean it is lawful. Once it is decided that the restraint is ancillary, it means the per se test isn't applied. Instead, you go ahead and do your Rule of Reason analysis to determine whether the procompetitive effects outweigh the anticompetitive effects.

The Supreme Court in *Dagher* never did that. The court of appeals did. The court of appeals went ahead and said, "Let's look at the traditional ancillary restraints test."

The Ninth Circuit said there were fact questions as to whether the defendants had proved ancillaryism. That's a big point about why I've been able to go around defending the Ninth Circuit. I really think what they were really doing is saying it was a matter of proof. Defendants failed to prove ancillarity. Defendants demonstrated how setting the prices of the two brands the same was reasonably necessary to achieve the efficiencies of the joint venture.

The purpose of the joint venture was to save cost. The evidence showed that the two products were physically different and marketed to different consumers. One brand of gasoline more for blue collar and one brand more upscale.

Witnesses testified that the two setting the price of the two products the same was unrelated to achieving the synergy or the joint venture.

The Ninth Circuit concluded that the case should be remanded to a jury for a determination as to whether the restraint was ancillary. If a jury found it was not, it would be per se illegal.

The bottom line is that now if the restraint alleged to products within the joint venture skipped the ancillary restraints test, then you're free to impose any restraints you want.

MR. O'KELLY: Thank you.

Vandy, do you have anything to add on *Dagher*?

DR. HOWELL: Not a lot. You know, basically two companies, commodity products, efficiencies in distribution, they do a JV. The authorities look at it with some detail. They actually ask them to divest certain assets so they can be comfortable that the downstream aspects would not be anticompetitive. Approved it, and then the question is: Are they allowed to price within that joint venture the way they see fit in a market which has been, through Rule of Reason, decided that they won't have the ability to impact anti-competitively?

It feels like the answer to that should be yes, they should be allowed to do that.

The one thing I think is interesting about it is in these two cases there is the inside/outside distinction. There's also a difference in the burden of proof on what is. I use

the word "necessary" to achieve the joint venture versus what would have an anticompetitive effect.

Obviously, those levels of proof are very different. In *Three Tenors* as well, where I think the economics got confused was about having to prove the procompetitive effect of the marketing of these three products, let's say, assuming you don't care about the inside/outside distinction.

How do you prove the procompetitive effect on the market of this marketing choice versus how do you just set the burden of showing that it's not anticompetitive? And they are different.

I think there are probably all sorts of practices in the world where showing the procompetitive effect may be complicated, but proving that it is not anticompetitive would be less complicated.

MS. KOSLOV: If you look at the *Three Tenors* Commission opinion at page 30, it pretty explicitly says that under the inherent suspect framework, "The defendant is not obligated to affirmatively show that it is procompetitive"—i.e., if it were at least plausible that it was competitively neutral, you would then shift the burden back to the plaintiff.

I think that was obfuscated in the D.C. Circuit opinion, so I would definitely agree. When I went back and looked at it, it is not as clear in the D.C. Circuit opinion. I can see where that would cause some problems.

But if you go back to the Commission opinion, I don't think that was the Commission's intent. I think the way the Commission framed it, if you could at least come up with something plausible and likely, even if that meant it was neutral, you wouldn't necessarily have to prove it was affirmatively procompetitive.

DR. HOWELL: I think my answer for that would be that, for the pricing in *Three Tenors* to be neutral, it just needs not to be anticompetitive. There wasn't, essentially, any proof that the impact of that pricing could harm consumers.

So in the same way that the Commission didn't have to prove that the choice of the pricing would harm consumers, you know what I mean? They didn't prove it would harm. The other side didn't prove it was procompetitive.

MS. KOSLOV: That's where you get back to the fundamental disagreement whether "inherently suspect" is a meaningful framework.

Going back through the history of antitrust, there's a pretty strong conclusion that restrictions on price discounts and the advertising of price discounts is never going to be good for consumers. It is going to deny consumers lower prices and the availability of lower prices.

It comes back to the same thing: Based on all these years of experience in antitrust, should we still need to start from square one and do an elaborate Rule of Reason analysis to show that price discounts are good for consumers? Our answer was no, we should be able to rely on a presumption that discounts are good and bans on discounts are bad.

DR. HOWELL: Maybe there's some sort of shortcut for market power as well that we could develop over time.

MR. O'KELLY: Time not being our friend, we need to move on.

We have devised a hypothetical where we have tried to bring together elements from the *Dagher* and *Three Tenors* cases. Before we got started here, Saul mentioned the Co-chair of this panel, James Yoon of the Attorney General's Office and to give credit where it is appropriate, James is the principal author of the hypothetical.

The hypothetical is to be found in the book. It actually starts on page 175. We have put up some of the highlights in the Power Point presentation. We also have in here an outline of the state of the antitrust law as it applies to joint ventures.

This joint venture has been—or this hypothetical has been circulating in draft form for several months now, and it was long before Apple announced its recent I-phone and I'm convinced that somehow Steve Jobs hacked into James Yoon's computer because we got there first. James got there first.

One of the players in the joint venture is Samson Corporation, which develops, manufactures and markets digital phones and hand-held devices, such as Blackberries and PDAs and so forth. The other party is the MeTube Corporation, which develops, manufactures and markets digital phones also but also manufactures video transmission devices.

For purposes of our JV, Samson and MeTube—well before the JV, they are aggressive competitors in the United States and worldwide in the development, manufacturing and marketing of digital phones.

One of the big selling points for Samson's phones is they had very clear visuals, very clear picture screens.

One of the big selling points for MeTube's phones is they have acknowledged superior capability for recording film clips and photos and so forth.

In the particular marketplace, Samson has a market share of 16 percent. It's the top-selling brand in the United States. MeTube was number two with 14 percent. They do have a very close competitor, W. Corp. which is 12 percent of sales and, of course, there are other players in the marketplace.

In 2005, Samson approached MeTube and proposed the formation of a joint venture. They hoped that they could improve their respective superior capabilities in the areas where they were strongest in order to produce a phone that would be capable of receiving full-length movies and music videos to be distributed over the air and playing them on the phone screen with a high degree of fidelity.

The proposed terms of the joint venture, principal terms were that Samson and MeTube would perform—would combine all of their digital phone research, manufacturing and marketing assets in this new venture which is to be called SamsTub.

For their sharing of the risks and profits, Samson would have 56 percent of the joint venture. MeTube would have 44 percent.

They both agree not to license any of the patents covering their earlier versions of digital phones or video transmission devices.

SamsTub, the new joint venture, in addition to selling the new SamsTub phone will not market aggressively or actively the earlier versions of the Samson and MeTube digital phones, and Samson and MeTube, the joint venturers, agree not to engage in the manufacturing, marketing of certain products, including the digital phones in the United States.

Let's just stop at this point before we go on to the next set of facts.

Tara, if the FTC were to look at this proposed joint venture, and conduct a merger analysis, how do you think the joint venture is doing so far?

MS. KOSLOV: Rather than give a thumbs up or thumbs down—obviously, it is a hypo with a lot of issues—I do want to flag the joint FTC/DOJ guidelines for collaboration among competitors which still do remain a primary source of guidance for people looking at these sorts of things. They were issued in 2000 so they do predate both *Three Tenors* and *Dagher*. But they certainly echo a lot of themes that came up later in *Three Tenors*. So that's the place that I certainly went back to, to figure out where the agencies would be on this fact scenario.

One issue that I wanted to tee up was the idea of: What is the market we are talking about? Obviously, whenever you analyze a joint venture and whether it is going to cause competitive harm, you need to identify in which market you're identifying the competitive harm. As I see it, you could have a couple, or maybe even three, markets at play here. There is obviously the market for the products themselves. We get into the question of whether the market is all digital phones or digital phones with particularly good video technology. So you've got some market issues there, possibly, that would probably require some more analysis.

But I also wanted to flag the concept of R&D markets and innovation markets because that's something that increasingly comes up in a lot of cases at the Commission, not just joint venture conduct cases. It is something we grapple with every day.

If you look in the guidelines for licensing intellectual property from 1995, if you've got a separate market for the IP itself, which would be the last—the middle bullet, the "agree not to license patents" bullet. If there is actually a market for the licensing of the intellectual property that is separate from the market for the products themselves, that market would comprise the intellectual property here plus any close substitutes for it.

So I think we need to look at, to an extent, whether this particular portfolio of IP is necessary to make digital phones at all. That's something we don't have in the fact pattern. That's, in large part, where the Commission would start, given the huge amount of attention to IP these days. Trying to figure out whether that separate agreement is practically cutting off all future entry or competition because nobody will be able to practice its IP anymore.

MR. O'KELLY: Vandy, when Lauren comes to you and says, "I represent one of the partners in this joint venture. We haven't worked out all the details yet." And hands you a printout, these five bullet points, and says, "As an economist advising us, help us get past the FTC." What is it we need to know to be able to give any kind of informed advice to Lauren and her client?

DR. HOWELL: Right, so there's a couple of things: The third bullet point which says, "Agree not to license patents of earlier versions of digital phones or video transmission devices." My question is the same as yours. I would want to know—first, define the market. Second, are those patents currently being licensed and would that impact? We saw these market share numbers and it seems like MeTube and Samson, by themselves, don't seem particularly large. Assuming, let's say, that the products in these markets are substitutes. But if MeTube and Samson, right now, as separate entities, are licensing critical IP to Gray Bar, and they decide to do a joint venture where the decision in the joint venture is, "We will no longer do that," then that can have a very big impact on the market. So I would want to understand not only what kind of IP it is, but also what their current licensing practices are. That was one thought.

MS. ALBERT: From a lawyer's perspective, I would be concerned that under *Three Tenors*, the agreement relating to patents, do the ancillary restraints analysis and its per se unlawful products, patents outside their joint venture—

DR. HOWELL: That's the other thing. I think that the digital phones would be inside the joint venture because, now, this is a joint venture that does all of their digital

phone operation. But it also says, "Samson and MeTube agree not to engage in the manufacturing and marketing of certain products, including digital phones," which implies there are other products that may not be inside the joint venture. And for me, whether they are in or out of the joint venture is less important than if they essentially don't compete in any way with the products inside. Hence, free-riding may be less of an issue and kind of what their reasons would be for constraining that.

MR. O'KELLY: Let's go back to the market share slide for a second. Would it matter to you how that Gray Bar—we know the market shares of the top three players in the market. Assuming this is the relevant product market, would it matter to you what the number four, number five and number six guys' shares were, Vandy, as an economist?

AUDIENCE MEMBER: Can you say the question again?

MR. O'KELLY: The question was: Would it matter to Vandy, as an economist, what the market shares of number four, five, and six, all lumped together, in that gray bar for the rest of the market?

DR. HOWELL: I would say yes and no. I mean, it's obviously a static market share chart. Let's say they were all one percent, you know. It might make you think that they weren't powerful competitors. But in a market where there's a lot of innovation, I think you cannot assume that. So it could very well be that, at one point in time, they were small, but two years ago one of them had 40 percent of the market, and they've invested in R&D to compete with the new products that will likely bring them back into 40 percent share of the market. I think you would need more information than just a one-time share to be able to assess the competition in that market.

MS. KOSLOV: It also goes back to the licensing question. If the IP is as important as we think it might be—and if removing the ability to practice that IP is going to dramatically influence market shares on an ongoing basis—then you absolutely cannot rely on static market shares to make predictions.

MR. O'KELLY: Lauren, what would you want to say to your client at this stage of the joint venture?

MS. ALBERT: So far, I think they are pretty good. I'm concerned about the last bullet with things other than digital phones. We'd take care of that. I'm a little concerned about the patents. We'd probably have to tweak that and place all the phone-related patents into the joint venture.

MR. O'KELLY: And you would need to place them into the joint venture because?

MS. ALBERT: Under *Dagher*, it is per se.

MR. O'KELLY: Okay, during the operation of the joint venture, the Samson and MeTube corporations will continue to operate as distinct corporations. Each will retain its own trademarks and keep control over its own brands. And SamsTub, within the operation of the joint venture, may not give preferential treatment to either Samson or MeTube.

SamsTub will maintain the Samson and MeTube brands as distinct products and each will have its own color, sound. And the two "parent corporations," if you will, will continue to compete for customers at the retail level. So they will continue consumer marketing.

Assume that they can satisfy the FTC and attorneys general and the formation of the joint venture can be approved, we go on to the question of how they are going to price their products. The SamsTub joint venture decides that the Samson and MeTube branded phones will have the same price structure, and they decide as a business matter to price their phone in each category lower than the competing products of the nearest competitor, W. Corp.'s digital phones. Any reactions to their initial pricing decisions?

MS. ALBERT: I think under *Dagher* it is pretty easy. Under *Dagher*, you can price it whatever way you want, the same or different. There was a lot of noise in *Dagher* about, before, the two products were priced separately, but then all of a sudden, they come out of the joint venture and they are priced the same. But the Supreme Court said it doesn't matter, pick whatever price you want. Which is the same in this matter.

MR. O'KELLY: You're comfortable that even though the Samson and MeTube phones are, to a certain extent, analogous to *Three Tenors I*, *Three Tenors II*—

MS. ALBERT: We are talking about the phones that are being marketed by the joint venture.

MR. O'KELLY: These are the phones—

MS. ALBERT: Right, now they are contributing to the joint venture and the joint venture now controls them. It's just like the Shell and Texaco gasoline. Contributing to the joint venture, so it is the output of the joint venture.

MR. O'KELLY: Tara, are you okay with that?

MS. KOSLOV: Again, I wouldn't want to start the inside/outside discussion. But I do think you need to look at the degree of integration. Here, where the first indicia they are integrating is the idea that they are contributing to the venture and sharing the profits and the losses. I think under the fact scenario we were given, the 56:44 was proportional to the contribution of their assets. That level of integration shows they are both vested in the outcome, the financial success of the joint venture. So that's a good indicia of integration.

The pricing bothers me because it seems almost axiomatic that low prices are not supposed to be a defense to something that's anticompetitive. It is never supposed to be a defense that, "We are fixing prices but we are fixing low prices, so that's okay." That gives me a little of heartburn, although here, I think you have a good chance of jumping over the ancillarity hurdle.

One point that occurred to me is that their ability to sustain a lower price structure in the first place might be a good indicator there really are genuine efficiencies from this joint venture. If they actually can price lower, and that means you've got cognizable, plausible benefits being passed onto consumers, that is a good thing.

MR. O'KELLY: Vandy, do you have any comments on this pricing arrangement?

DR. HOWELL: Just that you said assume that the FTC says it is okay and the JV is found to be—the formation is allowed. I'm assuming it's the formation with the previous five bullet points, which means that essentially the intellectual property markets have been sorted out and been found not to be blocking and, to the extent that there are efficiencies in the way they have chosen not to market their previous generation digital phones, that's been found to be okay, it seems like with all that together, I don't see why this would be a problem because I would assume that meant they did not have meaningful market power.

Additionally, I think it is a really good point about the lower prices potentially signaling the impact of the efficiencies.

MS. KOSLOV: I should caution that we are sort of presuming there was some sort of quasi-Section 7 analysis of the underlying joint venture. It is still unclear to me, based on these facts, whether there is sufficient integration where this would rise to the level of transaction where you would switch to that Section 7-type of analysis. I'm not entirely sure you would get there.

MS. ALBERT: Although I would like to say what Vandy said in explaining the facts of *Dagher*, the state's Attorney General said there were divestitures and still it got all the way up to the Supreme Court.

AUDIENCE MEMBER: I had a question: How much more integration do you need? This is all of the production, all of the R&D and all of the marketing put into a structural joint venture. You can't get much more integration than that.

MS. KOSLOV: They are putting everything in. But if you look at what's coming out, there are still products, as in *Three Tenors*, there are still some legacy products that are out there that are going to be competing against each other. It is not clear to me who is going to buy them because it is not clear who is going to be marketing them. It sounds, at least at a retail level, as if there is some incentive to pitch some of those older products one way or another. So you are still preserving some level of competition between the two of them.

In our hypothetical, are we presuming all of their R&D will be combined?

DR. HOWELL: In the first scenario. I think in the first scenario—well, it is a little confusing. They are sold separately in the downstream, but they are owned essentially by the joint venture, right? The old products?

MR. O'KELLY: I think the idea is that the Samson and MeTube brands have a wider recognition than just mobile phones.

MS. KOSLOV: One other point I want to raise is I had mentioned there are multiple markets, multiple layers where you might need to evaluate the competitive effects. One that we didn't mention is an R&D market, which is separate from the licensing market. The licensing market is where there is a separate market for licensing of the patents in addition to the product. But to the extent they are currently competing to innovate, to develop new products, obviously there are very strong procompetitive benefits from bringing that R&D together so they can innovate a fabulous new product that might get to market sooner. But you have to look at who else is out there and see who is doing R&D. And if these are the leaders in the race to innovate, and the race to market is really what's driving each of them to engage in R&D, there is some loss of competition on that level, and that's something we would look at closely as well.

DR. HOWELL: Although it looks in this case that there is specialization of the R&D, the patents they have are a little bit different. So they are competing downstream.

MS. KOSLOV: That would also come back to that market share chart we were looking at and would it be different depending on the composition of that other bar? If that other bar is fairly fragmented and there's maybe six or seven other companies out there and all innovating in the same product space, as opposed to now you only have three companies, two of which are combined in the joint venture. So now you maybe get into only two real players in this R&D market and are there incentives to include or coordinate?

MR. O'KELLY: Tara, you said the pricing arrangement gave you a little heartburn, but the heartburn was alleviated somewhat by the fact that they had agreed to set the price lower, due possibly to some efficiencies. Would your analysis be different if they decided to currently peg their prices higher than the next competitor?

MS. KOSLOV: I would have a lot more discomfort if the prices were higher. As I said, if the prices were lower,

you can try to tie that into some ancillary argument that you were able to create efficiencies in the form of lower prices. So that is both cognizable and plausible, back to our inherently suspect framework. Hard to argue that there is a procompetitive benefit to a higher price, unless you're making a very strong argument that it is a quality-adjusted price. That the value of this new product is so great that you can't look at it on merely a pricing dimension, you have to look at it on a nonpricing dimension as well.

AUDIENCE MEMBER: Why else would somebody be buying it at the high price?

MS. KOSLOV: You would have to assume that they wouldn't buy if it was higher and that would be a rational business decision. It depends on who else is out there. If there is only one other big player out there and they hike up their price too, so now you've raised the entire pricing structure in the market.

MR. O'KELLY: Lauren, aside whether or not it makes business sense, does it matter from a Sherman Act perspective, post-*Dagher*?

MS. ALBERT: I really don't think so. I think *Dagher* says, "You're taking the Shell and Texaco brands, taking the Samson and MeTube, you're contributing to the joint venture, you can do whatever you want under *Dagher*."

MR. O'KELLY: Tara, do you have a reaction to that?

MS. KOSLOV: I just don't like it.

AUDIENCE MEMBER: Wouldn't, however, in a post-deal Section 7-type analysis, the fact that the joint venture hikes their prices so much be a potentially relevant factor?

MS. ALBERT: Well, that's a good point. The merger was anticompetitive or the joint venture was anticompetitive, and the agencies blew the Section 7 analysis and you now need to come in.

MS. KOSLOV: That's sort of what I was getting at with the idea that you have to look at the rest of the structure of the market, and if the reason they were actually able to effectuate a price increase is not because they have a much better product and can sustain it on a quality-adjusted basis, but because there is no one else left in the market.

AUDIENCE MEMBER: What is the outlook of the joint venture going to be in a post-deal world? If prices go up, that will probably tell you that the quality of the product has probably improved and the demand for the improved product is such that it increased output, even though the price has gone up.

DR. HOWELL: I think that's the analysis that was used.

AUDIENCE MEMBER: The only market share data you have says that the joint venture entity is 30 percent. If someone else was 12 percent and everybody else has less than 12 percent, if that's the relevant market, your market structure is such that you probably wouldn't even get a second request. So if your relevant market is reflected by your market share, it seems to me a lot of your questions would go away. It doesn't even rise to a unilateral effects case, 30 percent.

DR. HOWELL: I think our stance in the hypothetical is that there would be a lot of inquiry about what the relevant market here is because you brought up R&D and IP markets. Additionally, to the extent these products are very differentiated, it may be the digital phones are their own market. Or someone argued that.

MS. KOSLOV: Or on the flip side, you could argue that digital phones capable of supporting high-end video are their own market.

DR. HOWELL: Right, a market unto itself. Right, so it is a creating a new market.

MS. KOSLOV: I guess that is what's very fact-specific about the analysis. My gut feeling is, under these facts, you would probably get far enough along the inherently suspect framework to actually get back to the point of needing a Rule of Reason analysis because I think it is market-specific.

AUDIENCE MEMBER: There seems to be some criticism of the analysis or answering the question whether the product is in or out of the venture as being overly formalistic. But in some sense, form really matters in trying to decide the capacity in which the seller is in. Now, if we think about a deviation on the *Dagher* facts, suppose that Shell and Texaco, after having formed Equilon, decided to sell Shell Classic and Texaco Classic gasoline in competition with the Shell and Texaco that Equilon was selling through the venture. In the process of selling Shell Classic and Texaco Classic, Shell and Texaco entered into an agreement with the executives at Equilon and said, "You know, our brands are a little close together here. Why don't we just agree that you guys will sell Shell and Texaco in your venture with all the promotion you want, and in order to make life easier, we, Shell, and we, Texaco, will sell our own new brands of gasoline, called Classic, without any promotion and ten percent higher than what you sell your gasoline." And they reach that agreement. And then they go to the Supreme Court with those set of restraints. Does anyone really think that that set of agreements between Shell and Texaco and Equilon, all as separately formed corporations, would have been given the blessing the Supreme Court gave the internal pricing decisions of Equilon? My guess is probably not. We would have thought that that was three separate actors on the marketplace, under *Copperweld*. Three centers of competi-

tion, because we create Equilon to be this independent self-sufficient joint venture, and that it was collaborating with the shareholders for separate companies who were on the marketplace in competitive capacity. If we go back to *Three Tenors* and we say, "Well, is this venture really a stand-alone recording company, or is it really just an agreement between Warner and Polygram to jointly market and record a Three Tenors concert?" And ancillary to that agreement, acting in our capacity as collaborators we will say, "We have these other obviously *Three Tenors* and in order to make this venture successful, since we are collaborating on the marketing and recording project here, we are just not going to market our old *Three Tenors* actively around the launch of the third *Three Tenors*." That looks a lot more like a constellation of agreements to actually promote and to make economically plausible the recording of a third Three Tenors concert. I mean, who would think—two might be enough. The third one might be redundant and the investment in the third recording project likely to succeed, you can't cut off its legs in the process. Instead of having a sort of formal view that these were three separate competitors on the marketplace, but rather two companies that were collaborating in the recording and sale of the third Three Tenors concert, it looks like an ancillary restraint.

Now, some might say that's form over substance, although I know that people who tread in the Section 1 world are enormously concerned about whether it is a single actor, whether they are acting as competitors. The answer to that question of course is a threshold question as to whether there is any restraint at all. And that, I think, is what the Supreme Court was saying in Equilon. There is simply no restraint here at all. It is the core of the joint venture's activity. The ancillary restraints doctrine doesn't apply.

MS. ALBERT: Your hypothetical kind of raises an issue that kind of lingers around *Three Tenors* and *Dagher*, which is the timing of the agreement. It didn't doom them in *Dagher*, but I think it was very important in *Three Tenors* that they came up with this moratorium a couple months after they formed the joint venture. And in your hypothetical, they are going around selling Shell and Texaco gasoline through Equilon for a while and then come up with this other restraint post-fact. And the courts may say that clearly wasn't ancillary because you didn't need it to do the joint venture, so we are not buying it.

AUDIENCE MEMBER: And in *Dagher*, it was clean because Shell and Texaco withdrew from the retail market for gasoline in the geographic territory of Equilon. So they really were pooling their assets and acting through a single actor. In *Three Tenors*, obviously, Warner and Polygram were still active in whatever the relevant market was. Once you call that enterprise a joint venture, it sounds like there are three players on the market as opposed to two who had formed a contract to jointly record the market.

MS. ALBERT: I just want to correct one thing: In *Dagher*, it looks clean if you read the Supreme Court. But it doesn't look clean if you read the Ninth Circuit. They came up with this pricing decision months after they formed the joint venture and there was a lot of evidence saying, "We really didn't need this pricing thing to achieve the efficiencies of the joint venture."

AUDIENCE MEMBER: Lauren, you put your finger on a critical distinction and important fact on the *Three Tenors*—that was the timing of that decision. The timing of that decision tells you that the decision was not essential to the creation of the joint venture in the first place. And I think people have a problem with the decision because it uses the language of per se or presumptions when, in fact, if you have these three separate entities go back and re-engineer the joint venture after they discover that the product they had gotten together to create really wasn't going to be that competitive. It changes the assumption that they went into the joint venture with. Maybe the solution would have been to simply disband the joint venture because the market really wasn't going to buy this new product rather than go back and try to change their marketing. The problem is restraints in the context of the joint venture where you have two parties who have complementary assets they need to put together to create this "new great product." The restraints make sense if they are necessary to create that great new product. The timing problem suggests that they weren't necessary to create this new great product until they discovered the Three Tenors were planning to record the same stuff they recorded before.

MS. KOSLOV: There is actually more to it that than that because there's another piece of evidence that shows it was not necessary to create the product. It would have existed no matter what. One of the companies was going to do it and then the other company came in looking for a piece of the recording rights. They said, "Why don't we do it together?" A third party developer, Rufus, I think, was his name, he was the one who created this concert. It was going to happen no matter what.

DR. HOWELL: The thing in *Three Tenors* that seems different also and underscores what you said are the efficiencies of the JV at all. You can see the efficiencies in *Dagher*. You can imagine what they might look like. It doesn't stretch. But when you think of the *Three Tenors*, the only efficiencies you can think of are maybe that one of them is better at distributing in the rest of the world than in the United States or something. But it is a little hard to understand. It seemed like the cause of the joint venture was really that they had different rights and the way that they could agree so that the album actually gets sold was they had to agree to sell it together.

AUDIENCE MEMBER: Moving back to the technology sector, would the nature of the proposed research get factored into the analysis? So imagine if the two companies decided they wanted to leapfrog several generations of technology and develop a head-mounted 3D phone, neither one of which could necessarily achieve the goal individually, and the goal itself being something that may or may not even be possible in the presence of the joint venture?

MS. ALBERT: Yeah, I'm not sure I understood your question. But would our analysis change?

AUDIENCE MEMBER: Right, would the analysis change if it was much farther down the road for the technology?

MS. ALBERT: Oh, this is something they can't do for, potentially, 10 years? Actually it wouldn't. That's a common purpose of a joint venture to try to come up and create something that's never been done before.

MS. KOSLOV: If you look at Section 3.2.3 of the IP guidelines, which talk about innovation markets—I hadn't memorized that. I happened to have it flagged—the agencies will delineate an innovation market only when the capabilities to engage in relevant research and development can be associated with specialized assets or characteristics of specific firms. So yes, I think that is relevant. If these two firms are uniquely qualified to do that sort of leapfrogging, by putting together these specialized assets, that is relevant.

MR. O'KELLY: Saul has given us the five-minute signal. We have time for one more question, then I'm going to ask the members of the panel, in light of *Dagher* and *Three Tenors* case, if they had to give a one-minute set of advice to somebody setting up a joint venture, how they would do that.

First, one more good question, if there is one?

We will segue in. Lauren, client comes to you, says, "I'm going to form a joint venture," what's the first thing you tell them?

MS. ALBERT: Put everything in it. Do whatever you want. It is so simplistic.

MR. O'KELLY: Vandy, would you concur with that?

DR. HOWELL: I would say hire an economist, ha! No, seriously, have someone look at the underlying economic impacts of the implications of the joint venture and really think hard about that so that you're not pulling things in you don't need to and so that the things you need to kind of be explicit about you are explicit about.

MR. O'KELLY: From an economist's point of view, is it a good idea if we practitioners tell our clients to put everything into the joint venture?

DR. HOWELL: No, I don't think so. Well, I guess they live in a world where the laws are what they are. So I would, on the one hand, I would say good counsel, but no, I mean I could imagine all sorts of reasons why you wouldn't want to put all of your assets in a joint venture with a competitor.

MR. O'KELLY: Tara?

MS. KOSLOV: I'm going to give you a little more of a big picture answer. When parties come in to advocate on behalf of either mergers or joint ventures, inevitably, the most compelling presentations are the ones where both the lawyers and the economists are able to sit back and let their business people do the talking. Because there is so clearly a contemporaneous procompetitive justification for this, they don't need the lawyers and economists to explain it. They can trust the business people to do it because it is real. Especially when there are contemporaneous documents to back it up from when this idea first came up explaining exactly why they need to do whatever it is they are telling us they need to do because this is the best way to run the business and benefit consumers. So when your client comes to you and says, "We want to do something," you should look them in the eye and say, "Why do you want to do this?" If they can, on the spot, give you an answer that you would be willing to let them go in and tell the Commissioners, you're probably on the right track.

MR. O'KELLY: Anybody have any last words? Thank you all. This was a fascinating discussion and I think we could have probably spent the entire two hours on *Three Tenors*.

(Applause.)

MR. MORGENSTERN: Thank you all. That was really excellent. We will now have a fifteen-minute refreshment break and be back for the final program on Ethics and Experts.

(Refreshment break.)

Ethics and Experts

MR. MORGENSTERN: This brings us now to our final panel of the day: Working with experts, in the ethical and tactical concerns.

Expert witnesses are unlike virtually any other participant in a litigation. They are supposed to have an objective, scientific view of the facts at hand, and yet, they are also working on behalf of a party who, presumably, they'd like to see succeed.

What are the best practices and tactics for working with and sharing information with experts? How do attorneys reconcile their obligation to provide zealous representation with an expert's obligation to provide full and fair analysis?

For our last program of the day we have a panel of experienced class action lawyers and experts who will address these and other related provocative issues that arise between attorneys and the experts they retain.

Our panel Chair and Moderator, Barbara Hart, is a partner at Labaton, Sucharow and Rudoff here in New York City, where she focuses her practices on securities and antitrust class actions. Ms. Hart is the counsel for the Office of the Treasurer of the State of Connecticut, whom she represented in *In re Waste Management Securities Litigation*, netting a settlement of $457 million. She has represented plaintiffs in a number of successful antitrust actions including *In re Warfarin Sodium*, *Maltol Antitrust Litigation* and *Continental Seasoning v. Pfizer*. She currently serves as lead counsel in the *JDS Uniphase Securities Litigation* and co-lead in the *In re Air Cargo Shipping Services Antitrust Litigation*. She has considerable experience working with experts and offering testimony on a wide range of econometric and accounting issues.

Linda Nussbaum is a partner at the law practice of Cohen, Milstein, Hausfeld and Toll in New York. She too is an experienced litigator, well regarded by peers and adversaries. Linda is, at present, lead or co-lead counsel for plaintiffs in a number of significant antitrust class actions pending throughout the United States, including *In re Remeron Direct Purchaser Antitrust Litigation*, *Microcrystalline Cellulose Antitrust Litigation*, *Plastics Additives Antitrust Litigation*, *Children's Ibuprofen Oral Suspension Antitrust Litigation*, *Foundry Resins Antitrust Litigation* and *In re DDAVP Litigation*. I'm going to ask her what that means later.

Joel Cohen is a partner and trial lawyer at the New York office of Clifford Chance US, where he practices in the securities and regulatory litigation group. He represents financial institutions, principals and officers in public companies, and hedge funds in connection with a broad range of criminal and civil matters. His clients have included Citigroup in the *Parmalat* class action, Alliance Bernstein in various regulatory and civil class action matters, and a hedge fund family in the SEC insider trading case. He has represented clients in rubber, chemicals, automobile dealer, and vitamin antitrust cartel investigations.

Dr. Richard Rapp is Chairman of NERA Economic Consulting. He has been a member of that firm for 30 years and was President of it from 1988 through 2006. Dick is a full-time consultant on the economics of antitrust, intellectual property and contracts. He has testified in many prominent cases including, for example, the FTC's *Rambus* litigation, *Concord Boat* and others. Before joining NERA, he was Associate Professor at State University of New York at Stony Brook. Those of us who have had the pleasure to work with Dick are looking forward to his comments.

Dr. Gary French is a Senior Vice President with Nathan Associates Inc. In his 30 years as an expert economist and litigation in regulatory proceedings, Gary has provided expert testimony in antitrust, bankruptcy, contract, employment, intellectual property and other commercial litigation. Many of his assignments have been in class actions in which he has provided expert testimony on class certification. His litigation and other assignments have involved a wide range of businesses and industries, notably telecommunications, pharma, airlines, insurance and restaurants.

Please join me in welcoming our panel.

(Applause.)

MS. HART: When Saul first asked me to do this panel it occurred to me it must be because he knows of my pristine ethical conduct throughout any career and my upstanding reputation. As I rolled up my sleeves more and more to wrestle with the issues and to engage our robust panel on these issues, it occurred to me it was really that Saul was perfectly willing to let me commit career suicide because, really, if we are to bestow upon you the ethics credits and fulfill our ethical duty to discuss ethical issues, we have to really wrestle with the ethical issues that present themselves each day as we try to act as officers of the court and we work with experts who are supposed to act with some modicum of independence or some pure independence. But again, as Saul pointed out, they are retained by parties and parties have their own goals. And their goals are victory and the respective victory means one's victory is the other's loss.

I am going to exercise some control over how this unfolds. I get to play Jim Lehrer. I've always wanted to be on *McNeil-Lehrer*. I'm going to pose questions. We are not going to be too closely tied to a hypothetical. But the hypothetical doesn't particularly matter.

Let's say, for instance, it is an antitrust case. A bunch of union welfare funds and benefit fund managers of pharmaceuticals are suing a brand name drug manufacturer and a generic drug manufacturer for having engaged in a deal whereby the generic manufacturer doesn't enter the market and there are issues, ramifications of whether that's an anticompetitive arrangement.

The plaintiff's lawyers on behalf of consumers and benefit funds file class actions and the defendants engage defense counsel.

Now as I pose questions—and that's really almost not germane. It could be any kind of price fixing conspiracy that's going to trigger the issues which are really about the experts and the ethics and how we work effectively, efficiently, ethically in trying to reach the truth.

As we try to reach the truth today or try to address the truth today, I would almost like to do a pens-down session, where this is Las Vegas and everything that's said in this room stays in this room or something like that. Because the point is for us to elicit, really, what these practitioners and these experts grapple with as we try to appear before the court and we deal with the tension of wanting to win and wanting to be "truth speakers" and wanting to help the court to get to the truth.

So to do this, I am going to pose questions, rather bland questions, in the hope that the panelists—we have all gone through these issues on the phone and I'm quite excited about what information I think is going to be shared, and the nature of the conversation.

But the panelists are going to try to tell you how they deal with the pragmatics, why they engage experts, what issues present themselves. And then to the extent Dr. Rapp has encouraged me to welcome participation from the audience, which I'm going to do, but if I don't call on you, it doesn't mean that I don't like you, I don't think you have something intelligent to say. It's that I believe the panel is going to get to something, because of the work that we have done in advance, and I want the momentum to stay here.

But I do welcome people to raise your hands and please don't take offense if I don't immediately call on you. We also will reserve time at the end to open it to discussion or actual war stories that, no doubt, many of you in the audience have that will be germane and illuminating.

So if I may, Linda, you've been retained by the UAW to sue the drug manufacturers because their health and welfare fund has overpaid, and as part of your endeavor to represent your client, you're going to retain an economist.

I'm asking you if you could tell us to what end you retain the economist? How do you explore who you should retain? What issues immediately present themselves? What questions do you pose? And what's in the back of your mind as you undertake this retention?

MS. NUSSBAUM: In the hypothetical that Barbara has put out here, I guess there would be three stages of the litigation in which we would look at experts. And it might not only be economists. We might work with an expert chemist, a patent lawyer. We might work with a physician in a particular medical field who has experience in the field for which the pharmaceutical medication would be provided. So the first step is clearly drafting your complaint or doing an amended complaint or amended consolidated complaint. And at that point, we probably would be working with a medical doctor who probably would be working with a patent expert and just trying to understand the allegations in the complaint.

We ordinarily would then retain an economist at a point that we were getting transactional data in litigation. We were trying to understand the market, the market forces. If there was a delay in generic entry, what that delay was, and how much it cost the class that we represented.

So Barbara's question is: What efforts do we make? How do we vet the expert? How do we decide who to retain and at what point?

So the points for us are the inception of the action, drafting the complaint. Then ordinarily there is class certification, there is liability and there are damages. And different experts play different roles at each of these times.

I think what's really very important and what we spend a lot of time doing before we retain anybody is vetting the expert because you want to know that you have the right expert before you retain the person and not months later.

How do you determine whether you have the right expert? I think, first, you need to have multiple conversations with the expert. You need to make certain that they understand who you represent, what positions you intend to take, and what the case is about and if they have any discomfort with any of that.

For example, if an expert does not want to be adverse to the pharmaceutical industry, in your hypothetical, I need to know that sooner rather than later.

If the expert has ever worked for the pharmaceutical industry or that particular drug manufacturer, I need to know that.

If the expert is on the staff of the medical school where he feels that it will not be in his interest to be a plaintiff's expert, I need to know that.

And you also really need to read articles that the expert has authored or co-authored in that particular area so you know the positions that the expert is taking before. You need to make certain that your particular area is, in fact, an area where the person is now practicing or is really an expert and he's not just an expert in the general area. And then that you have a rapport with the person.

Once we decide to retain the expert, you then enter into confidentiality agreements, you start to get them documents in the case and you start to work with them further. If it's at the beginning stage, if it is drafting a pleading, you want to talk through, you want to make certain that you understand this particular area and the expert is really there for you as a resource. And frequently there will not be a testifying expert at any point in the case, but there is somebody there as a resource for the lawyers to help you understand what are we going to be asking for in discovery? What are the major issues that may arise here? How should I plead this particular issue? What kinds of documents do I need? What third parties may be out there who can be helpful to us?

You take it forward, really, from that step. That's really the process that we engage in.

MS. HART: Linda, is that your consulting expert or your testifying expert, and what tensions present themselves in that question?

MS. NUSSBAUM: Well, you know, I think that we use both consulting and testifying experts, and it really depends on the reason that you've retained the person. In the hypothetical that you gave again, I may use, initially, a consulting medical expert because I need to understand the medical issues involved, or I may use a consulting FDA expert or patent law expert to help me understand the underlying patent litigation because I'm not a patent lawyer and nobody in my firm is a patent lawyer.

We may not necessarily ever have to use these people as testifying experts and these may not be issues or elements that we are going to need to prove later on. But for us to effectively draft a pleading, for us to effectively figure out what the issues are, what we would need in discovery, what documents we would be asking for, we need to educate ourselves.

As you go further in the litigation, for class certification we are going to need a testifying expert and at that point, ordinarily, we would retain an economist, ordinarily somebody who is familiar with class certification, familiar with the issues in class certification.

If it's the hypothetical that you've given us, that is the type of class that has been brought before. It's the kind of case that's been brought before. So it's almost more routine. I know what the issues are, the expert knows what the issues are.

If it's a more unique case, there is a whole series of chemicals cases out there now, rubber chemicals, plastics and MMA and PMMA and it goes on and on, but there's a series of about eight different antitrust class actions against various manufacturers of chemicals.

In those cases, your economist may need to look much more closely at product markets, at whether or not particular chemicals are within the definition and within the product market, whether it's one product market or more than one product market.

So depending upon the case, your expert in class certification may need to look at more broad issues.

MS. HART: Dr. Rapp, you wanted to comment?

DR. RAPP: It just occurred to me in listening to you, Linda, that there was a part of the sequence of retaining an expert that you either skipped over or didn't get to yet, and it's worth bringing to the fore because it is such a weird part. And that is the point where you call an expert and almost the first words that get spoken and all of the words afterwards are misnomers. That's where you say, "I want you to do a conflict check." Or maybe that happens more often with Joel than it does with you.

But whenever I get a call from a lawyer about new business or my colleagues, almost the first words are, "Let me tell you the names of the parties so you can do a conflict check."

And then I say, "Okay, I'll do a conflict check right away and get back to you."

"And as I understand it," he said very carefully, because he's not a lawyer, "as I understand it, nothing that we are talking about there or very little or very infrequently has anything to do with a conflict of interest in the law."

Just to explain what I mean before we discuss it is, again, this is just my understanding—and I'll tell you at some point where my understanding comes from—that the law of conflicts or the case law involving conflicts of interest for experts is very, very drastically different from that involving lawyers.

Precisely because experts are not supposed to align themselves as advocates for a client, the rule, informally spoken, as I understand it, is that a conflict of interest caused by an expert arises only when there is a real danger that confidential information can be misused or passed where it should not go. The implication of which is that there is no potential conflict that can't be cured by a firewall between individuals and groups of people.

So this weird conversation that I was referring to really ought to go like this: "I want to give you the names of the parties so that you can check and see if maybe there's

a conflict of interest, but more likely, there is some kind of client relations problem. So that if your firm is working for an adverse party, my client is going to be upset about that. If somebody else in your firm is working against my client or somebody is going to get upset about that."

I just want to draw that distinction. Again, my understanding of that distinction between conflict of interest as economists and other experts ought to be using the word and the way that lawyers do when speaking about conflicts in their own ethical considerations.

MS. HART: And I think that that point is well taken. I think that Linda was approaching that topic with her remarks about asking about affiliations or of other employment by the drug manufacturers and that one delves into that with the economists. And we had a conversation about the rules of conflicts of interests for accountants. And it's comparable, as it is with experts, it is a much narrower, much different doctrine than it is for lawyers.

But I think also what Linda is getting to is a credibility issue. That is, attention on some of what else she has said, which is the amount of information that you share with your expert. If your expert is going to be a testifying expert, everything that they rely upon is discoverable generally. And so how much do you give them so that they are credible in terms of the foundation for what they are saying, and how much do you want to give them because maybe not all of it is helpful?

So I think that, in part, it is an issue of whether it will create a client relation issue for the expert or it will create a credibility issue for counsel as the deposition testimony comes out. And it seems there is the possibility of another agenda or affiliation.

DR. FRENCH: Just to add a little to what you've said. I think beyond making sure you're not working at cross purposes, like work your firm is working for the client in one case over here and now they want you to work for them in a different case where you'd be opposite the same client.

Other than real obvious conflicts like that, once you've established that those don't exist, I think the expert wants to know a little bit about the case, and what the issues are and the positions that you as an advocate are going to take, primarily, so that he can advise the attorney before he's even retained, especially if he's going to be a testifying expert. That he can advise the client if he's taken a position in other cases on similar issues in the past that the attorney may not know about, that may cause a problem or may not cause a problem.

If you're being a consulting expert only, that's not so significant, but if you're going to be a testifying expert, it is.

Like in the hypothetical that Barbara has raised and cases like that, I have often rendered an opinion on what the relevant market is. So if this were the hypothetical, first thing I would say to them is, if they are looking at me as a possible liability expert, is that I have rendered such an opinion, and is that kind of definition consistent with what you think you're going to have to argue or propose or hope to see in the course of the case.

MS. HART: Joel, let me frame it this way because I know you want to remark on the comments of the other panelists, but additionally, I would like you to share with the audience how—you announced that the arms race is on. So you are also going to, no doubt, go out and hire your own experts and, in particular, for the purposes of this discussion, you're the only economist. So what issues do you vet? Why are you obtaining that person? What are the goals and objectives and what ethical issues present themselves as you endeavor to do so?

MR. COHEN: Sure. Let me first address a point that seems obvious in retrospect. I agree with everything that's been said, and I don't think the fundamental issues are all that different on the plaintiff's side or the defense side. You both have to be worried about the same issues, credibility, conflicts, prior opinions that have been stated and whether they are going to help or hurt your client's cause.

One experience that I had years ago in trial brought home very clearly an issue that perhaps many of us don't think about. There are practical conflicts of the kind we have been talking about. Conflicts as in things in the background of the expert that aren't vetted because they are not the obvious questions. The obvious questions, we discuss. You know, have you written opinions that are fundamentally the opposite of what this party is hoping you can do with this case? Have you worked for adverse parties? Is the client going to be unhappy you were retained because, in the last case, you killed them. That sort of stuff.

But there are personal conflicts that arise. There was an expert testifying against us. We were representing a large financial institution in an Enron-related case. We should not have invested these large funds in Enron because we should have known it was a company about ready to fall apart. There were all these obvious red flags that made that clear to anybody who reads the *Wall Street Journal*. And certainly to an expert like him and we should have known that and followed those red flags and stopped pouring the client's money into the investment.

What he didn't tell the counsel that retained him or they didn't discover was that he had purchased for his own children's trust fund Enron stock. That he had identified very clearly 17 very interesting red flags that would tell any idiot in the world, "Don't buy Enron." And he had purchased stock for his children's college fund.

Now, to be fair to the other side, maybe it is something that never crossed their minds. How could the guy render an opinion like this when he had done that? It is incredible. Well, it came out literally for the first time in

the cross-examination drama. It was high drama in the courtroom, and it is something that we just assumed when we discovered it that we held back, didn't bring it up in depositions because we figured," Well, they must know about it. They are going to withdraw this guy and bring in another expert."

MS. HART: Ah, the sand bag.

MR. COHEN: I call it "strategic delay."

MS. HART: AKA sand bag.

MR. COHEN: I had no obligation to tell the other side that their expert had acted in a personal way that was directly contrary to the opinion he was giving. In any event, which is an interesting ethical issue.

MS. HART: Right, but you're sleeping at night. I get that.

MR. COHEN: But I think it is just an example of—everyone has these examples. There's the obvious questions that we sometimes may not think to ask of the expert.

DR. RAPP: What did the guy say, Joel?

MR. COHEN: Oh, he admitted it. He said, "Yes, I did."

I said, "Don't you think that's a bit of a conflict? How do you explain to this jury you just rendered this opinion and you bought stock like that for your children?"

We got the public records, subpoenaed records. His lawyers knew we had subpoenaed the records. It was extraordinary. They let him testify and didn't bring it out in the deposition.

AUDIENCE MEMBER: No, seriously, what public entity would have contents of a private trust fund?

MR. COHEN: No, his stock records. We subpoenaed them and they were turned over.

AUDIENCE MEMBER: Those are not public records.

MR. COHEN: They were available to public discovery. They turned them over. You would think they had looked at them as well and seen what stocks he bought.

MS. HART: Now, what's your first conversation with your economist as you're speaking with him and what do you also discuss with plaintiff's counsel about the rules of the road going forward in a litigation, about how you want to conduct the litigation?

MR. COHEN: I think, typically, my experience is we are seeing more and more stipulations that are removing—as the rules have changed, I think both sides realize that the ante has been upped and we are not happy with it. We don't want to be turning over every shred of paper in connection with our conversations with experts that we may retain or do retain. So you see, stipulations entered into of that sort refer to the status quo, what it was before some changes came into effect.

MS. HART: And we have provided some of the drafts of documents that reflect those stipulations as part of your materials. But, of course, you need to do your own homework.

Dr. Rapp, as you get the call from—I'm going to say typically defense counsel—when you would have received the call, what are the first things that you are concerned about in regard to the stipulations? What thoughts do you have about what's the most efficient way to conduct your discussions with counsel? That's what we are talking about. How does the economist effectively, candidly work with counsel and yet maintain its independence and its pedigree as a fact finder or an independent opinion?

DR. RAPP: I'll answer in two parts. Early in the conversation, in addition to the sorts of literal conflicts that I described before, comes a conversation not only about as much as can be disclosed to the potential client/lawyer about background, but also about an additional dimension, maybe part of what you were saying, and that is intellectual, let's call them conflicts. That is to say whether not merely have I testified that relevant markets are large in some relevant case, but also other aspects of possible ways in which my version of good economics conflicts with what your case might be, where you might need to find somebody else's version of good economics to do that. So call that the category of intellectual conflicts or issues beyond the others that we have discussed.

Having said that and then turning to the issue of attorney/client communication, which is the first aspect of the business of how eventual expert discovery is going to affect the relationship between us. If stipulations aren't mentioned early in the game, I and my colleagues at NERA will bring them up because it enables conversations to happen between us that otherwise—in an unconstrained way, that otherwise would not.

The point that arises out of this is that stipulations limiting the scope of expert discovery are nifty. But if they come late in the game and there is uncertainty beforehand, then you still got a screwed up channel of communication. You have people not writing when good research would call for writing. You've got attorney/client communications in a stilted form.

It's much better if the parties can agree to stipulations. That's very true. If the parties can agree early, that's better still from the standpoint of working things out.

That begs the question, which I'll return to you, of the difference between consulting economists and testifying economists, because the game is very different.

MS. HART: So Linda, would you like to address how you broach the topic with defense counsel about entering into such stipulations and what type of horse trading might go on into that? With that stipulation we can exchange drafts, counsel can have a frank conversation, there's back-and-forth between Linda and Dr. French, possibly, in our hypothetical, and they can have a frank exchange, drafts, modifications, and thoughts, and they can get to a more perfect opinion and none of that is discoverable. Or is it?

What happens to deposition testimony? What happens when you put Dr. French on in the Eastern District of Pennsylvania, he's on the stand? What can't Joel ask? Or how do you try to premeditate some of what the issues are?

MS. NUSSBAUM: I think the stipulations that we are talking about, just to be clear, and there are people who have not done them, a real concern arose because of case law and the rules where number one, conversation with counsel would be discoverable. So clearly you don't want to have a deposition of a plaintiff's lawyer where the defense lawyer is asking your expert for every phone call. Who first reached out to you? What exactly did they say? What's your best recollection of the next call? The next call?

So the first thing in our stipulation is that we'd like to shield on both sides reciprocally conversations with counsel.

MS. HART: That's because you're not Gary's lawyer.

MS. NUSSBAUM: Correct.

MS. HART: So she's not Gary's lawyer.

MS. NUSSBAUM: Those conversations would otherwise not be privileged. So when we are talking about stipulations here, I think that most stipulations have three forms. The first part being that those stipulations would shield conversations with counsel and people who work in counsel's office, so conversations with paralegals or perhaps other experts or other people that work within our office.

The second, which we try to do and cannot always achieve in stipulation, is shield conversations with other consultants. So if I have a testifying consultant and a no-testifying consultant in the same area, or in different areas and I want to have a conference call where we are brainstorming and everybody is saying their piece, we would like to be able to shield those conversations as well. Some stipulations, some defense counsel will agree to that as well. Some will not or will limit it only to conversations with counsel or people who directly work with counsel.

And then the third piece is drafts of the report. Because otherwise, drafts of the report would be discoverable. And somebody could literally go through the report line by line by line. Who changed that line and why? Was there an early draft? Wasn't there an early draft?

And before stipulations became, I think, pretty commonplace now, I really can't think of a case that I'm litigating right now where we don't have a stipulation in one form or another. Before that started to happen on a regular basis, you know, people were just incredibly creative in terms of how they dealt with their experts, so that they would not create a paper trail or did not want—

MS. HART: You think that's creative?

MS. NUSSBAUM: Well, I can remember taking an expert's deposition and the expert had been instructed by their counsel—nothing was ever written down. So some associate would be on the phone for three hours reading a draft report, and whenever he didn't like something he would tell the person on the phone. But there was never any draft. This 40-page report is the first draft and the final. And that's how people would deal with it.

So I think there's a little more integrity and honesty in the process now where we have these stipulations which clearly recognize that each side's experts frequently have various drafts that are discussed with counsel, and that that is not discoverable in a deposition.

Clearly, you want to deal with that issue. You want to enter into a stipulation as early as you can in the litigation because that will then govern the early conversations that you have with your expert and will govern the way that you interact early on with your expert.

MS. HART: Joel, I want to ask you something that I would like you to wrestle with a little bit: You're going to enter into one of these agreements that limits the discovery, but on the other hand you need for your expert to have a significant amount of information so that they can speak with knowledge, right? There's a tension of how much information might you provide to them. Is it simply the transaction data? Or do you involve your economist, give them knowledge?

Let's say there was an analysis done by the company on market erosion, and what they wanted to do, what plan they wanted to put in place in order to avoid market erosion, and what are their profitability analyses under scenario A v. scenario B.

Now, I could see that might pose a dilemma on how much information you want to share with your economist and then what kind of credibility issues that might present for your economist, as the plaintiff's lawyer said—because the plaintiff's lawyer will, no doubt, get those documents if such documents were to exist.

So what kind of dilemma do you face in terms of how much information is enough and how much is too much?

MR. COHEN: Well, this begs the question of another aspect of stipulations that you see. There is a difference in general under the rules of discoverability as they apply to experts as between data that's relied upon and data that's considered. And depending on which jurisdiction you're in—different ones in the federal system, different rules in different states—sometimes they conflict. And parties sometimes will enter into agreements that they are only required to turn over the data that was relied upon, not considered.

That begs another question: What the heck does that mean? Well, there is obviously case law that helps the lawyers determine what that means. But the answer to your question more broadly, my experience in my practice is you have to give your experts sufficient data so that when they are being cross-examined in a deposition/trial, their theses, their conclusions are being tested, they can credibly say, "I've looked at enough stuff to be able to say this."

That's sort of my litmus test. That may seem simplistic, but if someone is going to sit across the table from them and say, "Don't you think you should have looked at this? And don't you think you should have looked at this?" And that makes sense, if they should have looked at those two items, you have to give it to them in some fashion.

There are two ways to do it: Hand it to them directly, read it to them or have the associate read it to them. Or the other way is you can do it through consulting. Then the real question is whether it is something they relied upon or just considered.

Sometimes when you're able to enter into a stipulation that only determines what you relied upon, you were able to let them see it, it is not something they relied upon. It is something they considered and rejected.

MS. HART: And then it bears on their credibility and appropriateness of the rejection.

Dr. Rapp, I think you wanted to say something? Then I will elicit some comments. And then, Gary, I'm going to hit you with a tough question. So I want you on the edge of your seat.

DR. RAPP: All that I want to say is that, speaking for myself and not necessarily my colleagues, although I expect they operate the same way I do, there needs to be an agreement beforehand with counsel that says, "Whatever is in the discovery record, whatever you have turned over because plaintiffs think it might be worthwhile and part of their case, I get to see it."

And yes, there is a selection process where does that mean I send junior colleagues of mine into rooms full of boxes, or I give counsel a data request and ask them to fulfill that. But there is no circumstance in which I would testify in which I would—sorry let me start that sentence again.

If I am testifying, I want to be able to say, "I've been granted access to it all. And if you show me something that I can't remember seeing, then it's a memory lapse or something like that."

So a short answer that might serve in some, if not all, circumstances.

MS. HART: As I age, I begin to believe the "I don't remember" more and more.

AUDIENCE MEMBER: By data, are you referring to empirical measurements related to the testimony or are we also talking about what academic references the experts consulted?

MS. NUSSBAUM: What we are talking about really is both. What Dr. Rapp was talking about, which I think is an extremely important point, is that you always want your expert to be able to truthfully testify that they had access to and they got to see whatever they wanted in the record of the case. And sometimes that could be 30, 50 boxes and they may not think that that's all germane. But the experts should be able to see and consider whatever they think they need to see and consider, whatever was in the case, including answers to interrogatories, requests for admission documents, whatever it was.

But then in addition to that, if there are articles or government studies or things of that nature that the expert has relied upon, I mean, that also will then be disclosed as part of the expert report. So it's both.

MS. HART: And I think, as contingent lawyers, which typically I think one of the issues that isn't obvious, that as the expert wants to see more and more, the out-of-pocket expenses that we must pay, and I'm just going to touch on this later up front, there's a tension just on how much you want them to be willing to go on and see everything because they bill you by the hour, and it's a hard call to cost overhead.

So there's a slight issue from the plaintiff's lawyer's point of view on how broad you want the expert to go a-wandering.

AUDIENCE MEMBER: If your economist does a hundred runs, do you have to report all of the hundred or just one or two that you like?

MS. HART: I'm charged with repeating back your question to the audience, but unfortunately I didn't hear it.

DR. RAPP: I'll do it. If the economist is running an econometric model and does repeated runs, a hundred of them, is the obligation in discovery to turn over every single one of them, or not?

MS. HART: Well, I'd certainly want to elicit testimony about the ones that weren't produced.

MR. COHEN: This is not a satisfying answer but it depends on—obviously, if there's a stipulation in place that requires you turn over everything relied upon as opposed to considered, and depending upon which route you choose to take with your adversary counsel in the case, whether the hundred models is something they relied upon. The fact that they ran them does not necessarily mean you have to turn them over if they didn't rely upon them. If you're going under the considered standard, I would think, generally, yes, you're probably going to, at least, have to notify your adversary party of the existence of the hundred.

Maybe that's a way to do it. But the standard you use really doesn't matter because if you run a hundred and you realize none of them are reliable, you did something wrong, the data is wrong, what's the relevance of turning it over?

MS. HART: Gary?

DR. FRENCH: I think that, as experts, we would really like to have some stipulations that limit such discovery to some degree. In terms of both documents and in terms of our own work product, which regression runs would be, we're scientists. We are exploring. We are trying to find things out. If we have to constantly be concerned about some little something over here that the other side might be able to make some big hay out of even though we think it is rather insignificant, it really does constrain the intellectual process under which we operate.

So I think we can do better work and reach, ultimately, better and more solid conclusions if we don't have to be so concerned with that.

On the other hand, opposing lawyers, their job is to impeach the expert if they can, and so there is a tension there. Exactly where the line should be drawn, I'm not so sure.

MS. HART: Gary, I'm going to come back to you, but Bill?

AUDIENCE MEMBER: The last comments you made sparked a thought that I've been harboring in my mind as this conversation has been going on. If you look to the end game, that's cross-examining the expert, what do we want the grounds for cross-examination to really be? The merits of the opinion? Or sort of the atmosphere that can be used to impeach the credibility of the expert?

The communications with the lawyer, the drafts, what would the lawyer say in response to the drafts, did you show the lawyer the drafts, did the lawyer not like the draft? And if you can sort of—if the lawyer can treat the expert as nothing more than the malleable mouthpiece of the lawyer that hired him, the tendency is to discard the substance of the opinion without regard to the merit of the opinion. If the idea is to limit the discovery to the final work product and say, "Look, here it is, and here is everything I relied on. If there's a flaw in there, find it. If it's sound, then let it rest on its merits."

MR. COHEN: Use my example of the testifying witness who didn't disclose, until he had to, the Enron purchase. I think the answer to your question is that—this may seem a bit tricky answer: You want the other side's witnesses, you want to be able to focus your cross-examination on the adversary's witnesses, hopefully on those external factors. The reason is because if you have something good to work with on cross-examination that undercuts their credibility, then they haven't done as good a job in picking the best expert as they could.

It isn't a matter of what's desired. If you want to try to design a desirable judicial system, I do think credibility matters. Using that as an example, that mattered. That should matter to a finder-of-fact to turn that over.

Now, there are other issues. He said, she said, he said. Who called whom first? What did the lawyers say? That can sometimes get carried away. But I think the general rule of good trial practice, good deposition practice will overcome that. If you waste too much time asking those silly questions and they don't lead to anything meaningful like the occasional softball with the Enron purchase—you know, the finders-of-fact, they're not stupid, whether it is a jury or judge. They see you're focusing on the inconsequential issues. So it is a bad tactic as a trial lawyer.

MS. NUSSBAUM: You can also get to the atmosphere in another way. The experts need to disclose what other matters within a period of years they were an expert in. Literally, if you want to show some bias that this expert is the house expert. I mean, we got an opinion from an economist in a price-fixing case a few weeks ago, and it turned out the person had first worked, actually, for that law firm, went to school around that firm and has basically been an expert 25 times in cases where firm X is the defense lawyer.

So that kind of thing, without asking him for the 20 drafts, you know, we certainly were allowed to cite the fact that there was a very good stipulation to go through all of that. That everything that—you've never found a plaintiff's case that you've testified where each and every time this is who you're testifying for, or you look at things that the expert has written. I think it's very important to get every article that could possibly be related and look at positions, at academic papers in other ways, other positions that the person has taken. Are they now taking a totally different position? And if so, why? If they are in a group have some of their colleagues written something that's totally opposite to what they are testifying to?

So I think there are ways of getting to bias and whether or not this expert is the mouthpiece of the lawyer without having to examine them about discussions that they've had with the lawyers specifically, or how many drafts or how many runs they did specifically.

AUDIENCE MEMBER: If you have deeper pockets and you're in "All Things Considered" jurisdiction, can you run into ethical problems for encouraging your expert to consider several orders of magnitude, more data than he actually needs to arrive at his opinion for the purpose of shipping a couple of 18-wheelers worth of discovery to the other side?

MS. HART: I've never had such pockets. I think that only Joel could address that.

MR. COHEN: I'm not going to comment on how deep the pockets are.

MS. HART: Gary, you're dealing with contingent lawyers, typically, who are very cost-conscious. We might encourage you to employ the talents of your junior colleagues. What are the tensions in terms of your own credibility without being able to testify to the way in which the work was performed? How much information do you really want to have? And is there really any benefit from distancing yourself from the hands-on work and what flows from that as you delegate the work in order to respond to my economic needs to keep my costs down?

DR. FRENCH: Well, that's several questions in one. Let's see if I can answer them.

In terms of using more junior staff than myself on a case where I'm the testifying witness, the key is the communication I and the staff have, and how frequent it is, and that the direction at what they are doing and how they are going about doing it comes from me. And in our firm, I think we are able to do that so that the bulk of the hours on a given case probably are not the testifying witness' hours. They are other people's hours, but nevertheless the witness is in charge and he's directing the activities and the research and analysis. And the staff needs to be given directions such as, "If you find out about anything, come back to see me about it. Don't guess. Don't make a judgment of your own. Bring it back to the witness to at least be privy to it." So I think that's how we handle that part.

It is true, not so much how much money the plaintiffs have, but more of a problem that I find is schedules imposed by the courts that none of us can necessarily control that put real-time crunches on things and force you to have to be more selective in what you're looking at and dealing with than you would like. But you have to do it.

So I think it's important that the whole team, then, be conscious that the expert needs to see the right kinds of things. And if there are things in the records that are pertinent—I don't care if they are pertinent to the other side more than the side you're working for—I think the attorneys have an obligation to make sure that the experts see those particular documents and information. And of course, you don't want us blindsided at a deposition anyway. So of course, you'd want to do that.

But sometimes we can do that, and if you work together and the idea is to try to make sure that the expert has everything that's pertinent or relevant to the issues he's doing, that the whole team knows what is in the record, then I think you're in pretty good shape.

But in a lot of cases there's a lot of documents or information that is really of no relevance or pertinence to the issues I'm dealing with. So I don't think there's a need for me to necessarily see everything that's been produced in a case. So I think it is fair to rely on counsel to some extent to do some sort of jiggle, screening of what might be relevant as long as they are not doing it in a way that would cause you to skew your opinion, if you will, about what you think about things.

MS. HART: Dr. Rapp?

DR. RAPP: Just a quick gloss on what Gary said, if I may.

The right way to think about economics is the way Gary mentioned in a previous question. Economics is a science. *Daubert*, before the later case law started extending gatekeeper tests to other disciplines besides scientific disciplines, has good descriptions of the way science works. And those apply very well to economists' work in antitrust cases. *Daubert* is the right standard.

I mention that as a precursor to observing that the use of junior colleagues as part of a research team is the way science routinely works. And there should be nothing surprising about the fact that senior team members, testifying ones in this case, rely sometimes heavily on others.

That doesn't mean, however, that there are no dangers in it. The danger is the over-leveraged expert, somebody who is spread so thin that he or she is too much removed from the data that will make that person, in the end, a "weak witness." And that, I think, is the principal tactical worry that trial lawyers have when they observe almost necessarily senior economists working with teams.

MS. HART: Which also interplays with credibility. If you're spread too thin, how familiar can you really be with the facts and how much have you grappled with the specifics as to which you are opining?

DR. RAPP: Exactly.

MS. HART: So I think the interplay on ethics and credibility is quite close.

Linda, as we go towards class certification, your comments so far, I feel, have kind of captured the economists addressing market definition, and the economic analysis of what the ramifications of the conduct are.

As we go into class certification, what is the mission for the economists and what might you hope to be able to get the economists to establish for the court in his or her report?

MS. NUSSBAUM: Well, clearly, in this kind of case, you know, and in the hypothetical that you gave to us, the most important thing is that damages here can be proved on a class-wide basis, so that there are not going to be differences between class members that would be so great that the damages could not be proved on a class-wide basis. Of course, there are always going to be small individual issues, but those individual issues are things that we would argue could be dealt with in a process that, at the end of the day, when one is determining the particular amount of damages that any particular class member has suffered, but whether or not damages as a whole are subject to an overcharge, for example, which on a class-wide basis one can argue that everybody was overcharged and the overcharge was X.

And therefore, whether somebody bought a thousand dollars of these widgets or of this pharmaceutical product or $10 worth, it really doesn't make a difference because everybody has been overcharged in the same way on a class-wide basis. At the end, one can have a claims administrator through the administration process determine any small differences that there might be—if somebody bought in a different period of time, or somebody only bought the brand name product and not the generics, or somebody bought the generic product and the brand name product.

Those are issues that can be dealt with later on in claims administration, but that for purpose of class certification, you want to be able to argue that damages here are on a class-wide basis.

In the pharmaceutical area, now—and even in other areas—you're having arguments made that damages are not on a class-wide basis, that there's a difference in the class members so that large class members perhaps might be better off using a loss-profit analysis and other class members might be better off using an overcharge analysis.

So those are also the kinds of issues, depending upon the case, that you're going to need your expert to give their opinion on. That's really critical, the most critical part, actually, of the class certification process. So that is something that you start dealing with your experts very early on, and you want to get the transactional data and you want to have your expert analyze that very closely because, if you can't persuade a court that the damages can be determined on the class-wide basis, you're never going to get a class certified.

MS. HART: And Gary—because it's my job to try to unearth the ethical issues, that's what we are trying to get to—so is it your job, Gary, just to make it look easy and do-able? Is it just a prima facie showing that yes, class-wide damages can be established and therefore you want to reach that opinion? And how do you come to grips with the complexities that may really present themselves? And how much do you have to wrestle with that?

DR. FRENCH: Well, it seems to vary some from jurisdiction to jurisdiction exactly what's required of the expert in showing, for example, that there is a feasible methodology for calculating class-wide damages. The biggest controversy, to me, is whether the formula has to apply to each member of the class separately or if it is an aggregate formula where you arrive at the aggregate class-wide damages even though it may not apply to each individual member. But those are questions that I look to the lawyers to guide me on in a given case, what's the case law and how should I approach it?

I think in this day and age at least, I think the plaintiff's burden is greater than it used to be. The expert has to have something fairly concrete. He can't just say, "Oh, well, there's a but-for price, and there's an actual price, and the difference is the overcharge, and you multiply it times the number sold, and that's it."

You have to do more than that certainly at this point in time. You have to indicate how you're going to get what that but-for price is. And is there data and information to do so? And so you have to go pretty far down the road. In fact, by the time you go through about three rounds of briefings, sometimes you've practically done the merit case at the class certification stage.

MS. HART: This is through regression analysis?

DR. FRENCH: Could be, yes. Often we use regression analysis, especially in price-fixing cases. Sometimes it is not regression analysis. A lot of times there is not sufficient data and information to develop and use an econometric model and you have to have something less rigorous than that. The court doesn't have the luxury of not having an answer and the expert has to find an answer if he possibly, at all, can. As long as it is not arrived at in an unscientific or unprofessional way.

MS. HART: So Joel, let's say the brand name manufacturer paid off the generic manufacturer—or entered into an agreement with the generic manufacturer that did elevate prices. Is it sufficient for the defense attorney simply to say, "But you can't establish class-wide damage." Is that your job and is that what you endeavor to engage them to demonstrate, with the engagement of an economist, that it is just too complex? Where does the interplay

between the merits—not that those merits are true, but let's say hypothetically those merits are true—but where is the interplay between the merits and grappling with whether the answer should be that, but it can't be done on a class-wide basis? How do you wrestle with what your mission is in serving your client and how you're going to employ the work of an economist?

MR. COHEN: You're speaking from an ethical perspective?

MS. HART: From an ethical perspective.

MR. COHEN: Well, I actually don't see any ethical issue here at all. Let's assume that that's true that that happened, this illicit conduct occurred. Unfortunately, it is almost never clear, even to the party representing the adverse interest, what really happened because you just don't know, although you often have inclinations one way or another. But that's irrelevant. Our ethical obligations as lawyers are often at odds, but not always at odds with our obligation to act zealously for our client's interests. They are only at odds when you reach these streams. You have to push it to the line but never push it over. It's where the line is drawn, that's where the rubber meets the road. No pun intended to the rubber case.

So maybe this doesn't answer your question, but it is the only way I can answer it. My obligation is to find an expert that can most credibly counter what my adversary's expert is going to say.

Now, the class issues, more specifically, the law has changed and is evolving with respect to classification. Many of you are familiar with the decision in the IPO. That may be heard in May, but that may act as a bellwether. Some people say it is a bellwether change in the evidence that needs to be proven to a court in order to certify a class. Others say it is not, it is just calling up other cases and making clear what the Second Circuit always intended.

Regardless, it is a big change. You can say, on the one hand, you only have to find an expert that can meet the prima facie showing.

On my end, I'm trying to find an expert that can credibly say it. My ethical obligation is to find someone that can represent my client's position and the finder-of-fact will figure out the rest.

MS. HART: The truth we are dealing with is not the merits of the conduct, or whether or not the conduct occurred. It is whether or not we can ascertain class-wide damages in this instance, right? So we are segregating the merits of culpable conduct or intent from whether or not the class can be certified. The merits affect the class outcome, but the issue is: If there is culpable conduct, a denial of class certification is essentially a death knell for any recovery for the class. And that's not, that's an ethical outcome if there was culpable conduct, at least from my point of view.

Dr. Rapp, as you're retained to assist Joel in his defense and his efforts to challenge the ascertainability of class-wide damages, there's some view that you—not you, personally, but you in the generic sense—are retained to say similarly to say, "A-ha, it's way too complex and cannot be done." Is that ethical to stop there, or could it be you might have to entertain whether it just isn't done yet, and whether Gary just hasn't polished the stone sufficiently, and that if you address this or that, "A-ha, it could be done." How do you view your charter?

DR. RAPP: I see about 17 different questions in there. I'll try and pick out a couple.

Viewed most narrowly, taking your question most narrowly, I think that typically my focus in class certification is on the subject of the misdefinition of the class, not on the issue that damages are complex or that the methodology hasn't been fully specified, because I don't think—and here I am parroting what lawyers have told me—I don't think judges are much persuaded by the notion that damages are too complex to evaluate when the time comes in the damages phase of the case. And I think that the real issue, which travels under the rubric "impact," that is, as fact of damages in class certification, is whether or not it is possible to show that there are sizable, non-trivial members of the class who are unaffected by the complained-of action.

And what that really goes to, is if you or Linda have gone too far in making, creating a big class for the sake of numerosity and eventually the size of the award that will take place, and the danger that you face—tell me if I have this right because this is surmise on my part—the danger you face, if you've done that and the judge sees that or rules that way, then it is game over. Whereas, an alternative, if I'm correct, is to begin with an unexceptionable class, a class that leaves me having to say to Joel, "Sorry, they did this in such a way that I don't have an impact story here, so let's just talk about how complex the damage methodology is." In which case, most of the time, you win.

MS. HART: If only.

Linda, as you grapple with trying to put this report together, how much do you think that the merits bear on the court's analysis and how much do you want that to be presented by your expert?

MS. NUSSBAUM: Well, two things, just one minute to just comment. I think that was an excellent comment that you made and I think that's really the most recent case, the points that you raised, really intraclass conflicts,

whether or not the class, as defined, is just too large, and whether some people actually benefited by the alleged wrongful conduct, some people did not benefit, some people would have benefited under a different set of circumstances. I think that in a more sophisticated class, really the argument that is coming more and more and being focused on more and more. Particularly, this is a pharmaceutical hypothetical again. In the pharmaceutical area where there are all sorts of issues with respect to downstream data, whether or not people benefited, whether or not there is more profit to be made in selling brand-name drugs as opposed to generic drugs, issues of assignment. So you're correct that it is, I think, what the defense lawyers are really focusing on now and the class lawyers clearly believe, and I believe strongly that that's really a red herring issue, and that any of those somewhat differences—that they really are not intraclass conflicts. Those "conflicts" are never being raised by the large class members, or never having the large class members opting out because they're saying, "We don't think the class lawyers are adequately representing us." But rather, these are issues always being raised by the defense lawyers.

But be that as it may, now to Barbara's point on the merits of the case. You know, I think it's important always to present your case as a meritorious case. You never want a judge to feel that you're wasting the judge's time. You want to use every opportunity that you can to highlight the wrongful conduct of the defendant, and to then show how that conduct caused this damage on a class-wide basis. So I think it's important, number one, for your expert to have some understanding not only of what the transactional data was like in the case, but what the case is about and what's being alleged. And it's also just very important for the court to understand that in court where your expert is not going to understand issues of the relevant market, of whether or not there's more than one product in that market, how that market was affected if you're not also really going to the merits of the case, that is, what happened here, and to the extent that you can also know why. So I just feel that that's very, very important and something that should be done in every class certification.

MS. HART: Gary, does that cause you to become an advocate?

DR. FRENCH: Which causes me to become an advocate?

MS. HART: Well, essentially if you recite Linda's --

DR. FRENCH: My answer is: Nothing causes me to become an advocate.

MS. HART: There you go. Now you know the answer.

Well, if Linda wants you to essentially adopt her view of the merits, so you do a recitation of the facts—as would I, I'm not certainly pointing the finger at Linda. I want you to adopt my view of the facts and the ramifications of the facts as I see it, and then you are going to opine on class-wide impact and the ascertainability of class-wide damage. Have you now become an advocate for the validity of the merits as we see it?

DR. FRENCH: I don't think so. I think that it's appropriate at the class certification stage for the plaintiff's expert to assume that the liability allegations are true. And then if they are true, what is the impact or what was the impact on the class? And how would you go about examining it and demonstrating that? And then how would you calculate damages to the class?

However, it's not quite that simple because, when you get into it sometimes and you're looking at how you might do it, it might have some implications about what the original applications are and their validity. So sometimes there has to be some back and forth on that. But to start out with the presumption at the class cert stage, I think, is appropriate for a plaintiff's expert to do without being an advocate.

MS. HART: Joel?

MR. COHEN: I don't have any problem with that. That's an assumption. What's the old joke about economists? They assume a hole in something and then there's a hole there. Forgetting it is a joke, that's what scientists do: They have to draw something, draw assumption. As long as it is clear that it is just an assumption. They're not testifying as to whether the conduct occurred. Of course, they can do that. It is the only meaningful way they can play a role in the meaningful adjudication of the issues.

MS. HART: So Dr. Rapp, do you endeavor to explore the issue of whether or not there's class-wide impact? Do you assume the truth of the plaintiff's allegations in regard to conspiracy or anticompetitive conduct?

DR. RAPP: The answer is: Not necessarily. Let me give you an example, and it's an example that has to do with this issue of class size that I mentioned before and it is a simpler one in a rather complicated issue of forestalling generic entry.

Suppose that there has been a government investigation of price fixing, and what the government investigation has turned up is the fact that—just making up a story—that three sales managers in the Southwest decided to talk to their equivalents at competitors and allocate customers that amounted to a relatively small fraction of national sales in whatever this product is. You can go to jail for that, and presumably somebody might, and it's a genuine price-fixing conspiracy.

It matters to me whether the record shows that that was the conspiracy if the allegation that I read in the plaintiff's complaint is that there was an all-encompassing, nation-wide agreement to restrict output and fix prices. Those are both Sherman Act Section 1 violations. They are very different. Don't ask me to assume the latter if there is a trial record, criminal trial record that sets that forth the former, limited-scope collusion.

MS. HART: Well, you could conceivably take it one step further. The plaintiff's lawyers could adopt a regional price-fixing and you could even analyze, consider the data and find that it was ineffectual, for instance, right? Conceivably, the data would reflect that the effort at conspiracy was not adhered to.

DR. RAPP: I mean, I wouldn't rule that out completely, but let's put it this way: The risk that I and counsel who retained me run in that circumstance is that the judge will say, "This is merits stuff."

You're looking at things that, first of all, have they even come into the record? I'm uncertain about that, and I think I would take some—I'd be cautious about making assumptions contrary to the allegations unless they were close to being a factual certain. I'm not as confident in that answer. It is a hard question, Barbara.

MS. HART: Good. I'm going to stick with the hard questions, though: If, under the pharmaceutical scenario, let's say you could adopt the conduct, might you also attack it by suggesting that certain purchasers in the market had such buying power or such ability to negotiate that, again, there wasn't class-wide damage essentially negating an impact but also kind of challenging whether or not the conspiracy itself could have been effective?

DR. RAPP: Let me say that I would be willing to consider it, yes, even though it runs squarely into merits, and there are risks in that strategy. If a reading of the record that's available to me at this early stage in the proceedings presumably tells me that there is no impact, either to the class in whole or in part, because of facts that an economist can process in what is, to me, a straightforward way, then the answer is that I would be remiss in not saying that to the court, right? I want my testimony about impact to contain as much real information as possible. The issue is: How far am I allowed to go by the rules of the game?

MS. HART: Joel, would you like to comment?

MR. COHEN: One thing you have to think about is the flip side of this. Generally, I think it goes one way. When an expert is called for any particular purpose, that doesn't allow the adversary to make them their expert completely unrelated to that purpose. But you can ask questions related to that purpose that that proponent of that witness didn't want to ask because it wasn't their witness. Arguably, if you don't touch upon this and then I get up and cross-examine and induce it from your expert, how is it going to come out there? Is it better to come out through you or through me? There are tactical situations as well.

MS. HART: Would you be suggesting that I would ask Gary about the issue because I want to be able to logic this through, but that I'd be asking Gary to wrestle with the issue that we have large purchasers with negotiating power and what ramifications that has for class-wide impact, and I want him to essentially inoculate against Dr. Rapp's challenge there couldn't be class-wide impact?

Gary, as you engage in the reality that certain purchasers do have negotiating power, what is it you want to know or how might you address that? The possibility that that's true? That all class members are not situated in a way in which they are injured?

DR. FRENCH: When I start out, I may be assuming the allegations made by the plaintiffs are true, but as I said a moment ago, I start doing some actual research and analysis in the marketplace. If I find along the way that some class members or category class members, where it doesn't appear they were affected for either bargaining power or they are in a strange marketing channel that the conspiracy just didn't reach, something like that, I usually try to bring that to the attention of the attorneys and suggest a class definition modification before Dr. Rapp points it out, if I can.

So that's what I mean, that sometimes the work you're doing, once you start down the path of trying to look at impact and methodologies for damages, class-wide damages, sometimes it leads you to something that is contrary to what the allegations you started out assuming are. I think when that happens, you have to deal with it. You can't just ignore it. The defense side is not going to ignore it. So I mean you have to deal with it in some fashion.

MS. HART: For that inconvenient truth, we'll assume that my cell phone went dead and not that I hung up on you.

So then you and I have come to a tension in our working relationship where you are suggesting that I have to possibly redefine the class and also be able to articulate a class that's now ascertainable. Because if I try to put a class before the court that is something obtuse like those class members are those without bargaining power, that's a non-ascertainable class that Gary has now inconveniently caused me to wrestle with; how do I articulate that? And I'm sure, with the benefit of Bernie's input, I could come up with something.

Yes?

AUDIENCE MEMBER: How would you handle a situation where you've been working with your expert, you're very pleased with your expert, you're approaching trial. For the first time, because you haven't worked with this expert before, you discover that the person is just generally incapable of performing on the stand as an appropriate actor and presenter of his own ideas. So you have an expert and your jury expert comes in and says, "My God! He's talking in a different language and all of our mock jurors hate and despise the guy with a passion."

Would you switch experts at the last minute and try to have someone else pick up the file where the first expert left off and use him for the presentation? Or to what degree could you coach the expert with how to perform on the stand?

MS. HART: Joel?

MR. COHEN: Well, I would like to say I'd never be in that situation. And by and large, wouldn't.

One of the very first things I do when I deal with an expert in any realm, first of all, I speak to my colleagues. I speak to the consulting firms, the other firms that we use—there are no other firms, excuse me. But you speak to your consulting experts you have a relationship with, you know. It is something I try to avoid and I'm in a case now with an expert who is technically wonderful. He is a non-U.S. expert and he is a horribly inefficient and laborious explainer of his ideas. He is going to be a horrible witness. I'm not using him. Other counsel may want to use him. I already know I can't call this guy. It doesn't matter how well you write it. If you can't communicate it to six jurors whose education level may range from Ph.D. to sixth grade—to answer your question: If that happens, what do you do?

You back up, you were on vacation when your colleagues picked the guy who can't talk his way out of a paper bag. You have to weigh the advantages and disadvantages. You're stuck in a bad situation. The question is: Is switching horses that late in the horse race going to be more harmful than helpful? Triage is what you do.

MS. HART: As you undertake that triage, your new testifying expert has to come up to speed sufficiently to be credible once you put them on the stand so you have a dilemma of reinventing the wheel.

MR. COHEN: Well, in big cases sometimes you have experts whose expertise and experience and work overlap somewhat, so you're able to accommodate both for the expert—never this bad a paradigm in my experience. The witness is just horrible. But sometimes you'll have one who is better than the other who's testifying, and you'll have in mind that's the one who will testify. But they can overlap.

MS. NUSSBAUM: You know, I think also it is unlikely that's going to happen because your expert will have been deposed. So you'll see ordinarily how somebody handled themselves in the deposition. And ordinarily before you even get that far, when you're seriously considering somebody as a testifying expert, you meet with them. Your co-counsel meets with them. You do a give-and-take. The likelihood of that happening, but then I think the point you make is a very good one. Frequently, if you have overlapping experts and you want people to have some things in their report that are just kind of door openers, they are not now relying totally on X issue, but want to kind of put in enough general language to leave the door open, so that if that kind of emergency happens or suddenly some other issues come up that you hadn't been contemplating, you can then have your expert opine at a later date further or on some additional issue. And that might be a way to do it.

Can I just comment on one thing that Gary raised before? That is the dilemma of what happens if your expert comes up with something that's not helpful for the class definition that you allege. As a practical matter, you know, when you're figuring out what your class definition is early on, when you are writing your first pleading, the complaint or the amended consolidated complaint, at that point you frequently have had little to no discovery. You frequently have not had transactional data. So very often, what you allege as the class period will change. That changes frequently, even during the process on the motion for class certification, and so it is important that you have that give-and-take with your expert and your expert may tell you, "People, early on in the class period, may not have been damaged or people later on may not have been damaged." You really need to listen to that. Your expert needs to tell you that because, clearly, you want to define the appropriate class because your adversary is going to tell you that.

MS. HART: Linda, can we make sure we cover the fundamentals. As contingent litigators, what's the payment arrangement that you have with your experts? What are the ethics in regards to what the record needs to look like?

MS. NUSSBAUM: Well, your expert is not contingent, although you as a lawyer may be contingent. Your expert gets paid on an hourly basis, ordinarily the same amount as defense firms pay their experts, and they get paid as they send in their bills. Their payment is not at all linked to success in a litigation, your success in a litigation or the fees that you may get in a litigation or anything else. You know, clearly, in complex class actions you need to use a caliber of experts that are as sophisticated and as well-known as experts being used by the defense firms. So ordinarily you're paying the same amounts to the same caliber experts, and frequently we are using experts that

are sometimes plaintiff's experts and sometimes defense experts, depending upon the situation.

MS. HART: Joel, what's good for the goose is good for the gander there, right? You can't have performance bonus that, if Dr. Rapp really kicks our butt, he does incrementally better?

MR. COHEN: No, of course not. You can't have contingency. There are these creative value-building approaches that somehow are used that, depending how they are structured, could run afoul to contingency.

MS. HART: Was this a value-added idea?

MR. COHEN: There are these notes of value building which may or may not be a euphemism for contingency. You're not going to be paid on an hourly basis. You're going to be paid on a daily basis. It is a measure of the amount of work you're doing. It doesn't bear relation to the outcome of the case. It is not contingency.

Where it becomes an issue, not ethical, but this sort of house expert. This runs equally true on both sides. You use the same expert time and again on similar cases and they are subject to the obvious cross-examination that you know, "Isn't it true you made $900,000 last year and $850,000 came from this law firm," all the connections that you see. In effect, it appears to be contingency because isn't it true you've won most of your cases? It looks like contingency, and we do have to be wary of that.

MS. HART: So what you're saying that comes out there is the appearance that they are beholden to the counsel that's retaining them, generally? Is that an appearance issue?

MR. COHEN: Well, it becomes a reality issue to the outcome of some cases. I don't know what judges think of this. I've never asked a judge. You know, I tend to think the judges see through that. That isn't what really matters. What matters is their opinion.

But judges are human beings too, and at some point, I'm thinking in particular of an expert witness we cross-examined at trial a couple of years ago. It was just that situation. He had a hefty income. He was a professor of economics at a well-known university, but five times his income as an academic came from being a consultant. It almost all came from one law firm, two or three cases. It didn't look good. At some point, it probably would have been a good decision to switch horses, even though he may have been perfectly competent, but it undercut his credibility.

MS. HART: But doesn't this also play out, Dr. Rapp, where the question gets presented—and I have no idea how you'll answer this—but have you ever seen a case where class-wide impact could be established and the issue of whether you'd ever acknowledge that a class treatment and whether then you're essentially saying the class action device is just an unworkable device or a concept because you could never actually ascertain class-wide damages?

DR. RAPP: I think that's a fair cross-examination question. I think its impact is on credibility and things like that is not likely to be large.

But the inference doesn't follow. In other words, if it turns out, just using myself as an example at hand, that in class certification matters, I've been hired mainly by defense attorneys, it doesn't mean that I think that—and that I have testified for them, meaning that my opinions were consistent with what they wanted to hear, it doesn't mean that I regard the system as unworkable. It doesn't mean that, if you called me up, I wouldn't work for you too. There's no real inference to be drawn. And as somebody who is accustomed to answering deposition questions or cross-examination questions, I think you can lessen the impact of that. When I work for plaintiffs all the time in this particular setting, it hasn't happened. So what?

MS. HART: And Gary, have you ever seen a class that couldn't be certified?

DR. FRENCH: Of course not, no.

The problem is in most of the class actions that I've been in I've been on the plaintiff's side and the class got certified. But what that record doesn't reveal is a number of cases that I was on I could not support common impact or find a damage methodology. So I wound up not being the testifying expert anymore. So I mean, if you get to the point where you're not going to be able to support your party's side of the case, you wind up not being their testifying expert. So of course, the ones that you're in you wound up being able to support it or you wouldn't be in it at that point in the case.

So yes, I've seen cases that I don't think can be certified, and I've had to tell some clients to that effect, even though neither of us were happy about that turn of events, but it nevertheless has to happen. Plus, I have testified in a case on the defense side where I didn't think it should be certified so. But most often I work for plaintiffs.

MS. HART: And Linda, under the situation with you're going to change horses and Gary is going to be your consulting expert, I think that presents a lot of issues in terms of going forward. How should we wrestle with that issue in terms of the findings that he's made? We would certainly Chinese Wall him from any future experts so that his conclusions are not discoverable at a minimum, and during the conversations with our new expert, I mean, we have got a real financial dilemma on our hands because we have to go forward with the case on a contingency basis—and it hasn't happened to you or me,

so this is all hypothetical—but our former expert is now having issues with whether or not the class-wide impact can be established, and we need to redouble our efforts for our UAW client.

MS. NUSSBAUM: I think that there are two things that then have to occur. Number one, if this is an expert who you had vetted properly and then you value their judgment, you really, first, need to understand what the issue is, and is there a way of either changing the class or changing the definition of the class or reframing some aspect of the case? You would clearly need to understand what the problem is here. Is the problem that there was not a big difference in price between the generic and the brand name? Is the problem that you're a third-party payor, that the copay here, that this drug was so cheap that the typical person's copay would be higher and therefore they weren't impacted?

So I think in a vacuum it's hard to deal with, but you really do need to, in any litigation—I think litigation is a living, breathing creature—you need to be constantly rethinking and re-analyzing and relooking at the facts as they present themselves and figuring out, okay, why in this particular situation—would this not be common impact? What is there here that's different? What is there here that we didn't understand initially? And then how to grapple with it.

Clearly, getting the second expert and having to deal with that expert is, from my perspective, almost the side show, the secondary issue. The first issue is an understanding of what the problem is, and then figuring out how can one deal with this problem. And maybe you did define the class too broadly in this particular case, and maybe there is some factual anomaly here, and because of that, the class should be defined differently.

Once that has been thought through and vetted with Gary and with others, you kind of come backwards and say, okay, this was the problem, this is how we're dealing with it. I think that you then would clearly probably go to another expert, start the procedure again from the beginning. But it would be something that you had already thought through and you would clearly present what the issue was, and what resolution you came to because you certainly don't want to repeat the same process with another expert.

If there was a fundamental problem with how you envisioned the case to start with, my view is that the defense expert is going to come up and says—well, so you're thanking Gary that he saw it sooner rather than later.

AUDIENCE MEMBER: At that point, would it be ethical, would it be biased to make a decision if the real problem with the class impact, for example, was three analytical documents that were found in various documents. In order to get your second testifying expert comfortable at the class certification stage with the class as an idea, would you consider not showing that expert that information?

MS. NUSSBAUM: No, because that to me—I mean, if there was a problem in the way we envision how to define this class initially and Gary had gone through that with me and he's persuaded me, I now see his issue, and I now see that there's a problem. And maybe, taking Barbara's hypothetical again, this is a third-party payor, and maybe because of the price of this drug, because of the nature of this drug, not everybody was damaged, let us think or something, you know, there is some difference here something that we did not see initially, then you need to think that through and plead around it. It's not a solution to say, "I'm not going to ship this box of documents to the next expert," because even if I were to choose not to do that, I mean first of all, we all would have to say to our experts, what do you want? What category of documents? This is what we think, but clearly there is a give and take. What kinds of documents are you going to need to see here? He's going to ship those to his expert. So on cross-examination it does me no good to have an opinion that I'm in love with and there are a million holes shot through.

DR. RAPP: I have to ask you, is there an assumption that Gary's conclusion of the class is incorrectly defined, is wrong?

MS. NUSSBAUM: Not necessarily. That's the next step in the process. Gary then says, "I think you have a problem here. This is not the situation that you thought. I've now analyzed the prices, I've analyzed the transaction data, I've analyzed whatever—"

DR. RAPP: If you agree with him, you read his analysis and do your own and you say the guy is right, what do you do then?

MS. NUSSBAUM: It is really a fact and circumstances, what do you do then? I think you need to rethink at that point, and frequently—I don't know what percentage, but it is not rare—I think frequently the definition of a class does change during the course of the litigation.

DR. RAPP: That's great. And that's the ethical answer, isn't it?

MS. NUSSBAUM: Yeah, and clearly what you know a year or two years down the line is not what you knew when you started it. And circumstances change and the markets change and things continue to be sold and you're no longer in a hypothetical world, but now you're getting real data. So you need to consider all of that.

MR. COHEN: I'm going to defend my colleague at the bar.

MS. HART: I think she did a fine job of defending herself.

MR. COHEN: Not that she needs it. She's right, you know, it's not a matter of ethics if you bring a case, whether you're on the plaintiff side or defendant side, and the facts suddenly cut against you and it looks like a less-good case. Obviously there is some point in the inquiry where there are rules that exist. There was Rule 11, where at some point if your case becomes frivolous, then, yes, you shouldn't be forwarding that case. Whether it is unethical, sort of doesn't matter because there is something near and dear to your heart, which is your license and the fees you're going to have to pay.

We had this in the Enron case and a well-known class action lawyer was found to have pushed the case beyond and there was a provision in the securities laws that allowed him to get Rule 11 sanctions. It happens.

My view of ethics is that—years ago, I did teach ethics, believe it or not, you find that shocking that a defense lawyer could teach ethics—but most ethical rules or constraints are intuitive. I mean, there's a reason why they exist. There are some that are not, but 95 percent of them are intuitive. It is unethical because it is also going to cut against the credibility of your case.

So that's not why you do it, but there are two reasons to do it. You're not going to advance a theory that's utterly incredible because you're not serving your client's interest. You're wasting their money or and your money, and it tends to run consistently with the notion of ethics.

MS. HART: Well, I have litigated across the country and state-by-state-by-state with my partner Bernie Persky and without being able to say—and what are the ethics, as Bernie would conclude, each class certification that if the class isn't certified, in essence, you have a wrong without a remedy.

This is actually where, I guess, philosophically, I always end up circling back to. If there is culpable conduct, and I guess I shouldn't use the word—what is the morality? Essentially, we don't have an ascertainable class, not all class members were damaged. But as to those that were, if we have culpability, recognizing Joel's point that he's empowered, he's charged with zealously trying to defeat class certification, that's where his obligations begin and end, what are the ethics of the law not really ending up giving redress to the injured class members? I felt, Dr. Rapp, that you've wrestled with this intellectually and, no doubt, professionally in terms of the infirmities of Rule 23.

DR. RAPP: I have and I have never put pen to paper or touched the keyboard about it because I didn't want to be deposed about it. And with the understanding that I won't be deposed about it today, I think that Rule 23 is upside down, and it is not an ethical issue unless you speak of the ethics of the rule rather than a lawyer's behavior constrained by that rule.

It occurs to me, and I must say I haven't thought deeply about it, that if we were starting from scratch, what we would do is we would try to establish the merits of the case by some kind of summary judgment procedure early in the game. And if it is a meritorious case, we would want to have the controversy about the class later on confined to getting the class defined right, and then the only remaining issue is: Is class certification with this properly defined class appropriate? And it is the simplest, most straightforward thing. It is not all this stuff about numerosity and commonality. It is whether or not—it is efficiency. In other words, is the recourse that individuals have too small to enable them to make it rational for them individually to sue? And if not, having previously determined that it is a meritorious case and having previously defined the class correct, game over.

But the rules of the game, as I understand it, the case law that—Rule 23 and the ensuing case law—doesn't give you those choices. It gives you the choices that we have been talking about up until now.

MS. HART: Well, strategically, we do sometimes try to get a quasi-summary judgment ruling on something if we feel that we can go for it in order to establish a predominance of common issues and hope that that ends up being a hook. But generally, I tend to think you are quite correct, that we can't get to the summary judgment because the issues are: Many would be in the gray area, so you're not going to get a summary judgment ruling from the court. You have to get to the trier of fact on it. But what's fascinating to me because, as I said we had this kind of salon discussion on the phone about these issues and I knew that Dr. Rapp had some strong feelings—it always struck me that the class—Rule 23, is somewhat of an economic proposition, that the claims are too small to be fruitful individually and that's why they come under the class action.

And in essence, he thinks we got it ass-backward from an economic point of view. That you should establish the merits and the merits should drive whether or not there then is a remedy.

Joel?

MR. COHEN: I'm sorry, I couldn't disagree more. And I understand your rationale.

First of all, you have to remember the class action mechanisms, state or federal, don't exist for differentiating actions ranging from civil rights actions, consumer rights, product liability, securities class action. And in many of those other realms the issue of the size of the individual harm is really not the main issue. It is not numerosity. It is whether the individual claims are sufficient or similar enough or any of the other three prongs that

matters. A perfect example, the tobacco litigation is, in general, just a fact not susceptible to class-action litigation. People may disagree with that's the way it should be, but that's the way it has been historically because the courts have found again and again and again that the issues that smokers share are not similar enough.

So the class-action mechanism is designed to come to many different kinds of claims, not just the one we are discussing today.

Also from a defense perspective, just because there's a harm doesn't mean there has to be a remedy. To put it in simple terms, stuff happens in the world and there isn't a remedy for every ill. If the world were that way, it would be wonderful. But it isn't. The law is not designed to remedy every ill. Maybe there should be a better law. Maybe we should say, "Here's the harm. Let's figure out how to split it up and give damages to people even though we can't really come up with a rational way of figuring out."

DR. RAPP: That's unsatisfying, I think. There's a better answer to that than that from the defendant's standpoint. Tell me if you disagree. The notion that you can have a harm but we can't come up with a remedy is a problem waiting for a solution. The more difficult matter, thus the symmetrical other side to the problem that I mention is that class action and the implicit, the necessary numerosity that implies is that if you lose in class action—you've got a defendant who loses. He's got a very, very large overhanging damage award and it is—I forget what the language that's quoted about this is, gun-to-the-head or something like that. So the corresponding difficulty is that the way the class, the way the sequence of events works today, if you win on class action, if you prevail, then it drives the defendants to the bargaining table. And there is some shortcut of due process in that. If that's not the right word, then I'll choose another one. I think that's a better defense of the status quo than saying, "Look, sometimes there's a remedy—there's a harm without a remedy."

MR. COHEN: I'm not defending the status quo. I just don't think we can ever establish a system where all harms are remedied.

MS. HART: I wasn't talking about harm. I was talking about wrongdoing.

AUDIENCE MEMBER: Part of the problem with your analysis is it is one-sided. Even if you accept the proposition that you want to find a remedy for every wrong—it is probably not a bad idea if you could actually find a way to do it—there are two sides in the class action to the litigation. One of the sides of the class action deal is, once you've certified the class and the defendant wins, the action has no merit, then the defendant gets to go home and doesn't have to litigate it again and again and again. If you litigate the merits first and then decide the class action, what happens when the defendant wins that first time? I would like to think that all of the rest of the potential claimants in the world will say, "Okay, no merit, go home." There are lots of plaintiffs with different perspectives, lots of lawyers, not all of them are as capable as Linda, Barbara and Bernie. They will say, "All right, I'll do it a different way."

So as a defendant you could find yourself dealing with multi-iterations of the same case. So candidly for the defendants, it is not just the notion of "Oh, I can defeat them by certification and make this go away and no one will then sue me." It is, "If I get a class certified, I might have to litigate it or maybe I can win that motion for summary judgment."

DR. RAPP: Saul, I'm going to allow you and Joel to win now. Otherwise, I'm going to have to ask Gary for a job.

MS. HART: Well, I think it is interesting. The securities area, in which I also litigate, has kind of done this. I think the objective here is to set us thinking about how we improve, how we make a more perfect attempt to get to the truth, a more perfect union, a more perfect search for the truth, and a proper outcome for remediation. What's fascinating to me is what the PSLRA has done in taking the class-action device and now says that the institution with the largest loss, clearly like a *Calvert* or *Connecticut*, could litigate these cases with a hundred million dollar loss as an individual case. But now that person is put in charge of all the mom-and-pop claims in the securities case, which is kind of a strange situation where they are captured and they always have, in essence, been captured in the class-action device. And I think it's been the law of unintended consequences. I believe it was intended to put plaintiffs' lawyers out of business. But in essence, it has given us more credibility, a sophisticated client, a better reception from defense counsel, and it is now being discussed, often in the plaintiff's bar, that we think about coming forward with a larger client. In the air cargo case, *Volvo*, it has traction for the court, it has traction vis-à-vis plaintiff's counsel, so there is all this discussion where that's going to be considered.

Now, is *Volvo* the small injured party without remediation that needs the class-action device for it to obtain remediation? Or does it have the ability to go to an Air Cargo and say, "You overcharged me, pay me back."

But here we have a situation where they are becoming part of the class action and it's where we are evolving and changing. Of course, we won't know how it turns out.

Bernie?

AUDIENCE MEMBER: Well, just one thing, the idea of a wrong without a remedy is wonderful, and I subscribe to the idea that there should not be a wrong without a remedy. But I think the litigation turns out generally not to be a search for truth or justice. It is just part of an adversarial system. I don't know that truth or justice—it's the goal but supposedly truth or justice will come from the clash of adversarial interests.

So I think the idea that truth or justice is not being served is wrong, but I think that often happens because of the adversarial system.

MS. HART: Well, so much for ethics then.

AUDIENCE MEMBER: Could the experts indulge this question: Could you identify the top two or three things that lawyers ask you to do that you find distasteful, if not unethical?

DR. RAPP: Want to go first? I've thought about this a bit too because I was giving a talk once and Andy Gavel, who is a very thoughtful commentator on antitrust, I forget how the subject arose, but he used the phrase "excessive zeal and advocacy by economic experts in antitrust." And I thought that that is something that we run the risk of doing badly, although there are actually two sides to that story that I won't go into because it is not responsive to your question.

But there is no bright line there and the answer to how scientific an expert can be and how much an expert and how forceful in his or her opinion as an expert can be is actually an interesting question because it also has to do with the way science works.

The answer to your question that comes directly to mind is that the need that both plaintiffs and defense lawyers have to engage in framing requires the participation of their experts and it is problematic.

"Framing" is a term that's used at the intersection of economics and psychology that means the following: If you can persuade an expert to say this case is a billion-dollar damage case, then when the jury sits down and it says, "You know, I really don't believe those plaintiff lawyers and the plaintiffs, let's not give them a billion dollars, let's give them 200 million." And if Joel can get his expert to say, "I've done the damage calculation. This is a $15,000 case." And the lawyer says, you know, "Joel isn't worth believing and his expert is not worth believing, let's really hand it to them. Let's give them $60,000." That's what framing is all about. The number that comes out frames the discussion. Both sides are, in some sense, compelled strategically to do that. It's very hard not to enlist your expert in that, and that is where pressure is applied in ways that we find difficult. So that's my answer.

MS. HART: Thank you.

Gary?

DR. FRENCH: Well, I don't think there's a lot that lawyers have asked me to do that's distasteful. I do have one pet peeve. It is when they want to designate me without me knowing or doing much. Sometimes it's okay because I know enough about the case and it's similar to other cases. And they are not asking me to reach a conclusion, but they are saying I'm going to talk about market share or pricing or something. Yes, I will, that's innocuous, I can talk about that. But don't say what I'm going to say about it.

So sometimes it's okay, and it rarely happens. I mean, but if you force me to say what's distasteful that's the only thing I can think of, and it's very rare.

MS. HART: Thank you all very much and enjoy the night.

(Applause.)

MR. MORGENSTERN: I would like to thank our panel and our moderator for an excellent program and thank you all for coming today.

(Whereupon, the proceedings concluded.)

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ANNUAL MEETING

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New York Marriott Marquis
New York City

Antitrust Law Section Meeting
Thursday, January 31, 2008