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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

10	Masimo Corporation,)	CASE No. CV 02-4770 MRP
11)	
12	Plaintiff,)	
13	v.)	MEMORANDUM OF DECISION RE:
14	Tyco Health Care Group, L.P. and)	Post-Trial Motions
14	Mallinckrodt, Inc.)	
15	Defendants.)	
16	_____)	

The parties have each filed post-trial motions. Defendants Tyco Health Care Group, L.P. and Mallinckrodt, Inc. ("Tyco") filed a Renewed Motion for Judgment as a Matter of Law, or Alternatively, a New Trial ("JMOL") and a Motion to Stay Entry of Judgment. The Motion to Stay Entry of Judgment was voluntarily withdrawn following the conclusion of patent litigation between the parties. Plaintiff, Masimo Corporation ("Masimo") filed a Motion for Entry of a Permanent Injunction. On June 28, 2005, this court heard oral argument and took the Motions under submission.

BACKGROUND

The court held a four week trial of this case during February and

1 March 2005. Before the trial, the parties stipulated to the relevant
2 product and geographic markets at issue in the case. The relevant
3 product market is the pulse oximetry systems market, which consists of
4 sensors, patient cables and pulse oximeter monitors. The relevant
5 geographic market is the United States. Pulse oximetry involves
6 measuring a patient's heart and lung function via a non-invasive
7 procedure that calculates pulse and arterial blood oxygen saturation.
8 A pulse-oximeter sensor is typically attached to the end of a
9 patient's finger. The sensor is made up of a photoemitter that sends
10 light through the patient's tissues, and a photodetector that measures
11 the light transmitted through the tissue. The monitor computes the
12 patient's blood oxygen saturation from the measured data.

13 Masimo claimed that Tyco violated Section 3 of the Clayton Act
14 ("Section 3") and Sections 1 and 2 of the Sherman Act ("Section 1" and
15 "Section 2"). Masimo identified five Tyco business practices that it
16 contended were anticompetitive under Sections 1 and 3. These
17 practices included: (1) providing "loyalty discounts" to hospitals in
18 exchange for a hospital's commitment to purchase not more than a
19 specified percentage of the hospital's requirements for oximetry
20 products from Masimo or other competitors of Tyco ("Market Share
21 Discounts"); (2) entering into "sole-source exclusive dealing
22 arrangements" with hospital Group Purchasing Organizations ("GPOs")
23 that effectively prevent Masimo and other competitors from selling
24 oximetry products to GPO hospitals ("Sole Source"); (3) offering
25 "bundled rebates" in which discounts on oximetry products were linked
26 with discounts on completely unrelated Tyco products ("Bundled
27 Discounts"); (4) entering into contracts with Original Equipment
28 Manufacturers ("OEMs") that effectively foreclosed OEMs from

1 manufacturing monitors compatible with Masimo and other rival
2 technology ("Co-marketing Agreements"); and (5) entering into oximetry
3 "equipment financing programs" that impose financial penalties on
4 hospitals that switch to rival oximetry monitors before the expiration
5 of financing agreements ("Equipment Financing Programs"). For its
6 Section 2 claim, Masimo asserted that liability was based on a
7 "monopoly broth" theory in which any of the alleged anticompetitive
8 practices independently or in combination, resulted in a Section 2
9 violation.

10 The jury found Tyco liable for violating Sections 1, 2 and 3, but
11 awarded damages for only the Section 1 and 3 violations. The jury
12 awarded Masimo \$140 million in damages and found that all damages
13 occurred prior to July 2001. The jury concluded that Tyco's Equipment
14 Finance Programs were lawful and found the remaining four practices to
15 be both "exclusive dealing arrangements" under Section 3 and
16 "unreasonable restraints of trade" under Section 1. The jury
17 apportioned damages based on the effect each practice had on Masimo.
18 The jury awarded Masimo \$57 million for Market Share Discounts and \$57
19 million for Sole Source GPO Contracts based on Section 1 liability but
20 did not award any damages for these practices based on Section 3
21 liability. The jury awarded Masimo \$13 million for Product Bundling
22 and \$13 million for Co-Marketing Agreements based on Section 3
23 liability but did not award any damages for these practices based on
24 Section 1 liability.

25 **LEGAL STANDARD FOR JUDGMENT AS A MATTER OF LAW**

26 Tyco has renewed its motion for judgment as a matter of law under
27 Rule 50(b) of the Federal Rules of Civil Procedure (FRCP). FRCP Rule
28 50(a)(1) establishes the standard by which this court must consider

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1 Tyco's motion for judgment as a matter of law:

2 If during a trial by jury a party has been fully
3 heard on an issue and there is no legally
4 sufficient evidentiary basis for a reasonable jury
5 to find for that party on that issue, the court
6 may determine the issue against that party and may
7 grant a motion for judgment as a matter of law
8 against that party with respect to a claim or
9 defense that cannot under the controlling law be
10 maintained or defeated without a favorable finding
11 on that issue.

12 FRCP Rule 50(a)(1). In accordance with this standard, this court
13 should grant Tyco's motion for judgment as a matter of law if
14 substantial evidence does not support the jury's factual findings or
15 if those factual findings cannot support the legal conclusions implied
16 from the jury's verdict. *Chiron Corp. v. Genentech, Inc.*, 363 F.3d
17 1247, 1252-53 (Fed. Cir. 2004).

18 A district court may overturn a jury's verdict only if reasonable
19 jurors could not have reached that verdict on the record that was
20 before them. *Bell v. Clackmas County*, 341 F.3d 858, 865 (9th Cir.
21 2003). This court must view the evidence in the light most favorable
22 to the non-moving party, draw all reasonable inferences in favor of
23 the non-moving party, and consider whether there is sufficient
24 evidence in the record to support the jury verdict. *Horphag Research
25 Ltd. v. Pelligrini*, 337 F.3d 1036, 1040 (9th Cir. 2003); *McEuin v.
26 Crown Equip. Corp.*, 328 F.3d 1028, 1036 (9th Cir. 2003).

27 **LEGAL STANDARD FOR REQUEST FOR A NEW TRIAL**

28 Tyco alternatively requests a new trial under Rule 59(a) of the
FRCP. FRCP Rule 59(a) reads in relevant part:

A new trial may be granted to all or any of the
parties and on all or part of the issues (1) in an
action in which there has been a trial by jury,
for any of the reasons for which new trials have
heretofore been granted in actions at law in the
courts of the United States.

1 Under applicable law, "a new trial is proper only if the 'verdict is
2 contrary to the clear weight of the evidence, or is based upon
3 evidence which is false, or to prevent, in the sound discretion of the
4 trial court, a miscarriage of justice." *Hangarter v. Provident Life &*
5 *Accident Ins. Co.*, 373 F.3d 998, 1005 (9th Cir. 2004). In ruling on a
6 new trial motion based on insufficiency of the evidence, the court
7 need not view the evidence in the light most favorable to the
8 prevailing party. *Landes Constr. Co. V. Royal Bank of Canada*, 833 F.
9 2d 1365, 1371 (9th Cir. 1987).

10 ANALYSIS

11 In considering the parties' motions, the court first reviews the
12 jury's verdict with respect to liability and then examines the issue
13 of damages and the motion for permanent injunction. The jury found
14 Masimo did not suffer damages after July 2001. For that reason, and
15 because Masimo did not have a product approved for sale by the FDA
16 until February 1997 the court limits its analysis to the time period
17 February 1997 to July 2001.

18 I. SECTION 1 AND 3 LIABILITY

19 Section 3 of the Clayton Act prohibits companies from making
20 exclusive agreements that prevent buyers from dealing in the goods of
21 a competitor where the effect of the agreements "may be to
22 substantially lessen competition or tend to create a monopoly." 15
23 U.S.C. § 14. Section 3 of the Clayton Act seeks to prevent the
24 anticompetitive effects of exclusive dealing arrangements. See *Twin*
25 *City*, 676 F.2d at 1302. To fall within the purview of Section 3, the
26 contract must be "truly an exclusive dealing one." *Tampa Elec. Co. v.*
27 *Nashville Coal Co.*, 365 U.S. at 329-30. Exclusivity alone is not
28

1 sufficient to establish an antitrust violation under Section 3; the
2 contract must also foreclose competition. See *Tampa Elec. Co.*, 365
3 U.S. at 327 (even though a contract may be found to be an exclusive
4 dealing arrangement, it does not violate Section 3 unless the court
5 "believes it probable that performance of the contract will foreclose
6 competition in a substantial share of the line of commerce affected")
7 (emphasis added); see also *Omega Envtl. v. Gilbarco*, 127 F.3d 1157,
8 1162 (9th Cir. 1997) ("[T]he main antitrust objection to exclusive
9 dealing is its tendency to foreclose existing competitors or new
10 entrants from competition in the covered portion of the relevant
11 market during the term of the agreement.").

12 The Supreme Court has explained that a contract need not include
13 specific terms of exclusivity in order to qualify as an exclusive
14 dealing contract under Section 3, as long as the "the practical
15 effect" of the agreement is to exclude competitors. *Tampa Elec. Co.*,
16 365 U.S. at 329-30 (*de facto* exclusivity is sufficient to qualify
17 under Section 3). However, "virtually every contract to buy
18 'forecloses' or 'excludes' alternative sellers from some portion of
19 the market, namely the portion consisting of what was bought."
20 *Gilbarco*, 127 F.3d at 1162. Therefore, the first step in evaluating a
21 Section 3 claim is to determine whether the challenged practice is
22 actually an exclusive dealing arrangement. *Tampa Elec. Co.*, 365 U.S.
23 at 327, 329-30. If an agreement is an exclusive dealing arrangement,
24 it is then analyzed under the antitrust rule of reason to determine if
25 it has anticompetitive effect. *Gilbarco*, 127 F.3d at 1162.

26 Section 1 of the Sherman Antitrust Act prohibits every contract,
27 combination in the form of trust or otherwise, or conspiracy, in
28 restraint of trade or commerce. See 15 U.S.C. § 1. The elements of a

1 Section 1 case are: (1) an agreement or conspiracy among two or more
2 entities; (2) with the intent to unreasonably restrain competition;
3 (3) which causes injury to competition. See *Eichman v. Fotomat Corp.*,
4 880 F.2d 149, 161 (9th Cir. 1989). SCANNED

5 In cases where the business practices challenged under Section 1
6 are not considered per se illegal under antitrust law, the analysis of
7 a Section 1 claim is very similar to the analysis of a Section 3
8 claim. Like Section 3 claims, Section 1 claims that are not per se
9 illegal are analyzed under the rule of reason.¹ See *Twin City*, 676
10 F.2d at 1304; *Gilbarco*, 127 F.3d at 1162 (the rule of reason analysis
11 used to determine a Section 1 Sherman Act violation is also the
12 appropriate test for a Clayton Section 3 violation, citing *Twin City*);
13 see also *Jefferson Parish Hospital District No. 2 v. Hyde*, 466 U.S. 2,
14 45 (1984) (O'Connor, J. concurring). Under the rule of reason, "[o]nly
15 those arrangements whose 'probable' effect is to 'foreclose'
16 competition in a substantial share of the line of commerce affected"
17 violate the antitrust laws. *Omega*, 127 F.3d at 1162 (citing *Tampa*
18 *Elec.*, 365 U.S. at 327 and *Jefferson Parish*, 466 U.S. at 45).

19 Although there is no set percentage for how much of the relevant
20 market must be foreclosed, it must be substantial enough that
21 competitors are truly "frozen out of a market." *Omega* 127 F.3d at 1162
22 (38% foreclosure was not actionable); but see *Twin City*, 676 F.2d at
23 1304 (24% foreclosure was actionable). In determining whether
24

25
26 ¹ The Ninth Circuit has found that exclusive dealing
27 arrangements challenged under Section 1 are not per se violations
28 and are evaluated under the rule of reason. See *Twin City*, 676
F.2d at 1304, n.9 (citing *Tampa Elec. Co.*, 365 U.S. at 327).
Masimo has never contended that any of the alleged practices were
per se illegal and therefore the appropriate legal analysis to
use in evaluating the Section 1 claims is the rule of reason.

1 substantial foreclosure exists, courts must evaluate whether
2 alternative distribution channels were available, whether the
3 challenged contracts were in practice terminable on short notice, and
4 whether one or more competitors was able to enter or expand business
5 in the relevant market during the time in which the challenged
6 contracts were in effect. *Omega*, 127 F.3d 1163-64.²

7 **A. Market Share Discounts**

8 Throughout the trial, Masimo referenced Joint Trial Exhibit 1392,
9 an internal Tyco strategy document. The document includes a depiction
10 of a castle surrounded by a series of walls. The castle keep is
11 labeled "sensors". According to Masimo, the protective walls are
12 labeled with each of the anticompetitive practices at issue in this
13 case and the exhibit illustrates Tyco's intent to insulate its sensor
14 franchise from competition with the practices at issue. The court did
15 not find the exhibit as persuasive as the jury apparently did and
16 reviews the accused practices individually.

17 The evidence established that Tyco offered hospitals increased
18 discounts on the purchase of pulse oximetry sensors in exchange for a
19 hospital's commitment to buy a greater percentage of its oximetry
20 needs from Tyco. Masimo argued these contracts prevented hospitals
21 from purchasing more than small amounts of their oximetry needs from
22 other suppliers like Masimo.

23 During the trial, Masimo demonstrated the effects of a typical
24

25 ² The Ninth Circuit also has explained that it is easier to
26 meet the threshold of foreclosure for a Section 3 violation than
27 it is for a Section 1 violation. See *id.* at 1304, n.9 ("a
28 greater showing of anticompetitive effect is required to
establish a Sherman Act violation than a [S]ection 3 Clayton Act
violation in exclusive-dealing cases.").

1 Market Share Discount agreement. Pursuant to an agreement with Tyco,
2 a hospital received a 40% discount on sensors if it bought at least
3 90% of oximetry products from Tyco. JTX-85; JTX-335. The discounts
4 dropped to 16%-18% on all oximetry sensors if the hospital bought less
5 than 90%. Tr. 1743-47, 1751-55. Masimo argued that the possible loss
6 of Tyco's maximum discounts on all of a hospital's sensor purchases
7 functioned as a "penalty" forcing hospitals to deal exclusively with
8 Tyco. According to Masimo, for a hospital to purchase Masimo sensors,
9 even if they were offered at a substantially lower price than Tyco's,
10 a hospital would have to replace some or all of its existing Tyco
11 compatible monitors. In most cases, Masimo claimed, it could not
12 price its sensors low enough to compensate hospitals for the cost of
13 replacing monitors and the loss of Tyco's discounts. Opp'n. at 18,
14 citing Tr. 443-47.

15 In 1997, Masimo was a new entrant into the oximetry systems
16 market. Tyco was the well established market leader with a 15-year
17 head start. By virtue of its earlier entry, Tyco had a preexisting
18 installed base of oximetry monitors that had been previously sold to
19 hospitals. As shown at trial, oximetry monitors are expensive pieces
20 of equipment that have a usage life of 5 to 7 years. Stand-alone
21 monitors made by a particular manufacturer are typically compatible
22 with only one kind of sensor. Once a hospital has purchased a
23 particular manufacturer's monitor, it must purchase compatible sensors
24 and can only purchase non-compatible sensors if it buys additional
25 monitors. This was the market environment in which Masimo first began
26 to sell its products.

27 The jury had to decide whether Masimo's difficulties were the
28 result of anticompetitive Market Share Discounts, or instead, whether

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1 Masimo's difficulties stemmed from the fact that it was trying to win
2 business from customers with pre-existing investments in a
3 competitor's product (i.e. Tyco monitors). Irrespective of the Market
4 Share Discounts, in most cases, hospitals already had strong
5 incentives to buy a certain percentage of their sensor requirements
6 from Tyco in order to support their Tyco compatible monitors.
7 Although the court might have reached a somewhat different conclusion,
8 the jury concluded the Market Share Discounts were anticompetitive.
9 The jury could reasonably have reached that conclusion.

10 In order for the Market Share Discount agreements to be
11 considered exclusive dealing arrangements, the agreements must, in
12 practical effect, exclude other sellers. See *Tampa Elec. Co.*, 365
13 U.S. at 329-30. The jury was free to conclude that Tyco's Market
14 Share Discounts, in practical effect, offered hospitals their best
15 discount only if they dealt with Tyco exclusively.

16 The evidence, however, showed that Tyco's Market Share Discount
17 agreements were contractually terminable by hospitals on short
18 notice.³ (Tr. 2438:25-2439:15, 2440:18-2441:13, 2445:1-10, 2449:21-
19 2451:22.) In general, exclusive dealing arrangements that are
20 terminable on short notice are not anticompetitive because foreclosure
21 is very unlikely. See *Western Parcel Express v. United Parcel*
22 *Service*, 190 F.3d 974, 976 (9th Cir. 1999); *Concord Boat Corp. v.*
23 *Brunswick Corp.*, 207 F.3d 1039, 1062-63 (8th Cir. 2000). Even if a
24 buyer has an agreement to purchase 100% of its requirements from a
25 single supplier, if the buyer is free to terminate the agreement on

26
27 ³The ability of hospitals under Sole Source contracts to
28 terminate Market Share Discount agreements on short notice is
discussed separately under the next subsection.

1 short notice, the agreement is generally not anticompetitive. In the
2 absence of long-term commitments, an efficient competitor can offer a
3 competitive price at any time and win the buyer's business.

4 Although the Market Share Discount agreements appear to have been
5 terminable on short notice on their face, the jury could reasonably
6 have concluded that in practice they were not. A number of hospitals
7 were financially locked into purchasing a fixed amount of Tyco sensors
8 to support their installed Tyco monitors. These hospitals were locked
9 into those purchases for the duration of the useful life of their
10 installed Tyco monitors. This fixed demand for Tyco sensors for an
11 extended period of time, when combined with the Market Share
12 Discounts, effectively prevented the hospitals from purchasing sensors
13 outside of the Market Share Discount agreements on short notice. The
14 jury therefore, could reasonably conclude those agreements were
15 defacto exclusive.

16 Tyco argues that *Omega Environmental., Inc. v. Gilbarco, Inc.*,
17 127 F.3d 1157 (9th Cir. 1997), comprehensively addresses what evidence
18 is sufficient and insufficient to sustain a jury verdict of
19 foreclosure in an exclusive dealing case. In that case, the court
20 concluded that exclusionary agreements that foreclosed 38% of the
21 market did not, as a matter of law, substantially foreclose the
22 market. The court based its decision on two primary factors. First,
23 the court held that agreements with distributors "are generally less
24 cause for anticompetitive concern" because they do not necessarily
25 foreclose competitors from reaching end-customers directly. *Id.* at
26 1163. Second, the court held that the "short duration and easy
27 terminability" of the agreements at issue in the case "negate
28 substantially their potential to foreclose competition" because the

1 termination provisions allowed the plaintiff to induce switching by
2 offering a better product or a better deal." *Id.* The Market Share
3 Discounts at issue in this case were made directly with hospitals, and
4 as previously discussed, the agreements were not in practice
5 terminable on short notice.

6 In *Twin City Sportservice v. Charles O. Finely & Co.*, 676 F.2d
7 1291, 1298 (9th Cir. 1982), the Ninth Circuit found that where an
8 exclusionary agreement was not terminable on short notice, market
9 foreclosure of 24% was sufficient to trigger Section 1 and 3
10 liability.⁴ Ample evidence was introduced at trial showing that
11 Masimo was not foreclosed from all hospitals. In fact, the record
12 shows that Masimo was able to convince a number of hospitals to
13 replace their existing oximetry monitors with Masimo technology and
14 from 1998 to 2001, Masimo was able to grow revenues from zero to over
15 \$14 million and capture over 10% of new oximetry monitor sales.
16 Nevertheless, the jury could reasonably conclude from the evidence
17 presented at trial that competitors were foreclosed from greater than
18 24% of the market and that the foreclosure was substantial. The jury
19 could also reasonably conclude that the anticompetitive effects of the
20 foreclosure outweighed the procompetitive effects of the Market Share
21 Discounts. The jury's liability verdict with respect to Market Share
22 Discounts must therefore, be sustained.

23 B. Sole Source GPO Contracts

24 The evidence showed that Tyco entered into Sole Source contracts
25 with certain GPOs. Under the Sole Source agreements, the GPOs offered
26 their member hospitals pre-negotiated discounts on Tyco oximetry

27
28 ⁴ A Section 3 claim may be supported by less than 24%
foreclosure. *Id.* at 1304 n.9.

1 products. Under the Sole Source agreements, Tyco was the only
2 provider with which the GPOs had pre-negotiated discounts. GPOs
3 function as agents for their group hospitals, investigating products
4 and using their group members' combined power to negotiate discounts.
5 It was the hospitals, however, that were the direct purchasers of
6 products. At trial, Masimo focused on Tyco's contracts with three
7 GPOs: Premier, Consorta and Novation.

8 The Sole Source GPO contracts, essentially, were Market Share
9 Discount programs, like those discussed in the previous section. The
10 only difference was that the contract terms were negotiated with GPOs,
11 rather than directly with hospitals. Masimo argued the Sole Source
12 contracts were exclusionary for the same reasons as the Market Share
13 Discounts. In addition, Masimo argued the GPO contracts were
14 exclusionary because, by their terms, they restricted hospitals from
15 purchasing from Masimo and other oximetry providers.

16 There was conflicting evidence as to whether the Sole Source
17 agreements expressly restricted GPO members from purchasing Masimo
18 oximetry products. A reasonable jury could have concluded that
19 agreements with Premier and Consorta were exclusionary on their face.
20 However, a jury could not reach the same conclusion with respect to
21 Novation or its predecessor organizations.

22 Evidence was presented that Premier and Consorta members were
23 required to purchase 90% and 85%, respectively, of their oximetry
24 products from Tyco. JTX-97, JTX-983. Evidence also was presented
25 that members of both GPOs were prohibited from buying outside of the
26 GPO contracts (except for allowed minimums), and that members were not
27 permitted to belong to more than one GPO. Id. With respect to
28 Premier, the jury also could have concluded from the evidence that

1 hospitals that were not in compliance with GPO agreements could be
2 penalized or ejected from the GPO. JTX-480.

3 With Novation, an explicit term of the GPO contract provided that
4 no member hospital was required to buy anything from Tyco. JTX-304 at
5 NOV000931; Tr. 1033:9-14. In addition, the Novation Sole Source
6 agreement was not in effect until January 2001. Therefore, the
7 Novation agreement, even if restrictive, could only have had a minimal
8 impact on the market before the jury concluded damages ceased in July
9 2001.⁵

10 Tyco claimed that the Sole Source agreements were terminable on
11 short notice and, therefore, under *Concord Boat*, even if the
12 agreements were exclusionary, they were not anticompetitive. In
13 support, Tyco elicited evidence that the GPO contracts with Premier
14 and Consorta were terminable at will on 90 days notice. Tr. At
15 2448:21-2449:20, 2873:17-2874:19. This evidence, however, only
16 demonstrates that the GPOs could terminate their agreements with Tyco.
17 The relevant inquiry is whether member hospitals could get out of the
18 agreements on short notice. A reasonable jury could conclude that
19 member hospitals could not. To get out of an agreement with Tyco, a
20 member hospital would either have to leave the GPO or ask the GPO to
21 terminate its agreement with Tyco. A jury could conclude that neither
22 option was a credible short-term solution. With respect to the
23 hospitals, the GPO contracts were effectively long term. The question
24 then becomes whether the jury could reasonably conclude that the

25
26 ⁵ In ft. 9 on page 15 of the opposition, Plaintiff argues
27 that Tyco had Sole Source agreements with VHA and UHC, Novation's
28 predecessors. However, evidence introduced at trial, including
cited exhibits, failed to demonstrate that members of VHA and UCS
were required to purchase oximetry products from Tyco.

1 | agreements foreclosed a substantial share of the market. *Omega*, 127
2 | F.3d at 1162.

3 | According to Tyco documents, in July 2001, Premier and Consorta
4 | membership accounted for 31% and 5% of U.S. hospitals, respectively.
5 | JTX 483. Masimo argued that these percentages actually represented an
6 | even greater portion of the overall oximetry market, because Premier
7 | included many of the country's largest hospitals which have greater
8 | oximetry needs.

9 | Tyco contends that Masimo failed to offer evidence showing that
10 | the 36% of hospitals covered by Premier and Consorta were actually
11 | foreclosed from purchasing oximetry from Masimo or other
12 | manufacturers. To the contrary, Tyco argues the evidence showed
13 | Masimo was successful in winning 14% of targeted Premier accounts and
14 | 96% of targeted Consorta accounts. Tr. At 675:12-682:20; Plaintiff's
15 | Demo 17. Tyco claims that proof of Masimo's sales to Premier and
16 | Consorta hospitals conclusively establishes that Masimo was not
17 | foreclosed. However, a closer inspection of Masimo's success rate
18 | shows that it was calculated from a total of 22 targeted hospitals in
19 | the case of Premier and 24 targeted hospitals in the case of Consorta.
20 | In 2002, Premier had 1,473 member hospitals and Consorta had a couple
21 | of hundred member hospitals. The jury was free to conclude that the
22 | handful of accounts won at Premier and Consorta were the result of
23 | selective enforcement of the GPO contracts, rather than an indication
24 | that Masimo had the ability to sell directly to GPO members.

25 | As with the Market Share Discounts, Tyco relies on *Omega*
26 | *Environmental* to argue that the evidence introduced at trial was
27 | insufficient to sustain a jury verdict of foreclosure in an exclusive
28 | dealing case. Because GPOs are not traditional distributorships like

1 those at issue in *Omega* and because, as previously discussed, the GPO
2 contracts were not in practice terminable on short notice, the court
3 finds *Omega Environmental* inapplicable. GPOs do not buy, sell or
4 physically deliver products to their members. As was noted above,
5 GPOs function as the agents of the hospitals and pre-negotiate
6 contract terms on behalf of hospitals, but it is the hospitals that
7 contract directly with the sellers. The GPO contracts with Premier
8 and Consorta were directly restrictive on the hospitals because they
9 prevented the hospitals from purchasing more than allowable minimums
10 of non-Tyco oximetry products. With respect to Premier and Consorta
11 members, Tyco's competitors were foreclosed, not just from selling
12 through GPO negotiated contracts, but from selling through any method.

13 *Twin City Sportservice* provides the standard for evaluating
14 foreclosure caused by Sole Source agreements. The jury could
15 reasonably infer that as a result of the GPO contracts with Premier
16 and Consorta, competitors were foreclosed from greater than 24% of the
17 market and that the foreclosure was substantial. The jury could also
18 reasonably conclude that the anticompetitive effects of the
19 foreclosure outweighed the procompetitive effects of the pre-
20 negotiated discounts.

21 C. Product Bundling

22 The evidence showed that Tyco offered "bundled discount"
23 agreements to GPO members, hospital networks and individual hospitals.
24 These discounts rewarded hospitals for purchasing certain minimum
25 quantities of a number of unrelated products. By purchasing all of
26 the bundled products, the hospital got additional discounts above and
27 beyond those offered in connection with the sale of each product
28 individually. Masimo argued that in order for it to compete against

1 bundled discounts, it would have to have sold "its products
2 substantially below cost and, in some accounts would have been able to
3 match Tyco's pricing only by paying the accounts tens or hundreds of
4 thousands of dollars." Opp'n. at 20 (citing Tr. 1239-43; 1789-90).
5

6 In evaluating a Section 1 or Section 3 claim, absent evidence of
7 a tying arrangement or predatory pricing, there is nothing problematic
8 about a company offering increased discounts if two or more products
9 are purchased together. *Jefferson Parish*, 466 U.S. at 11-12. Masimo
10 did not argue that the bundled discounts were predatory or functioned
11 as a tying arrangement and there was insufficient evidence introduced
12 at trial to reach either conclusion.

13 The court could not find a case where voluntary package discounts
14 were found to be unlawful exclusive dealing arrangements, under either
15 Section 1 or 3. *LePage's Inc. v. 3M*, 324 F.3d 141(3d Cir. 2003), upon
16 which Masimo primarily relies, and *SmithKline v. Eli Lilly & Co.*, 575
17 F.2d 1056 (3d Cir. 1978), upon which the *LePage's* decision was based,
18 both found bundling practices violated only Section 2. If a customer
19 has the alternative of purchasing the product separately, then barring
20 evidence of predatory pricing or tying, offering customers the product
21 in a package does not constitute a restraint of trade under Section 1
22 or 3. Insufficient evidence was presented for a jury to reasonably
23 conclude that the bundling programs were compulsory, predatory in
24 nature or tying arrangements.

25 Additionally, Masimo's expert estimated that 30% of oximetry
26 sales were affected by bundling practices. Tr. 1782:25-1783:5. The
27 expert included Novation's bundling programs in his estimate, however
28 the Novation bundling agreement did not go into effect until April
2001. Because the jury found all damages occurred prior to July 2001,

1 the Novation bundling program was only in effect for 4 months before
2 that date. The 30% potential market foreclosure figure therefore
3 appears to have been overstated.

4 The evidence also showed that bundling programs varied widely in
5 terms of the number and types of products included, as well as in the
6 amount of the discounts that were offered. Some bundles even included
7 products from manufacturers other than Tyco. Even if the jury could
8 have concluded certain bundles were anticompetitive, it was impossible
9 for the jury to determine, even in general terms, how much of the
10 bundled oximetry sales were sold in connection with anticompetitive
11 bundling practices as compared to legal bundling practices.

12 D. Co-Marketing Agreements

13 The evidence showed that Tyco entered into co-marketing
14 agreements with General Electric ("GE") and Hewlett Packard ("HP"),
15 the largest original equipment manufacturers ("OEMs") of multi-
16 parameter patient monitoring devices ("MPPMs"). MPPMs incorporate
17 oximetry and measure a number of patient vital signs, in addition to
18 blood oxygen levels. The co-marketing agreements provided that Tyco
19 would license its oximetry technology for inclusion in MPPMs and pay
20 GE and HP to market and promote Tyco sensors for use with Tyco
21 compatible MPPMs. Tr. at 2179:8-2180:9; 2182:18-2183:9; 2188:15-
22 2190:6. Masimo argued the agreements expressly required all MPPMs to
23 be compatible with Tyco and, as a result, they were not compatible
24 with Masimo. Masimo contends this result made the agreements de facto
25 exclusive.

26 The evidence, however, showed that neither the GE or HP agreement
27 included express terms requiring exclusive dealing with Tyco and both
28 agreements were terminable at will on 90 days notice. Tr. at 2174:6-

1 11; 2176:21-2177:7. As discussed previously, even if an agreement is
2 exclusionary, if it is terminable on short notice it is usually not
3 anticompetitive because foreclosure is very unlikely. See *Western*
4 *Parcel Express*, 190 F.3d at 976. As with the Sole Source agreements
5 previously discussed, there was no evidence that co-marketing
6 agreements directly restrained hospitals.

7 In addition, there was substantial evidence that the co-marketing
8 agreements did not foreclose competition and that the OEMs could and
9 did market more than just Tyco oximetry. GE offered Datex-Ohmeda
10 oximetry, as well its own technology. In 1999, over a year before the
11 expiration of the Tyco/GE co-marketing agreement, GE began marketing
12 Masimo technology. Tr. 2178:16-2179:3, 2190:20-2191:5; Tr. 699:16-
13 700:18, 1873:12-25, 2190:14-19, 2191:6-16; 823:22-824:1, 2190:14-19.
14 Similarly, HP offered its own competing oximetry technology and
15 sensors throughout the term of HP's co-marketing agreement with Tyco.
16 Tr. at 2177:8-18. Accordingly, a reasonable jury could not conclude
17 the co-marketing agreements were exclusionary or that they
18 substantially foreclosed competition.

19 II. SECTION 2 LIABILITY

20 Section 2 of the Sherman Act prohibits monopolies, attempts to
21 form monopolies, and combinations and conspiracies to do so. 15
22 U.S.C. § 2. To establish a violation of Section 2, a plaintiff must
23 show that (1) the defendant possessed monopoly power in the relevant
24 market and (2) the defendant willfully acquired or maintained that
25 power through "anticompetitive conduct," as opposed to gaining that
26 power as a "consequence of a superior product, business acumen, or
27 historical accident." *Image Tech. Serv., Inc. v. Eastman Kodak Co.*,
28 125 F.3d 1195, 1202, 1208 (9th Cir. 1997).

1 The possession of monopoly power in and of itself does not amount
2 to a Section 2 violation; the monopoly power must be maintained
3 unlawfully. *Verizon Communications, Inc. v. Law Offices of Curtis V.*
4 *Trinko, L.L.P.*, 124 S.Ct. 872, 879 (2004). SCANNED

5 A. Monopoly Power

6 Monopoly power is defined as the "power to control prices or
7 exclude competition." *Image Tech. Serv., Inc.*, 125 F.3d at 1202
8 (quoting *United States v. Grinnel Corp.*, 384 U.S. 563, 570-71 (1966));
9 see also *United States v. Syufy Enters.*, 903 F.2d 659, 664 (9th Cir.
10 1990). Market power can be proved by either direct evidence of the
11 "injurious exercise of market power" or through circumstantial
12 evidence. *Image Tech. Serv., Inc.*, 125 F.3d at 1208. When proving
13 monopoly power by circumstantial evidence, the plaintiff must
14 establish more than just market share; the plaintiff must: "(1) define
15 the relevant market, (2) show that the defendant owns a dominant share
16 of that market, and (3) show that there are significant barriers to
17 entry and . . . that existing competitors lack the capacity to
18 increase their output in the short run." *Rebel Oil Co. v. Atlantic*
19 *Richfield Co.*, 51 F.3d 1421, 1434 (9th Cir. 1995). A rebuttable
20 presumption of market power arises where the defendant has 65% or more
21 of the relevant market. See *Image Technical Serv., Inc. v. Eastman*
22 *Kodak Co.*, 125 F.3d 1195, 1206 (9th Cir. 1997).

23 Based on the evidence at trial, a jury could reasonably have
24 concluded Tyco had market power in the pulse oximetry systems market.
25 Professor Elhauge testified that Tyco's market share based on revenue,
26 ranged from 75% to 91% during the relevant time period. Tr. at 1163.
27 Dr. Leitzinger offered similar testimony (Tr. at 1678) and internal
28 Tyco documents suggested at least someone at Tyco believed its market

1 share was in excess of 65%. See, e.g. JTX-686 (78% "total market
2 share"); JTX-88 (89% "national market share" in oximetry as of
3 9/29/1999). Dr. Willig testified for Tyco that Tyco's market share
4 was 60.9% in 2002. Tr. At 2577:12-2579:3. His testimony, though
5 raising questions about the reliability of Leitzinger's market share
6 analysis, only presented data for 2002 and did not specifically
7 challenge market share numbers prior to July 2001. The jury was free
8 to infer that because Willig only introduced a market share number for
9 2002, even if his method of analysis was applied to the pre-July 2001
10 periods, Tyco's market share would have exceeded 65%. Additionally,
11 Masimo introduced evidence that Tyco was able to maintain high gross
12 profit margins in the face of competition and that there were
13 significant barriers to entry in the pulse oximetry market. Tr. 1163-
14 71, 1665-66, 1678-84. A reasonable jury could therefore have
15 concluded Tyco had market share in excess of 65% and that Tyco failed
16 to rebut the presumption that it had market power.

17 **B. Wrongful Maintenance of Monopoly Power**

18 The second element of a Section 2 monopoly claim, referred to as
19 the "conduct" element, addresses the question of whether Tyco used its
20 "monopoly power to foreclose competition, to gain a competitive
21 advantage, or to destroy a competitor." *Image Tech. Serv., Inc.*, 125
22 F.3d at 1208 (internal quotations omitted). To prove a Section 2
23 violation, the plaintiff must show that the defendant "willfully
24 acquired or maintained [monopoly] power" through anticompetitive acts.
25 *City of Anaheim v. Southern Cal. Edison Co.*, 955 F.2d 1373, 1376 (9th
26 Cir. 1992). A jury could reasonably have determined that the Market
27 Share Discounts and Sole Source contracts discussed in the previous
28

1 sections were designed to and did maintain monopoly power. Therefore,
2 the jury's verdict, with respect to Section 2 liability, is sustained.

3 As noted earlier, insufficient evidence was presented to the jury
4 to permit it to reach any reasonable conclusion about the
5 anticompetitive effect of Tyco's bundling practices. The bundling
6 programs varied widely in terms of the number and types of products
7 included, as well as in the amount of the discounts that were offered.
8 The bundling programs were dealt with so imprecisely at trial that a
9 jury could not reasonably conclude how much, if any, of the bundled
10 oximetry sales were sold in connection with anticompetitive bundling
11 practices as compared to legitimate bundling practices. For that
12 reason, Tyco's bundling practices do not form an independent basis for
13 Section 2 liability.

14 Additionally, during the course of the trial and the preparation
15 of this memorandum, the court has had the opportunity to reconsider
16 Masimo's bundling claims and the practice of bundling in general
17 within the context of Section 2. In support of its bundling claims,
18 Masimo relied primarily on the *LePage's* and *SmithKline* decisions
19 previously cited. The *LePage's* and *SmithKline* decisions held bundled
20 rebates violated Section 2 when the bundled discounts "linked a
21 product on which [the Defendant] faced competition with products on
22 which it faced no competition." *LePage's* at 156 (citing *SmithKline* at
23 1065). This court allowed Masimo's Section 2 bundling claim to
24 proceed to trial based on the reasoning of the *LePage's* case and
25 Masimo's assertion that "Tyco introduced bundled discount programs
26 that sought to leverage Tyco's dominant position in [non-oximetry]
27 products with its dominant position in pulse oximetry." Masimo
28 Summary Judgment Opp. at 10-11. (Emphasis added). At trial Masimo

1 failed to demonstrate that Tyco did not face competition in the non-
2 oximetry products it included in some bundles. According to *LePage's*
3 and *SmithKline*, it is only when products that do not face competition
4 are included in a bundle that the bundle can conceivably be
5 anticompetitive.

6 In *SmithKline*, defendant Eli Lilly offered bundled discounts for
7 the purchase of three different cephalosporin antibiotics. Eli Lilly
8 had patents on two of the antibiotics and according to the trial
9 court, Eli Lilly had monopoly power with respect to both of them. In
10 *LePage's*, defendant 3M offered bundled discounts for generic
11 transparent tape, bundled with a variety of other products, including
12 3M's Scotch-brand tape. The *LePage's* court found that Scotch-brand
13 tape was indispensable to retailers in the transparent tape market and
14 as such Scotch-brand tape was essentially like a monopoly. *LePage's*
15 at 156. The *LePage's* court concluded:

16 3M bundled its rebates for Scotch-brand tape with other
17 products it sold in much the same way that Lilly bundled
18 its rebates for [its three antibiotics]. In both cases,
19 *the bundled rebates reflected an exploitation of the*
20 *sellers monopoly power. Just as "[cephalosporins] [were]*
carried in . . . virtually every general hospital in the
country," SmithKline, 575 F.2d at 1062, the evidence in
this case shows that Scotch-brand tape is indispensable to
any retailer in the transparent tape market.

21 *Id.* (Emphasis added). The court then held that 3M's conduct, like
22 Lilly's before it, was anticompetitive because 3M leveraged Scotch-
23 brand tape (a monopoly) against captive purchasers of Scotch tape to
24 create a new monopoly in generic transparent tape. *Id.*

25 Based on *LePage's* and *SmithKline*, Masimo would have had to have
26 shown at a minimum: (1) that Tyco had monopoly or near monopoly power
27 in at least one non-oximetry product included within its bundles (i.e.
28 that such product faced no competition), and (2) that Tyco used that

1 monopoly power as leverage in maintaining its monopoly in the relevant
2 market. Insufficient evidence was presented for a jury to conclude
3 that either requirement was met. Therefore, even if this court were
4 to continue to be persuaded by the reasoning of *LePage's* and
5 *SmithKline*, Tyco's bundling practices would not have violated Section
6 2.

7 Upon careful consideration, this court disagrees with the
8 reasoning of the *LePage's* and *SmithKline* opinions. The court
9 concludes that as a general matter, absent evidence of predatory
10 pricing or tying, the practice of offering a discount on two or more
11 bundled products is not anticompetitive under Section 2. There may be
12 factual circumstances that warrant consideration of the antitrust
13 implications of bundling practices, separate and apart from predatory
14 pricing and tying, but those circumstances are not present in this
15 case or, in the court's opinion, in the factual record presented in
16 the *LePage's* and *SmithKline* opinions.

17 **III. DAMAGES**

18 As previously discussed, the jury's Section 1 and 3 liability
19 verdict is sustained based only on the anticompetitive effects of the
20 Market Share Discounts and Sole Source contracts. For that reason the
21 damages the jury apportioned to the other alleged anticompetitive
22 practices cannot be sustained. Accordingly, the damages awards of \$13
23 million related to Product Bundling and \$13 million related to Co-
24 Marketing Agreements are vacated. Because the jury did not award
25 damages for the Section 2 claim, the only damages issues that remain
26 for the court to review are the awards of \$57 million related to
27 Market Share Discounts and \$57 million related to the Sole Source
28 contracts.

1 Dr. Leitzinger, Masimo's damages expert, calculated Masimo
2 suffered \$97.41 million in damages prior to July 2001 as a result
3 all of the allegedly anticompetitive practices. Tr. at 3263:24-
4 3264:3. The damages figure was reached using a "yardstick"
5 methodology which purported to measure the relative performance of
6 Tyco and Masimo in an isolated portion of the oximetry market that was
7 not subject to the alleged anticompetitive practices. From that data
8 or "yardstick" measure, the expert extrapolated what Masimo's profits
9 would have been in the whole market absent the alleged anticompetitive
10 practices. Tr. 1812.

11 Leitzinger used oximetry monitor sales made to defibrillator
12 manufacturers as his "yardstick" . Id. He calculated that Masimo's
13 market share in this segment of the overall market averaged 50.2% over
14 its first four years. Tr. at 439-40, 1804-06; Demo-118. Based on
15 this information, he calculated his damages figure for the entire
16 oximetry market. He concluded that absent Tyco's alleged
17 anticompetitive practices Masimo would have sold 8% of all new
18 oximetry monitors in 1998 (its first year of sales), 25% in 1999 and
19 50% in 2000 and 2001. Tr. 1806-07; Demo-119.

20 Dr. Leitzinger's analysis, however, ignored some critical
21 problems with using the defibrillator market as a bench mark for
22 comparison. The defibrillator market accounted for a very small
23 percentage of the overall oximetry market, approximately 4% in 2002.
24 Id. The fact that Masimo was able to quickly attain 50% market share
25 in 4% of the market, does not necessarily imply that it would have
26 achieved commensurate success in the remaining 96% of a \$150 million
27 market. Leitzinger's methodology did not account for differences in
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1 the competitiveness and complexity of the overall market and the
2 defibrillator segment.

3 Masimo sold oximetry for inclusion in defibrillators primarily to
4 Zoll Medical Corporation, one of the two dominant defibrillator
5 manufacturers. In 1998, and particularly in 1999, Zoll achieved
6 breakthrough innovations in defibrillator technology that dramatically
7 increased sales. By virtue of its association with Zoll, Masimo's
8 market share in that segment also increased. As Dr. Ordover
9 testified, although Masimo's technology may have been a benefit to
10 Zoll, it was Zoll's technological advances that substantially
11 increased Masimo's market share. By applying Masimo's Zoll-assisted
12 market share to the overall market, Leitzinger inflated the success
13 Masimo would have had on its own in the overall market.

14 Despite the analytical shortcomings of Leitzinger's damage model,
15 the jury awarded Masimo \$140 million, over \$40 million more than
16 Leitzinger's pre-July 2001 damages figure of \$97.41 million. Masimo
17 contends the jury was free to conclude Leitzinger's estimates were
18 unduly conservative. Opp. at 43. For the reasons previously
19 discussed, the court disagrees and finds that even if the jury's
20 liability findings had survived in their entirety, the award would not
21 have fallen "within the range sustainable by the proof." *United*
22 *States v. Sullivan*, 1 F.3d 1191, 1196 (11th Cir. 1993). The court,
23 therefore, cannot sustain the damages awards associated with the
24 Market Share Discounts and Sole Source contracts because they were
25 derived from the larger unsustainable damages figure and the court
26 does not find them independently supportable.

27 Leitzinger's method of apportioning damages among the various
28 practices appeared to the court to be without basis. In fact at one

1 point in the trial he indicated there was "no way" for him to
2 determine the damages caused by an individual practice. Tr. at
3 3074:10-3075:3. It is clear that in many cases the evidence of Market
4 Share Discounts and Sole Source GPO contracts involved the same
5 conduct at the same hospitals. Leitzinger's method of allocation did
6 nothing to separate the substantial overlap of conduct and this led to
7 what appears to have been a substantial duplication of damages.

8 Additionally, Leitzinger's allocation of damages to Sole Source
9 contracts was premised on his opinion that Sole Source contracts
10 affected 70% of the market. This conclusion was wholly
11 unsubstantiated by the evidence. To take one example, Leitzinger
12 included the Novation Sole Source GPO agreements in reaching his 70%
13 figure. As was discussed, the inclusion of these agreements to the
14 same extent as Premier and Consorta created significant errors.

15 For the foregoing reasons, the court finds the damages awards of
16 \$57 million related to Market Share Discounts and \$57 million related
17 the Sole Source contracts do not "lie within the range sustainable by
18 the proof." *Los Angeles Memorial Coliseum Comm'n v. Nat'l Football*
19 *League*, 791 F.2d 1356, 1366 (9th Cir. 1986). The damages "verdict is
20 contrary to the clear weight of the evidence," and enforcing it would
21 be "a miscarriage of justice." *Hangarter v. Provident Life & Accident*
22 *Ins. Co.*, 373 F.3d 998, 1005 (9th Cir. 2004). Accordingly, the court
23 grants Defendants' motion for a new trial on damages relating to the
24 Market Share Discount agreements and Sole Source GPO contracts for the
25 pre-July 2001 damages period.

26 IV. THE MOTION FOR PERMANENT INJUNCTION

27 The court's power to issue an injunction against threatened
28 anticompetitive conduct stems from Section 16 of the Clayton Act, 15

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1 U.S.C. § 26, which allows suits for injunctive relief "against
2 threatened loss or damage by a violation of the antitrust laws."
3 demonstrating a threat of antitrust injury, the plaintiff must show
4 that it is suffering or is likely to suffer the kind of injury that it
5 would otherwise be entitled to relief for under antitrust law.
6 *Cargill, Inc. V. Monfort of Colorado, Inc.*, 479 U.S. 104, 112, 107
7 S.Ct. 484, 93 L. Ed. 2d 427 (1986).

8 The court has sustained the jury's finding that Tyco violated
9 Sections 1, 2, and 3 through the use of Sole Source contracts and,
10 that Masimo suffered damages prior to July 2001. The record
11 demonstrates that the practices employed by Tyco and the oximetry
12 market in general have changed substantially since July 2001. By
13 2003, Masimo was on contract with Premier and Novation, the largest
14 GPOs, dramatically altering the possibility of market foreclosure from
15 Sole Source contracts.

16 The jury was not specifically asked to determine liability by
17 time period. The jury however, allocated the entire damages award to
18 the pre-July 2001 time period, necessarily finding that Nellcor's
19 conduct did not cause Masimo injury post-July 2001. The court finds
20 no evidence that Masimo is currently suffering, or is likely to
21 suffer, antitrust injury from the Market Share Discounts or Sole
22 Source contracts. Accordingly, the court is unlikely to find that the
23 imposition of a permanent injunction is a necessary remedy. However,
24 it will consider that matter at a later time.

25 CONCLUSION

26 The jury's Section 1, 2 and 3 liability verdict is sustained
27 based on the anticompetitive effects of Market Share Discounts and
28 Sole Source contracts. The jury's findings of liability based on the

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1 other alleged anticompetitive practices are vacated. The jury's
2 damages award is vacated in its entirety. The court GRANTS
3 Defendants' motion for a new trial on damages.
4

5 IT IS SO ORDERED

6 DATED: March 22, 2006

Mariana R. Pfeelzer
Honorable Mariana R. Pfeelzer
United States District Judge

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