**IN THE UNITED STATES DISTRICT COURT**
**FOR THE DISTRICT OF MASSACHUSETTS**

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

**PLAINTIFFS' MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANTS' MOTION TO EXCLUDE THE EXPERT REPORT AND OPINIONS OF PROFESSOR EINER ELHAUGE**

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## I. INTRODUCTION

Plaintiffs Natchitoches Parish Hospital Service District and Smith Drug Co. ( collectively "Plaintiffs") respectfully submit this memorandum in opposition to Defendants' (collectively "Tyco") Motion to Exclude the Expert Report and Opinions of Prof. Einer Elhauge.

Tyco's long-awaited *Daubert* motion provides no basis to exclude Prof. Elhauge's testimony and no real challenge to his qualifications or expertise. Tyco's purported *Daubert* issues are nothing more than tiresome repetition of the same flawed arguments that Prof. Elhauge has already rebutted, in some instances numerous times, or desperate last-minute (and untimely) attacks that reveal a total lack of understanding of the case.

Tyco's claim that Prof. Elhauge is not qualified to offer an opinion in this case is groundless, and ignores: a) Prof. Elhauge's particular expertise in antitrust economics, b) his extensive economic qualifications, and c) his peer-reviewed economic articles, textbooks and service on law and economic advisory boards. Moreover, numerous courts (and the U.S. Congress) have qualified Prof. Elhauge to testify on the very same issues as those involved in this case. Recognizing, as this Court did, that both parties' experts are "highly qualified antitrust titans" engaged in a "robust economic debate,"[1] Plaintiffs chose not to waste this Court's time with a motion to exclude Prof. Ordover. Plaintiffs did not forego a *Daubert* challenge to Prof. Ordover due to a lack of flaws, errors or meritless rejoinders in his report. There are certainly many of those, and many have been repeated in Prof. Ordover's latest declaration. Indeed, Prof. Elhauge has already shown that there are numerous serious problems with Prof. Ordover's report, especially where he attempts to challenge Prof. Elhauge's application of his methodology to the facts of this case. However, Plaintiffs recognize, as does the weight of authority, that such errors

[1] *Natchitoches Parish Hosp. Svc. Dist. v. Tyco Int'l et al.*, 247 F.R.D. 253, 273 (D. Mass. 2008).

and flaws are to be challenged on cross-examination of the expert at a trial on the merits.[2] Tyco, however, filed a baseless motion, used as an excuse to merely rehash the "battle of the experts" which has fully engaged this Court for over a year in this litigation already.

Not only did Tyco include an additional declaration from Prof. Ordover, which supposedly seeks to "clarify and summarize" his earlier report,[3] but far more egregiously, Tyco introduced a completely new expert, Dr. McFadden, into the process many months after expert disclosure and discovery has closed, in open defiance of this Court's scheduling orders and case management prerogatives.[4] Tyco has deliberately muddled the process by forcing Plaintiffs to engage in a second "battle of the experts," simultaneous with the *Daubert* briefing. In addition to being untimely, Dr. McFadden's report is also, as Prof. Elhauge demonstrates, not tied to the particulars of this case and flawed in other ways including basic errors (such as claiming to have run regressions that were not actually done), thus making that report subject to a *Daubert* challenge and exclusion in its own right.

Having no real criticisms of Prof. Elhauge's qualifications or methodologies, and thus no legitimate issues under Rule 702 or *Daubert*, Tyco instead uses large portions of its motion as a soapbox to: 1) lament the result of a two-year old discovery dispute and once again complain that Magistrate Judge Sorokin and this Court incorrectly decided that motion; and 2) improperly

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[2] *Daubert v. Merrell Dow Pharmaceuticals, Inc.,* 509 U.S. 579, 595-96 (1993).

[3] It is not clear where there is any authority for an expert to "clarify and summarize" his expert reports submitted nine months earlier.

[4] Plaintiffs have separately moved for an order striking Dr. McFadden's declaration from the record and for costs under Rule 37(c) (Docket Nos. 190 and 191); however, pending resolution of that motion, Plaintiffs here respond to the opinions contained therein and submit the accompanying declaration of Prof. Elhauge responding to both Prof. Ordover's and Dr. McFadden's new declarations.

attempt to frame legal questions with regard to the state of the law of exclusive dealing (which is alleged in this case) and predatory pricing (which is not). Neither of these issues has any relationship to whether Prof. Elhauge is a qualified expert or to whether his methodology is viable and admissible under *Daubert* standards. As a result, Plaintiffs respectfully request that Tyco's Motion be denied.

## II. ARGUMENT

### A. Prof. Elhauge Is Qualified to Give an Expert Opinion in This Case

Tyco states that Prof. Elhauge is not an expert in the relevant discipline, which it describes variously as "economics", "statistical modeling" and "econometrics", and cites case law supposedly supporting its position that a witness must be qualified in the *specific* subject for which his testimony is offered. In actuality, Tyco has not even correctly identified the "specific subject" of expertise that best qualifies someone in this case. It is in fact, exactly what Prof. Elhauge identifies as his area of expertise: antitrust economics, which he defines as "the application of economic principles and methods to antitrust issues." Elhauge Dep. at 8, *see also* Elhauge Declaration at 99.[5] He testified at his deposition that he considers this discipline to be distinct from economics in general. Dep. at 8. He also qualified his statement that he is not an econometrician by defining that person as someone who "specializes in developing methodologies for [statistical] analysis of economic problems," and stating that he applies

[5] References to the deposition transcript of Prof. Einer Elhauge, dated March 11, 2008, which is attached to the accompanying Declaration of Archana Tamoshunas, are designated as "Elhauge Dep." or "Dep.". "Elhauge Declaration" or "Declaration" refer to the Declaration of Prof. Einer Elhauge, dated November 14, 2008, and filed concurrently with this brief. "Elhauge Report" and "Elhauge Reply" refer to Prof. Elhauge's Expert Report, dated December 18, 2007, and his Reply Report dated February 15, 2008, respectively (Docket Nos. 133 and 135). "Def. Bf." refers to Defendants' Motion to Exclude the Expert Report and Opinions of Prof. Einer Elhauge, filed October 17, 2008.

econometric methods to various issues, but he is not a "scholar who develops methodology in econometrics." Dep. at 9. The *specific* expertise required for this case is the practical application of economic principles to antitrust theory – not the scholarly development of econometric models or expounding on economic theories in general or performing economic tasks for their own sake. Prof. Elhauge proves his expertise, and the appropriateness of his methodology by applying well-recognized methodologies to the particular facts of the case.[6]

Here, in keeping with his area of expertise, Prof. Elhauge has properly applied economics (and some econometrics) to analyze the evidence in this case. Elhauge Declaration at ¶¶99-100. As Prof. Elhauge points out, despite Tyco's dramatic protestations, he applies econometric methods only for his regression analyses, the results of which were already confirmed by extensive non-econometric evidence. Tyco is also wrong that anything but Prof. Elhauge's regressions require econometrics. *Id.* at ¶¶101-103, 105.

The law does not require that one possess a specific educational background in order to be qualified as an expert. As is explicit in Rule 702, and well-settled in the law, an expert's qualifications may be based on "knowledge, skill, experience, training, or education." FED. R. EVID. 702. *See also Zuzula v. ABB Power T&D Co., Inc*., 267 F. Supp. 2d 703, 713 (E.D. Mich. 2003) (a particular degree is "neither necessary nor a sufficient condition for qualification as an expert"). The court must look at the totality of the witness's background and qualifications, not just education. *See Humphrey v. Diamant Boart, Inc.*, 556 F. Supp. 2d 167, 174-75 (E.D.N.Y. 2008).

As Prof. Elhauge states in his declaration, Tyco has ignored all of his qualifications in

[6] Notably, this is something that Dr. McFadden has completely failed to do.

antitrust economics including: a peer-reviewed economics article on loyalty discounts published in the Journal of Competition Law & Economics; several other published antitrust economics articles; peer-reviewed textbooks on antitrust law and economics; being selected as the editor of the *Research Handbook on the Economics of Antitrust Law*; co-authoring a volume of the Areeda antitrust treatise that covered both law and economics of tying; and serving on a number of law and economic advisory boards. Declaration at ¶93. Prof. Elhauge's report to the U.S. Senate, despite Tyco's attempt to cast it as some sort of blight on his record, is a reliable indicator that he is considered one of the foremost experts in the field on the issues directly pertinent to this litigation (as does the fact, despite Tyco's exaggerations, that Elhauge has been consulted by a number of plaintiffs that have challenged exclusionary GPO contracting practices). Def. Bf. at 19-20, n.20. Tyco, of course, has no basis whatsoever to know whether Prof. Elhauge has ever "concluded that a medical device manufacturer did not engage in anticompetitive conduct." *Id.* at 20. While Tyco attempts to imply that Prof. Elhauge only "advocates" for plaintiffs in similar cases (which is not true, *see* Elhauge Declaration at 98), Tyco's expert, Prof. Ordover, who is apparently Tyco's "advocate by choice" (Def. Bf. at 19), has repeatedly testified on behalf of Tyco or provided reports in defense of Tyco's contracting practices in multiple litigations.[7] In fact, despite writing that the type of conduct complained of here could have anticompetitive

[7] *See Daniels Sharpsmart, Inc. v. Tyco Int'l (US) Inc.*, et al, No. 05-cv-169 (E.D. Tex.); *Allied Orthopedic Appliances, Inc. v. Tyco Healthcare Group LP* No. 05-CV-6419 (C.D. Cal.); *Masimo Corp. v. Tyco Health Care Group*, No. CV 02-4770 MRP (C.D. Cal.). If it has any significance, as Tyco suggests it does, as far as Plaintiffs can tell, Prof. Ordover has never testified that any medical device manufacturer has engaged in anticompetitive conduct by entering into exclusionary contracts.

effects, he now, for purposes of litigation, attempts to walk away from those academic writings.[8]

Putting aside Tyco's mischaracterization that Prof. Elhauge "protest[ed] the evils of GPOs," what Elhauge's Senate report actually focuses on is that some GPO contracting practices (the very same type challenged here) could lead to anticompetitive effects[9]; therefore, unlike Prof. Ordover, who appears to have adjusted his opinions for litigation purposes, Prof. Elhauge's non-litigation work as an expert in his field is consistent with the tenor and quality of his analysis here.[10] This is one of the many reasons that his analysis passes muster under *Daubert*. *See Kumho Tire Co., Ltd. v. Carmichael*, 526 U.S. 137, 152 (1999) (the objective of the gatekeeping requirement is "to make certain that an expert, whether basing testimony upon professional

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[8] *See* Elhauge Report at ¶41; Elhauge Reply at ¶¶13-14, citing Ordover & Shaffer, *Economics of Loyalty Rebates: Where Are We Now?* (FTC/DOJ Hearings, Nov. 29, 2006); Ordover & Shaffer, *Exclusionary Discounts*, Working Paper, May 2007; Ordover & Shaffer, *Exclusionary Discounts I* (Aug. 25, 2006); Ordover & Shaffer, *Exclusionary Discounts 3* (Aug. 25, 2006); Ordover & Shaffer, *Exclusionary Discounts 4* (Aug. 25, 2006); Ordover, J & G. Saloner, *Predation, Monopolization and Antitrust*, in R. Schmalensee & R. Willig, eds, Vol. I, HANDBOOK OF INDUSTRIAL ORGANIZATION 537 (North-Holland, Amsterdam 1989).

[9] Elhauge, *The Exclusion of Competition for Hospital Sales Through Group Purchasing Organizations*, June 25, 2002 ("Senate Report") at 1 ("The essential problem is that large incumbent medical device makers have entered or offered exclusionary agreements through GPOs that effectively foreclose member hospitals to rival device makers").

[10] Tyco's twisting of the truth here continues an escalating trend of misleading assertions from Tyco with respect to Plaintiffs' theories and their experts' methodologies. As Plaintiffs and Prof. Elhauge have previously pointed out many times, this case is not about whether or not GPOs are "evil" or whether or not GPOs should or would exist in the but for world. Prof. Elhauge has been most clear that he is not opining that GPOs are the problem. As Prof. Elhauge has stated,

> This is *not* a claim that GPOs themselves are anticompetitive. To the contrary, GPOs are a highly efficient means of brokering medical device sales. The anticompetitive effects arise when GPOs take part in exclusionary agreements, like Tyco's, that have the aggregate effect of impairing rival competition. Thus, it is Tyco's exclusionary contracts *with* GPOs, and not the GPOs themselves, that are anticompetitive.

Elhauge Report at 17. *See also* Senate Report at 40.

studies or personal experience, employs in the courtroom the same level of intellectual rigor that characterizes the practice of an expert in the relevant field").

Tyco also misleads the Court regarding other courts that have qualified Prof. Elhauge as an expert in antitrust economics and have admitted his testimony on the same issues raised in this case. Despite Tyco's claims, no court has held that Prof. Elhauge is not qualified to testify on these issues or as an expert in antitrust economics. Contrary to Tyco's mischaracterizations:

- In *Applied Medical v. Johnson & Johnson*[11], the court never excluded any part of Prof. Elhauge's testimony for being legal in nature or for any other reason. The court issued a general jury instruction indicating that the jury should disregard any opinions from any expert that conflict with instructions on the law. Elhauge Declaration at ¶95.
- In *Masimo v. Tyco*[12], Prof. Elhauge was qualified as an expert and testified on the same types of issues raised in this case, and the jury made a finding of liability against Tyco. In the damages re-trial, the judge determined that his testimony was unnecessary, (but still allowed for rebuttal), since liability had already been determined. *Id.*
- *The Pinal Creek Group v. Newmont Mining Corp.*[13] was not an antitrust case and did not involve any issues of antitrust economics. Prof. Elhauge was permitted to testify as an expert on the transgression of traditional corporate norms in an environmental clean-up case. A few pages related to interpretation of certain past antitrust laws were excluded. The case has no relation to Prof. Elhauge's qualifications to testify in this case. *Id.* at ¶95,

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[11] *Applied Med. Res. Corp. v. J&J, etal.*, SACV-03-1329-JVS (C.D. Cal)

[12] *Masimo Corp. v. Tyco Health Care Group*, No. CV 02-4770 MRP (C.D. Cal.)

[13] *Pinal Creek Group v. Newmont Mining Corp.* 352 F. Supp. 2d 1037, 1046 (D. Ariz 2005)

n. 134.

Indeed, all Tyco has achieved is to provide a list (though not exclusive) of the cases in which federal district courts have qualified Prof. Elhauge as an expert.

### B. Tyco's Selection Bias Arguments Are Wrong and Have Been Repeatedly Rebutted by Prof. Elhauge

#### 1. Tyco's Selection Bias Argument Does Not Reflect Rational Economic Behavior

Tyco has returned to a familiar theme, once again arguing that all of Prof. Elhauge's results are caused by self-selection rather than its own exclusionary contracts. Prof. Elhauge provides numerous reasons why Tyco's selection bias arguments fail. Tyco's claim that the gaps in rival performance shown in Prof. Elhauge's comparisons are explained by self-selection rather than anticompetitive impact makes no sense under the standard economic assumption that actors make rational, profit-maximizing decisions. As Prof. Elhauge points out, if the contracts had no impact on purchasing behavior in the market, that must mean, contrary to rational conduct, that Tyco is "irrationally spending money to secure ineffectual contracts." Declaration at ¶23; *See also* Elhauge Report at ¶199. What purpose do Tyco's contracts serve, and why does Tyco do everything in their power to get buyers to sign on to them, if they have no impact on buyers' purchases? Tyco has no answer. Moreover, as Prof. Elhauge has discussed in his reports, there is an abundance of evidence showing that Tyco considered these contracts to be essential to its success. *See* Elhauge Report at ¶¶119-137.

#### 2. The Longitudinal Novation Study

Tyco's selection bias argument cannot explain Prof. Elhauge's longitudinal Novation study. Declaration at ¶¶24-25, Elhauge Report at ¶196. Furthermore, Prof. Elhauge disproves

Dr. McFadden's conclusion that there was supposedly no significant difference between the rates of rival share growth before and after the Novation sole source contract ended. As Prof. Elhauge explains, Dr. McFadden, despite claiming to be an expert in econometrics, failed to properly run the regression that he proposed. Declaration at ¶¶26-27.[14] In fact, when Dr. McFadden's regressions are run the way he actually proposed to do them, they confirm Prof. Elhauge's conclusions, and show a statistically significant difference between rival growth before and after the contract change at Novation. *Id.* at ¶¶28-29. Prof. Elhauge also shows, using a control group where rivals were not excluded as they were at Novation while it was sole source, that "rivals clearly performed much worse at Novation relative to the control groups when the Novation contract was sole source, and since the Novation contract has become multi-source, the gap between the share at Novation and the control groups has narrowed considerably." *Id.* at ¶¶31, 33 and Ex. 17B.

### 3. The Simultaneous Comparisons

Selection bias cannot explain the simultaneous comparison showing that buyers purchase much less from rivals when their GPO has a sole source contract with Tyco. As Prof. Elhauge has explained, given the thousands of medical and other products that most of these buyers purchase, they do not select their GPO based on the GPO's contracting status on sharps containers. Declaration at ¶34; Elhauge Report at ¶198.

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[14] Whether caused by his last-minute arrival, failure to review the evidence, or general carelessness, Dr. McFadden has made a number of statements and criticisms that are not supported, and in fact contradicted, by his back-up data. He has offered alternate analytic approaches without even bothering to actually carry them out (as noted above) or check whether they would result in the conclusions that he suggests. Elhauge Declaration at ¶67. Moreover, in at least one instance, as Prof. Elhauge has noted, Dr. McFadden has reported in his declaration the opposite conclusion from what his back-up data reveals. *See* Elhauge Declaration at ¶¶84, 88.

Tyco claims that Prof. Elhauge's method for classifying buyers into the burdened and unburdened groups is flawed because he 1) classifies buyers as burdened if they purchased some containers through a sole-source GPO contract (rather than if they had access to a GPO contract) and 2) reassigns a buyer to the unburdened group if it stops purchasing through a sole-source GPO contract. As to the first point, this methodology is not flawed, but in fact the only methodology that makes sense given the claims in this case. Elhauge Declaration at ¶35. As to the second point, Tyco is wrong about what the methodology is. Despite Prof. Elhauge setting the record straight in his Reply Report many months ago, Tyco continues to insist incorrectly that he "reassigns" buyers in this manner. As he explains again in his Declaration, Prof. Elhauge only assigns a buyer to the unburdened group if it did not purchase any containers at all through any sole-source GPO. Declaration at ¶36; Reply at ¶36; Report at ¶¶180-81.

Moreover, it is not correct that he assigned buyers that did not purchase containers through GPOs to the unburdened group. In fact, he did not assign these buyers to either group, as they are not in the market for GPO brokerage services. As he explains, "[this] approach is actually conservative because buyers and rivals do suffer additional anticompetitive harm when buyers must, to buy the rival container they prefer, dispense with the GPO brokerage services that they and rivals would enjoy without the sole source contract." Declaration at ¶36.

Tyco asserts that buyers should be classified according to whether they have access to GPO contracts. Prof. Elhauge explains why Tyco's "access" approach makes no sense.

> First, Tyco's 'access' approach is inferior because actual contractual status, not 'access' to such contracts, is what produces the anticompetitive impact. The relevant issue in this case is how the challenged exclusionary commitments affected the choices made by buyers or GPOs subject to those commitments. The anticompetitive effect flows from the fact that rivals lost sales when buyers or GPOs

> made exclusionary commitments to Tyco. There is no anticompetitive effect when rivals lost sales to buyers or GPOs that made no exclusionary commitment, but had 'access' to a chance to do so. Focusing on whether buyers had access to the challenged contracts would thus be economically incorrect and fail to test the relevant anticompetitive theory.
>
> My approach was thus economically proper because it was designed to assess the impact the challenged exclusionary terms had on rival sales to buyers who were purchasing under contracts with those exclusionary terms. The anticompetitive effects arise from the fact that the exclusionary terms of the contracts themselves restricted the choices of buyers who bought under those contracts. There is no anticompetitive effect on rival sales to buyers who do not purchase under such exclusionary contracts but were offered the chance to do so. Therefore, to measure the exclusionary effects that the terms of the contracts themselves have, it is plainly necessary to classify buyers based on the terms the contracts through which they actually purchased. Any alternative means of classification would not focus on the effect of exclusionary contracts, and thus would distract attention from the relevant issues at stake in this case.

Declaration at ¶¶59-60.

Prof. Elhauge further explains that, even if one used the "access" approach advocated by Tyco and its experts (using the definition of "access" that Tyco suggests – affiliation with a GPO that has a sole-source contract or offers buyer commitment contracts), it would show an ***even larger impact*** on rival sales. *Id.* at ¶67; *see also* ¶¶69, 71, 73. Again, even when Tyco's criticisms have been completely rebutted and shown to be false, it continues to suggest "fixes" for Prof. Elhauge's purported "errors." However, even those "fixes" lead to the unmistakable conclusion that Tyco's conduct caused significant anticompetitive impact.

#### 4. *Ex Ante* Competition and Purchasing Outside GPOs

Tyco's arguments about why its sole source contracts are not exclusionary also have nothing to do with Prof. Elhauge's methods. As it has done throughout the litigation, Tyco simply assumes away the claims, and then pretends it is a criticism of the methodology. Tyco

will have its opportunity to litigate whether or not its conduct was illegal, but that is a determination to be made at trial. Even if the issues of *ex ante* competition and some buyers purchasing outside of GPOs were relevant to the analysis of the anticompetitive effects of exclusionary contracts, Prof. Elhauge has already rebutted these points. *See* Elhauge Reply at ¶¶41-46, 138-43; Declaration at ¶38 ("my reply report showed that effective ex ante competition for GPO sole source contracts did not exist, would not alter the foreclosing effect even if it did, and did not generate any procompetitive benefits"). More importantly, this Court has already held that there is an issue of fact as to the existence of *ex ante* competition for placement on GPO contracts. Memorandum and Order, August 29, 2008, at 23. Moreover, Prof. Elhauge has also shown that the ability of buyers to purchase outside of GPOs is not relevant to whether GPO brokerage services were foreclosed, since those buyers are not in the GPO brokerage services market. Reply at ¶49; Declaration at ¶38.

**5. The Regressions**

Despite numerous new flawed arguments disputing Prof. Elhauge's regressions, selection bias cannot explain the regressions that show that the same set of buyers whose contract status changed bought far less from rivals when they were subject to an exclusionary contract than when they were not. Elhauge Report at ¶¶188-92; Declaration at ¶40. Tyco argues here that, rather than showing that the change in contract precipitates the change in purchasing behavior, this instead shows that a buyer's purchasing preferences always coincidentally change at the same time that its contract status changes. This is particularly ridiculous, especially when one considers that it is the GPOs that decide when the contract status will change. Elhauge Declaration at ¶¶42-43. As Prof. Elhauge explains, "[n]or is it plausible that buyer preferences

radically shifted every time their commitment contracts ended and they were able to switch to a rival, but never shifted during the period of any commitment contract." *Id.* at ¶42. As he has shown, this claim is also rebutted by direct evidence. Elhauge Report at ¶¶132, 134, 176, 173-74.

Tyco's criticisms of Prof. Elhauge's classification of buyers into the burdened and unburdened categories also must fail, because as he has explained many times, he included all buyers with commitment contracts in the burdened category, even when they did not comply with those commitments in those contracts. Elhauge Report at ¶180, Reply at ¶¶86-87. Moreover, even if Tyco were correct that "purchasing pattern determines" contract status (and there is no evidence of this), Prof. Elhauge has shown that his results would not significantly change even if he never reclassified buyers who stopped buying from Tyco. Declaration at ¶46.

Dr. McFadden's criticism that Prof. Elhauge should have used linear regressions instead of logarithmic regressions ignores the fact that Prof. Elhauge's method actually avoids selection bias by focusing on buyers that purchased from both Tyco and rivals. Elhauge Declaration at ¶¶48-49. Further, as Prof. Elhauge explains,

> Professor McFadden's alternative linear regression makes the fundamental error of including every buyer who bought 0% from rivals without also including thousands of observations from buyers who bought 0% from Tyco. This error biases his linear regressions against finding any effect from the challenged contracts. When the error is corrected, the linear regression strongly confirms all of my conclusions.

*Id.* at ¶48. Prof. Elhauge goes on to explain in detail each of the fundamental mistakes that Prof. McFadden made and discusses why Prof. Elhauge's logarithmic regression is superior for this purpose to Dr. McFadden's linear regression. *Id.* at ¶49. Prof. Elhauge also explains why it is wrong to use a fixed effects model in this case because such an application would "essentially

drop from the analysis *all* buyers that either (1) consistently were unburdened by the exclusionary contracts; or (2) consistently were burdened by the exclusionary contracts." *Id.* at ¶55. Prof. Elhauge also shows that, even using the fixed effects model, it does not alter his conclusions. *Id.* at ¶56, Table 1B, Table 1C.[15]

### C. Buyers' Subjective Preferences Are Not Relevant to the Theory of Harm in This Case

Tyco spends a large portion of its brief complaining about and attempting to re-argue a discovery dispute that Magistrate Judge Sorokin decided over two years ago, when Tyco impermissibly sought to take numerous depositions of absent class members, and arguing again that this Court was wrong to affirm that order.[16] Tyco has inserted a similarly misplaced grievance into a number of its filings on other issues, continuing long after discovery closed. Notwithstanding Tyco's obsession with attempting to connect that discovery order to every subsequent event in the case, there is absolutely no connection between the denial of Tyco's discovery motion and the admissibility of Prof. Elhauge's testimony.

As Plaintiffs have maintained throughout this litigation, subjective consumer preferences are not relevant to the theory of harm in this case. Furthermore, to the extent that purchasing behavior is relevant here, the proper and only reliable way to assess it is through analysis of the

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[15] Tyco also claims that Prof. Elhauge should have controlled for relative prices at burdened and unburdened buyers. This argument again ignores the fundamental nature of the claims in this case. It is Tyco's anticompetitive conduct itself that determined the prices paid by customers, thus obviating any utility from controlling for prices in the analysis. Elhauge Declaration at ¶75.

[16] Ignoring this Court's order, Tyco has attempted to nonetheless inject purchaser testimony into this case by providing an unsupported characterization of testimony from another litigation into this case. Def. Bf. at 8, n. 6. Tyco's pronouncement about what discovery supposedly revealed in *Daniels Sharpsmart, Inc. v. Tyco Int'l (US) Inc., et al*, No. 05-cv-169 (E.D. Tex.), is inappropriate and inadmissible here.

sales data in the market. As Prof. Elhauge explained, hospital purchasing preferences should be determined "from actual market decisions," which are revealed by actual purchase data, "rather than by a direct inquiry into their preferences." Elhauge Dep. at 138. "[A]s a matter of economics, we are better off relying on revealed preferences rather than on survey sorts of evidence; and here, the revealed preferences show that these hospitals do buy a much higher share from rivals in the portions of the market that aren't burdened." *Id.* at 139. "[T]he best evidence that I'm basing my analysis on is the statistical evidence of . . . what choices hospitals make when burdened versus unburdened." *Id.* at 140. As Prof. Elhauge points out, rather than asking questions to get the subjective feelings of a handful of purchasers regarding sharps containers, the correct economic methodology is to do what he did, and to examine the sales data, which reveals the actual purchasing decisions of all purchasers in the market. With respect to each purchaser, the proper methodology is to rely on the "actual evidence of its behavior" rather than "what it says about its preferences." *Id.* at 141. *See also id.* at 142 (the data is a "survey of [hospitals'] actual transactions" not a "survey of what they say about their preferences").

### D. Tyco's Attempts To Argue the Legal Standards Under Which Its Conduct Will Be Judged Are Incorrect, Misplaced and Inappropriate In a *Daubert* Analysis

Tyco also uses its brief as an opportunity to create more distraction by attempting to argue the legal framework for determining whether Tyco has violated the antitrust laws. As Prof. Ellhauge has made quite clear, his methodology is aimed at determining whether Tyco's conduct has caused anticompetitive effects, and he is not offering any legal opinions on whether Tyco's conduct is illegal. Yet Tyco makes the nonsensical argument that Prof. Elhauge's analysis cannot be admitted in this case because the "theories underlying his opinions are incompatible

with the weight of antitrust jurisprudence and scholarship." Def. Bf. at 17.

Tyco has fabricated a *Daubert* issue here, when it is really using the opportunity as an excuse to argue unrelated questions about to the state of the law on whether Tyco's conduct is illegal. As with many of its prior submissions, Tyco's primary argument appears to be that it has not done anything illegal. This is a question for the trier of fact to determine. It has nothing to do with the experts' methodologies, and the legal standard to be applied to the conduct in this case is not an issue to be determined in a *Daubert* proceeding. Tyco attempts a tenuous connection by suggesting that Prof. Elhauge is somehow advocating a particular rule of law. He has done no such thing. As is clear from his reports and as he stated during his deposition, he is not offering any legal conclusions in this case. *See* Dep. at 29, 61.

The fact that Tyco wishes evidence of below-cost pricing was required in an exclusive dealing case is absolutely irrelevant to both (a) whether Prof. Elhauge meets the standards of *Daubert*, and (b) the actual state of the law – which is far different from the framework Tyco advocates. Even if it were somehow relevant to a *Daubert* analysis, Tyco's recitation of the law, and its statement that "courts have repeatedly required evidence of below-cost pricing before condemning discounting arrangements," (Def. Bf. at 18) is not dispositive of any issue in this case, nor is it even relevant since this case is not about predatory pricing or "discounting arrangements." This Court has already recognized that, "the theories that support the Plaintiffs' claim of antitrust injury are. . . not 'novel,'" and noted numerous examples of how similar exclusive dealing arrangements can give rise to anticompetitive injury. Memorandum and Order, August 29, 2008, at 12-13.

Furthermore, Prof. Elhauge has cited numerous sources of peer-reviewed economic

scholarship that support his economic theories (Elhauge Declaration at ¶¶107, 111-14; Report at ¶¶26-37), as well as economic literature on loyalty discounts explicitly rejecting a cost-based test. Elhauge Declaration at ¶117. As Prof. Elhauge states,

> The fact that the loyal price exceeds costs does not eliminate the anticompetitive effect; it makes it all the greater. Unlike with predatory pricing, what causes the anticompetitive effect from loyalty discounts is *not* low prices, but the *exclusionary conditions* attached to price differences.
>
> ****
>
> [A] cost-based test would perversely exempt the *most* anticompetitive form of loyalty pricing, namely charging penalty prices to get buyers to agree to loyalty contracts at supracompetitive prices that are above but-for levels, and thus necessarily above cost.

Elhauge Declaration at ¶115 (emphasis in original).

Prof. Elhauge has shown that scholarship in the field of antitrust economics supports his theories and methodologies, and that he has applied those methodologies correctly while considering all the evidence in this particular case. This is more than sufficient for the purposes of determining that his testimony is admissible. *See, e.g., Ruiz-Troche v. Pepsi Cola of Puerto Rico Bottling Co.*, 161 F.3d 77, 85 (1st Cir. 1998) ("*Daubert* neither requires nor empowers trial courts to determine which of several competing scientific theories has the best provenance. It demands only that the proponent of the evidence show that the expert's conclusion has been arrived at in a scientifically sound and methodologically reliable fashion"). If Tyco wants to argue over the proper legal standards to apply in this case, or whether it has done anything that violates the antitrust laws, a *Daubert* motion is not the proper vehicle, and such an argument has no relevance to the admissibility of Prof. Elhauge's testimony.

## III. CONCLUSION

For the foregoing reasons, and for the reasons stated in Prof. Elhauge's accompanying

Declaration, Plaintiffs respectfully request that the Court deny Tyco's motion to exclude Prof. Elhauge's report and opinions.

Dated: November 14, 2008

Respectfully submitted,

**/s/ Archana Tamoshunas**
Bruce E. Gerstein (*pro hac vice*)
Brett Cebulash (*pro hac vice*)
Archana Tamoshunas (*pro hac vice*)
GARWIN GERSTEIN & FISHER LLP
1501 Broadway, Suite 1416
New York, NY 10036
(212) 398-0055

Thomas G. Shapiro BBO #454680
Adam Stewart BBO #661090
SHAPIRO HABER & URMY LLP
53 State Street
Boston, MA 02109
(617) 439-3939

ODOM & DES ROCHES, L.L.P.
John Gregory Odom
Stuart E. Des Roches
Andrew Kelly
Suite 2020, Poydras Center
650 Poydras Street
New Orleans, LA 70130
(504) 522-0077

THE SMITH FOOTE LAW FIRM, L.L.P.
David P. Smith
720 Murray Street
P.O. Box 1632
Alexandria, LA 71309
(318) 445-4480

BERGER & MONTAGUE, P.C.
Daniel Berger
Eric L. Cramer
David Sorensen
Keith Verrier

1622 Locust Street
Philadelphia, PA 19103
(215) 875-3000

KOZYAK TROPIN & THROCKMORTON, P.A.
Adam Moskowitz
Tucker Ronzetti
2525 Ponce de Leon, 9th Floor
Coral Gables, FL 33155
(305) 372-1800

LAW OFFICE OF ALFRED G. YATES JR. PC
Alfred G. Yates, Jr.
519 Allegheny Building
429 Forbes Avenue
Pittsburgh, PA 15219
(412) 391-5164

BERGER SINGERMAN, P.A.
Mitchell W. Berger
Rene Harrod
350 Las Olas, Suite 1000
Fort Lauderdale, FL 33301
(954) 525-9900

HANGLEY ARONCHICK SEGAL & PUDLIN
Steve D. Shadowen
30 North Third Street, Suite 700
Harrisburg, PA 17101
(717) 364-1030

SCHIFFRIN, BARROWAY, TOPAZ & KESSLER, LLP
Joseph H. Meltzer
John Gross
280 King of Prussia Road
Radnor, PA 19087

**CERTIFICATE OF SERVICE**

I hereby certify that this document(s) filed through the ECF system will be sent electronically to the registered participants as identified on the Notice of Electronic Filing (NEF) and paper copies will be sent to those indicated as non registered participants on November 14, 2008.

**/s/ Archana Tamoshunas**
Archana Tamoshunas