IN THE MATTER OF

TECH SPRAY, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3377. Complaint, Mar. 25, 1992--Decision, Mar. 25, 1992

This consent order prohibits, among other things, a Texas corporation and its owner from making false and unsubstantiated environmental claims in the marketing of any product. In addition, the order requires respondents to maintain, for three years, all materials relied upon to substantiate any representations, and for a copy of the order to be distributed to each operating division.

Appearances

For the Commission: *Michael Dershowitz* and *Mary Koelbel Engle.*

For the respondents: *Robert D. Forrester, Gibson, Ochsner & Adkins*, Amarillo, TX.

COMPLAINT

The Federal Trade Commission, having reason to believe that Tech Spray, Inc., a corporation, and Richard Russell, individually and as officer of said corporation ("respondents"), have violated the provisions of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, alleges:

PARAGRAPH 1. Respondent Tech Spray, Inc. ("Tech Spray") is a Texas corporation with its office and principal place of business at 88 North Hughes Street, Amarillo, Texas.

Respondent Richard Russell is an officer of Tech Spray. He formulates, directs, and controls the acts and practices of Tech Spray. His business address is the same as that of Tech Spray.

The aforementioned respondents cooperate and act together in carrying out the acts and practices hereinafter set forth.

PAR. 2. Respondents have advertised, offered for sale, sold, and distributed certain electronic equipment cleaning products containing the chemicals chlorofluorocarbons ("CFCs"), 1,1,1- trichloroethane, and/or hydrochlorofluorocarbons ("HCFCs") to the public, including but not limited to Blue Shower, Flux Stripper OF, Instant Chiller, Precision Duster, and Kleen-All ("respondents' products").

PAR. 3. The acts and practices of respondents alleged in this complaint have been in or affecting commerce, as commerce is defined in the Federal Trade Commission Act.

PAR. 4. Respondents have disseminated or have caused to be disseminated advertisements, including product labeling, and other promotional materials for respondents' products, including, but not necessarily limited to, the attached Exhibits A and B.

The product labeling on the caps of the Blue Shower (Exhibit A) and Instant Kleen-All cans includes the following statement:

Ozone Friendly Formula

The product labeling on the front of the Precision Duster and Instant Chiller cans (Exhibit B) includes the following statement:

OZONE FRIENDLY

PAR. 5. Through the statements referred to in paragraph four in product labeling (Exhibits A and B), respondents have represented, directly or by implication, that there are no ingredients in respondents' products that deplete the earth's ozone layer.

PAR. 6. Respondents have disseminated or have caused to be disseminated advertisements for respondents' products, including, but not necessarily limited to, the attached Exhibit C.

The aforesaid product labeling on the cap and the can of Flux Stripper OF (Exhibit C) includes the following statements:

Ozone Friendly Formula [cap]
CFC Free [can]

PAR. 7. Through the statements referred to in paragraph six in product labeling (Exhibit C), respondents have represented, directly or by implication, that because respondents' product contains no CFCs, it will not deplete the earth's ozone layer.

PAR. 8. Respondents have disseminated or have caused to be disseminated print advertisements for respondents' products, including, but not necessarily limited to, the attached Exhibit D.

The aforesaid print advertisement (Exhibit D) includes the following statements:

The Best Reason For Our Ozone-Friendly Products.

Because we take our responsibility to future generations seriously, Tech Spray has introduced a line of high performance Ozone-Friendly products. Tech Spray's Ozone-Friendly products have ozone depletion potential levels lower than those specified by the Montreal Protocol or current EPA guidelines.
... Tech Spray will continue to develop efficient and environmentally safe solutions to meet tomorrow's needs. Not only do Tech Spray's new Ozone-Friendly products help protect the environment, but they provide the same level of product quality and efficiency you have come to expect from the leading manufacturer of electronic production and field service chemicals.

PAR. 9. Through the statements referred to in paragraph eight in advertising (Exhibit D), respondents have represented, directly or by implication, that respondents' products are environmentally safe, do not pose a significant adverse risk to the environment or the ozone layer, and contain levels of ozone-depleting chemicals lower than those specified for products by the Montreal Protocol and EPA guidelines.

PAR. 10. In truth and in fact, respondents' products contain harmful ozone-depleting chemicals -- CFCs, 1,1,1-trichloroethane, or HCFCs -- which contribute to the depletion of the earth's ozone layer; the Montreal Protocol and EPA guidelines do not specify ozone-depletion potential levels that products may contain; and respondents' products, though they have lower ozone-depletion potentials than they did before they were reformulated, still consist primarily of ozone-depleting chemicals. Therefore, the representations set forth in paragraphs five, seven, and nine were, and are, false and misleading.

PAR. 11. Through the statements and representations referred to in paragraphs five, seven, and nine respondents have represented,

directly or by implication, that at the time they made such representations, respondents possessed and relied upon a reasonable basis for such representations.

PAR. 12. In truth and in fact, at the time respondents made such representations, respondents did not possess and rely upon a reasonable basis for such representations. Therefore, the representation set forth in paragraph eleven was, and is, false and misleading.

PAR. 13. The acts and practices of respondents as alleged in this complaint constitute unfair or deceptive acts or practices in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act.

EXHIBIT A

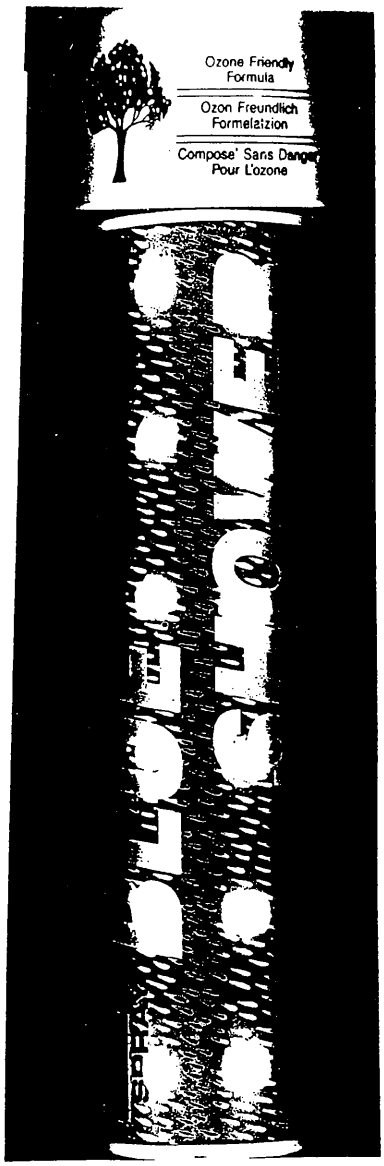


EXHIBIT A

EXHIBIT B


96
ZONE FRIENDLY
Thermal Intermittents
CAUTION: CONTENTS UNDER PRESSURE

433

EXHIBIT C

EXHIBIT D

The Best Reason For Our Ozone Friendly Products.

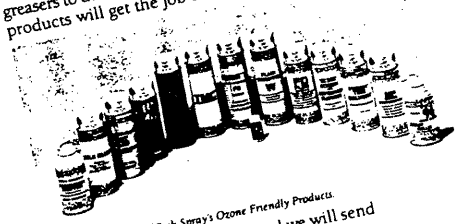
Because we take our responsibility to future generations seriously, Tech Spray has introduced a line of high performance Ozone-Friendly products.

Tech Spray's Ozone-Friendly products have ozone depletion potential levels lower than those specified by the Montreal Protocol or current EPA guidelines.

And this is only the beginning. Tech Spray will continue to develop efficient and environmentally safe solutions to meet tomorrow's needs.

Not only do Tech Spray's new Ozone-Friendly products help protect the environment, but they provide the same level of product quality and efficiency you have come to expect from the leading manufacturer of electronic production and field service chemicals.

The reformulation of these products has not altered their effectiveness, safety or odor. From cleaners and degreasers to dusting gas and freeze sprays, these products will get the job done.



These are just some of Tech Spray's Ozone Friendly Products.

See for yourself. Simply call and we will send you free information and samples of the new Tech Spray Ozone-Friendly products.

TECH SPRAY

Chemically Engineered Solutions ...
Solutions For Your Problems.

P.O. Box 949 ■ Amarillo, TX 79105-9935
Phone: (806) 372-8523 ■ Toll-Free: (800) 858-4043
In TX: (800) 692-4677 ■ Fax: (806) 372-8750

Tech Spray (EC) LTD
55 East Parade ■ Harrogate HG1 5LQ
North Yorkshire ■ England
Phone 0423-520699
Fax 0423-504630

EXHIBIT I

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the above caption, and the respondents having been furnished thereafter with a copy of a draft complaint which the Bureau of Consumer Protection proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft complaint, a statement that the signing of the agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings, and enters the following order:

1. Respondent Tech Spray, Inc. ("Tech Spray") is a Texas corporation with its office and principal place of business at 88 North Hughes Street, Amarillo, Texas. Respondent Richard Russell is an officer of Tech Spray. He formulates, directs, and controls the acts and practices of Tech Spray, and his principal office and place of business is located at the above address.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

DEFINITIONS

For purposes of this order, the following definitions shall apply:

"*Class I ozone-depleting substance*" means a substance that harms the environment by destroying ozone in the upper atmosphere and is listed as such in Title 6 of the Clean Air Act Amendments of 1990, Pub. L. No. 101-549, and any other substance which may in the future be added to the list pursuant to Title 6 of the Act. Class I substances currently include chlorofluorocarbons, halons, carbon tetrachloride, and 1,1,1-trichlorethane.

"*Class II ozone-depleting substance*" means a substance that harms the environment by destroying ozone in the upper atmosphere and is listed as such in Title 6 of the Clean Air Act Amendments of 1990, Pub. L. No. 101-549, and any other substance which may in the future be added to the list pursuant to Title 6 of the Act. Class II substances currently include hydrochlorofluorocarbons.

I.

It is ordered, That respondents Tech Spray, Inc. ("Tech Spray"), a corporation, its successors and assigns, and its officers, and Richard Russell, individually and as an officer of said corporation, and respondents' representatives, agents, and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the advertising, labeling, offering for sale, sale, or distribution of any product, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from representing that any such product containing any Class I or Class II ozone-depleting substance is "ozone friendly," "ozone safe," or, by words, depictions, or symbols representing directly or by implication that any such product will not deplete, destroy, or otherwise adversely affect ozone in the upper atmosphere.

II.

It is further ordered, That respondents Tech Spray, a corporation, its successors and assigns, and its officers, and Richard Russell, individually and as an officer of said corporation, and respondents' representatives, agents, and employees, directly or through any corporation, subsidiary, division, or other device, in connection with the advertising, labeling, offering for sale, sale, or distribution of any product, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from representing, directly or by implication, by words, depictions, or symbols, that any product offers any environmental benefit, unless at the time of making such representation, respondents possess and rely upon competent and reliable scientific evidence that substantiates such representation. To the extent such evidence consists of scientific or professional tests, analyses, research, studies, or any other evidence based on expertise of professionals in the relevant area, such evidence shall be "competent and reliable" only if those tests, analyses, research, studies, or other evidence are conducted and evaluated in an objective manner by persons qualified to do so, using procedures generally accepted by others in the profession to yield accurate and reliable results.

III.

It is further ordered, That for three years from the date that the representations to which they pertain are last disseminated, respondents shall maintain and upon request make available to the Federal Trade Commission for inspection and copying:

A. All materials relied upon to substantiate any representation covered by this order; and

B. All tests, reports, studies, surveys, or other materials in respondents' possession or control that contradict, qualify, or call into question such representation or the basis upon which respondents relied for such representation.

IV.

It is further ordered, That the corporate respondent shall distribute a copy of this order to each of its operating divisions and to each of its officers, agents, representatives, or employees engaged in the preparation and placement of advertisements, promotional materials, product labels, or other such sales materials covered by this order.

V.

It is further ordered, That the corporate respondent shall notify the Commission at least thirty (30) days prior to any proposed change in the corporation such as a dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries, or any other change in the corporation which may affect compliance obligations under this order.

VI.

It is further ordered, That the individual respondent shall promptly notify the Commission in the event of the discontinuance of his present business or employment and of each affiliation with a new business or employment. In addition, for a period of five (5) years from the date of service of this order, he shall promptly notify the Commission of each affiliation with a new business or employment whose activities include the sale, distribution, and/or manufacturing of industrial cleaning or degreasing products or of his affiliation with a new business or employment in which his own duties and responsibilities involve the sale, distribution, and/or manufacturing of industrial cleaning or degreasing products. Each such notice shall include the individual respondent's new business address and a statement of the nature of the business or employment in which such respondent is newly engaged, as well as a description of such respondent's duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

VII.

It is further ordered, That respondents shall, within sixty (60) days after service of this order upon them, and at such other times as the Commission may require, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

IN THE MATTER OF

U.S. PIONEER ELECTRONICS CORP.

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT AND ORDER TO SHOW CAUSE

Docket C-2755. Consent Order, Oct. 24, 1975--Modifying Order and Order to Show Cause, April 8, 1992

This order reopens the proceeding and modifies, in part, the Commission's consent order issued in 1975 [86 FTC 1002], by allowing the company to withhold cooperative advertising allowances from dealers and to unilaterally terminate dealers who have advertised its products at prices other than those suggested by the company. In addition, the Commission ordered the respondent to show cause why additional modification to paragraph I.10. should not be made.

ORDER GRANTING IN PART AND DENYING IN PART REQUEST TO REOPEN AND MODIFY ORDER ISSUED OCTOBER 24, 1975, AND ORDER TO SHOW CAUSE

Pioneer Electronics (USA) Inc., the successor corporation to U.S. Pioneer Electronics ("Pioneer"), has filed a "Petition to Reopen Proceedings and to Modify Consent Order ("Petition")[1] in Docket No. C-2755, pursuant to Section 5(b) of the Federal Trade Commis-sion Act, 15 U.S.C. 45(b), and Section 2.51 of the Commission's Rules of Practice and Procedure, 16 CFR 2.51. Pioneer asks the Commission to reopen and modify the consent order issued by the Commission on October 25, 1975 ("order"), *U.S. Pioneer Electronics Corp.*, 86 FTC 1002 (1975). The order was previously reopened by the Commission on November 5, 1982, 100 FTC 526 (1982), pursuant to an order to show cause and modified on March 18, 1983, 101 FTC 372 (1983).[2]

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[1] Pioneer submitted a Memorandum in Support of Petition to Reopen Proceedings and to Modify Consent Order ("Petition Memo") with its Petition.

[2] The Commission modified paragraph I.11. to allow Pioneer to prevent transshipment of its products to outlets that do not provide adequate point of sale promotions and service.

Pioneer asks the Commission to set aside and modify several provisions contained in paragraph I of the order, each of which limits Pioneer's ability to impose restrictions on its dealers' advertised prices in connection with the sale of consumer electronics products. In support of its Petition, Pioneer argues that the modifications are warranted by changed conditions of law and fact, and by the public interest. Pioneer's Petition was placed on the public record for thirty days, pursuant to Section 2.51 of the Commission's Rules. No public comments were received.

For the reasons discussed below, the Commission has determined that Pioneer has not shown that changed conditions of law or fact require reopening the order but that Pioneer has demonstrated that it is in the public interest for the order to be reopened and modified in part. The Commission has, therefore, reopened and modified the order. Also, pursuant to Section 3.72 of the Commission's Rules, the Commission is issuing an Order to Show Cause why it is not in the public interest for the Commission to modify the order further to remove restrictions regarding Pioneer's ability to terminate a dealer who does not comply with suggested resale prices.

I.

The Complaint and Order

The complaint in this case alleged that Pioneer violated Section 5 of the Federal Trade Commission Act, 15 U.S.C. 45, by engaging, in combination with its dealers, in courses of action to unlawfully fix, establish, stabilize or maintain the suggested retail prices at which its products were resold.[3] The complaint listed seven specific acts and practices in which Pioneer engaged in "furtherance of" those courses of action, including, for example, establishing agreements, under-

[3] At about this same time, the Commission issued a number of similar vertical price fixing complaints and orders against Pioneer's competitors. *See United Audio Products, Inc.*, C-2828, 88 FTC 24 (1976); *Nikko Electronic Corporation of America*, C-2829, 88 FTC 31 (1976); *Sansui Electronics Corporation*, C-2754, 86 FTC 995 (1975); *Sherwood Electronic Laboratories, Inc.*, C-2753, 86 FTC 988 (1975); *TEAC Corporation of America*, C-2752, 86 FTC 981 (1975).

standings, or arrangements with its dealers, as a condition precedent to granting or retaining a dealership, that such dealers will maintain certain resale or retail prices, and soliciting and obtaining its dealers' cooperation and assistance in identifying and reporting any dealer who advertises, offers to sell, or sells products at prices lower than certain resale prices, 86 FTC at 1003. The order prohibits Pioneer, its successors and assigns, from engaging in any of twelve specified acts and practices related to vertical price fixing. *Id.* at 1005-6. Pioneer consented to the Commission's order.

II.

Pioneer's Petition

The prohibitions at issue in the Petition relate to the advertising restrictions in paragraphs I.2., I.5., I.6., I.8., and I.10. of the order. Specifically, Pioneer requests the Commission to delete paragraph I.6.[4] (which refers to cooperative advertising restrictions) and modify

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[4] Paragraph I.6. prohibits Pioneer from:

> Threatening to withhold or withholding earned cooperative advertising credits or allowances from any dealer because said dealer advertises respondent's products at retail prices other than that which respondent deems appropriate or has approved.

paragraphs I.2., I.5., I.8., and I.10.[5] by removing all other advertising restrictions.

Pioneer argues that the relief it is seeking is required by changed conditions of law and fact, and by the public interest. Pioneer asserts that Minimum Advertising Price ("MAP") programs prohibited by the order "are not by themselves agreements to fix prices. Instead they are merely 'fencing-in' provisions. As long as there is no resale price maintenance behavior, and there cannot be given the clear case law from the Supreme Court as well as the provisions of the order which remain in effect, these 'fencing-in' provisions are no longer necessary." Petition Memo at 15. Pioneer asserts that under decisions rendered by the Supreme Court and the Commission since entry of the order in 1975, non-price vertical restrictions are to be governed by the rule of reason, and are no longer considered *per se* violations of the law.

Pioneer states that the requested modifications are necessary because it is "one of only a few manufacturers in the home electronics industry that cannot adopt" MAP programs, *i.e.*, Pioneer cannot compete on a level playing field. That unequal playing field

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[5] Pioneer requests that the Commission delete the bracketed words from the following order paragraphs. Paragraph I.2.:

> Fixing, establishing, controlling or maintaining the prices at which dealers may [advertise, promote, offer for sale or] sell respondent's products.

Petition at 1. Paragraph I.5.:

> Refusing to sell or threatening to refuse to sell to any dealer who desires to engage in the sale of respondent's products for the reason that such dealer will not enter into an understanding or agreement with respondent to [advertise or] sell said products at respondent's established or suggested retail price.

Petition at 2. Paragraph I.8.:

> Securing or attempting to secure any promises or assurances from dealers or prospective dealers regarding the prices at which such dealers will [advertise or] sell respondent's products [or requesting or requiring any dealer or prospective dealer to obtain approval from respondent for prices offered by said dealers in advertisements for respondent's products].

Petition at 2-3. Paragraph I.10.:

> Terminating, threatening, intimidating, coercing, delaying shipments, or taking any other action to prevent the sale of respondent's products by a dealer because said dealer has [advertised or] sold, is [advertising or] selling, or is suspected of [advertising or] selling such products at other than prices that respondent may deem to be appropriate or has approved.

Petition at 3.

impairs interbrand competition by disadvantaging Pioneer when competing for dealers because dealers find Pioneer brands less profitable than those of manufacturers with MAP programs, and damaging competition for consumers because the public "often forms an incorrect impression of the quality of Pioneer products because the advertised Pioneer price is often well below the advertised price of the comparable product . . ., though the actual sales prices for the products are nearly the same." Petition Memo at 7.

Pioneer states that dealers must invest a large amount of money, space and resources when adding a new brand of electronics for sale. These investments will only be made if "there is a reasonable assurance of a profitable, long term relationship with the new supplier." Petition Memo at 8. This relationship depends upon getting consumers to the store. In the electronics field, that is done predominantly through advertising.

Pioneer claims that the use of "blow-out" advertisements -- advertisements of well-known products that are offered near dealer cost to build store traffic -- destroys the attractiveness of Pioneer as a product line for "virtually all dealers." Petition Memo at 9. As a result, Pioneer alleges, "dealers either refuse to carry Pioneer or simply do not carry it in quantities or promote it as heavily as competing products which have MAP programs." *Id.* Retailers are harmed by the low advertised prices because the customers "will" buy the products at the stores with the lower price, whether or not another retailer would have matched the price, and customers may decide that the higher priced retailer is not competitive generally and refuse to shop there. Petition Memo at 10.

Pioneer states that MAP programs are especially important for "'high-end' 'big ticket' products" such as projection televisions because of the greater need for retailer investment in sales and service training. Petition Memo at 10. Pioneer also cites the lack of MAP programs as harming its ability to distribute through "channels of trade other than retail dealers." *Id.* The only different retail channel Pioneer discusses is a nation-wide catalog distributed thrice yearly. The catalog chooses to limit the Pioneer products it carries to "step-up" products because they are less often "blow-out" advertisement targets.

Pioneer also claims that "controlling advertising prices allows a manufacturer to position and promote high-end products properly and to introduce new products." Petition Memo at 11. Pioneer states that a damaged reputation in the electronics industry is especially difficult to rehabilitate because of the constant inflow of entirely new products onto the market. Pioneer and its customers have been harmed the most because, Pioneer alleges, it is a leading innovator in the home electronics industry and it "has lost many sales and its reputation as a high quality innovator has been seriously damaged by advertisements of these new products at prices at, or below, dealer cost." *Id.* As a result, dealers will shy away from investing in the products and, Pioneer claims, customers ultimately will be harmed. Finally, Pioneer notes that the "inconsistent treatment of manufacturers is magnified by the fact that consumers are not aware of the unlevel field." Petition Memo at 13. Consumers, therefore, incorrectly conclude that Pioneer products are "lower quality or less technologically sophisticated" when they see them advertised at only sales prices. Petition Memo at 13 (citing affidavit of Mark Smith, Senior Manager, Planning and Coordination, for the Home Electronics Division of Pioneer ("Smith Aff.") at ¶9 and ¶10).

III.

Standards for Reopening and Modification

Section 5(b) of the FTC Act, 15 U.S.C. 45(b), provides that the Commission shall reopen an order to consider whether it should be modified if the respondent "makes a satisfactory showing that changed conditions of law or fact" require such modification. A satisfactory showing sufficient to require reopening is made when a request to reopen identifies significant changes in circumstances and shows that the changes eliminate the need for the order or make continued application of it inequitable or harmful to competition. *Louisiana-Pacific Corp.*, Docket No. C-2956, Letter to John C. Hart (June 5, 1986), at 4.

The Commission may also modify an order pursuant to Section 5(b) when, although changed circumstances would not require reopening, the Commission determines that the public interest

requires such action. Therefore, Section 2.51 of the Commission's Rules of Practice invites respondents in petitions to reopen to show how the public interest warrants the requested modification. In the case of a request for modification based on this latter ground, a petitioner must demonstrate as a threshold matter some affirmative need to modify the order. *Damon Corp.*, Docket No. C-2916, Letter to Joel E. Hoffman, Esq. (March 29, 1983), at 2. If the showing of need is made, the Commission will balance the reasons favoring the requested modification against any reasons not to make the modification. *Id.* The Commission will also consider whether the particular modification sought is appropriate to remedy the identified harm.

Whether the request to reopen is based on changed conditions or on public interest considerations, the burden is on the respondent to make the requisite satisfactory showing. The language of Section 5(b) plainly anticipates that the petitioner must make a "satisfactory showing" of changed conditions to obtain reopening of the order. The legislative history also makes it clear that the petitioner has the burden of showing, other than by conclusory statements, why an order should be modified.[6] If the Commission determines that the petitioner has made the required showing, the Commission must reopen the order to consider whether modification is required and, if so, the nature and extent of the modification. The Commission is not required to reopen the order, however, if the petitioner fails to meet its burden of making the satisfactory showing required by the statute. The petitioner's burden is not a light one given the public interest in repose and the finality of Commission orders.[7]

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[6] The Commission may properly decline to reopen an order if a request is "merely conclusory or otherwise fails to set forth specific facts demonstrating in detail the nature of the changed conditions and the reasons why these changed conditions require the requested modification of the order." S. Rep. No. 96-500 96th Cong., lst Sess. 9-10 (1979). *See also* Rule 2.51(b), which requires affidavits in support of petitions to reopen and modify.

[7] *See Federated Department Stores, Inc. v. Moitie*, 425 U.S. 394 (1981) (strong public interest considerations support repose and finality).

IV.

Pioneer Has Failed to Demonstrate Changed Conditions of Law or Fact That Require Reopening of the Order

Pioneer has failed to show that the modifications it seeks are required by changes of law. The provisions that Pioneer seeks to have set aside are part of the order's overall prohibition on resale price maintenance. Nothing in the complaint or order suggests that the cooperative advertising restrictions or any of the other advertising restrictions were imposed because the prohibited conduct itself, absent resale price maintenance, was *per se* unlawful.[8] The Pioneer order is, in that sense, virtually identical to the order in *The Magnavox Company*, 78 FTC 1183 (1971). In its modification of the order in Magnavox ("1990 Magnavox Modification"), the Commission denied Magnavox's request for a reopening and modification of the "fencing-in" provisions of the order on the basis of changed conditions of law. The Commission's denial of Pioneer's Petition based on change of law is consistent with the Commission's analysis in the 1990 Magnavox Modification.

Resale price maintenance schemes remain *per se* unlawful. *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977), which was decided two years after the Commission issued the order in this case, recognized that non-price vertical restraints are not inherently anticompetitive and must thus be judged under the rule of

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[8] *Cf. Sharp Electronics Corporation*, 112 FTC 303 (1989), in which the Commission set aside the order based on change of law. The Sharp Electronics order prohibited Sharp from engaging in only non-price vertical restraints, such as territorial restrictions; the non-price vertical restrictions were not a part of an overall order prohibiting resale price maintenance. At the time the order was entered all vertical restrictions were *per se* unlawful under *U.S. v. Arnold Schwinn & Co.*, 388 U.S. 365 (1977). The Commission vacated the order based upon the change in law in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977) and its progeny, which changed the test from *per se* to rule of reason analysis for non-price vertical restraints. The Commission noted that GTE Sylvania did not "change the *per se* rule against resale price maintenance." 112 FTC at 306 fn. 3. The Pioneer order differs from the Sharp Electronics order in that the complaint against Pioneer was concerned with non-price conduct that was a part of resale price maintenance and the order prohibited non-price vertical restraints as a part of the prohibitions on resale price maintenance.

reason.[9] The Supreme Court, in GTE Sylvania, replaced the *per se* test for non-price vertical customer restraints outside resale price maintenance with a rule of reason test, but the Court did not change the *per se* rule for non-price vertical restraints that are part of a resale price maintenance scheme. Pioneer has failed to show that any of the actions in which it wishes to engage as a result of the proposed modification have become lawful if part of resale price maintenance. Because the provisions of paragraph I generally prohibit conduct that is unlawful if engaged in as part of resale price maintenance, and because GTE Sylvania did not change the law as to such conduct, Pioneer has failed to show that its request should be granted based upon a change in law.

Pioneer has similarly not made the necessary showing that changed conditions of fact require the Commission to reopen and modify the order. Although Pioneer has alleged that the United States consumer electronic products market today appears to be competitive, Petition Memo at 16-17, just as Magnavox did in its request, the record does not contain any evidence of market structure at the time the Commission issued the order, because the complaint was premised on a *per se* theory of resale price maintenance. Thus, based only upon Pioneer's description of today's consumer electronic products market, Pioneer has not shown that changed conditions of fact make those provisions for which it requests a modification no longer necessary or harmful to competition. Indeed, resale price maintenance would be unlawful today, even if Pioneer had shown that the market had changed from a concentrated to unconcentrated one since the order was issued.

V.

The Cooperative Advertising Restrictions (Paragraph I.6.)

Although Pioneer has failed to demonstrate changed conditions of law or fact that require reopening of the order, Pioneer has shown

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[9] *See* In the Matter of *Beltone Electronics Corporation, et al.*, 100 FTC 68 (1982) (illustrating that GTE Sylvania has significantly affected the Commission's analysis of non-price vertical restraints).

that the public interest warrants reopening and modifying the order to delete paragraph I.6. The provision Pioneer seeks to have deleted prohibits conduct that may be lawful if engaged in outside of a resale price maintenance scheme, and Pioneer has shown that it is being injured in competing with other firms that are free to and do engage in cooperative advertising programs.

Pioneer has requested that paragraph I.6. be deleted from the order to allow it to offer certain price-restrictive cooperative advertising programs. Pioneer has shown that its ability to compete is adversely affected by the order's restrictions concerning price-restrictive cooperative advertising programs. Pioneer has demonstrated that many of its competitors currently use such programs with respect to consumer electronic product lines that are directly competitive with the Pioneer lines. For example, Mark Smith, Pioneer's Senior Manager, Planning and Coordination, for the Home Electronics Division of Pioneer Electronics (USA), states that Pioneer's competitors, Sony, Mitsubishi, Hitachi, JVC, and RCA, use MAPs to build dealer support. *See* Smith Aff. at ¶15. The competitors generally receive cooperative advertising allowances for maintaining MAP. According to the evidence submitted by Pioneer, some dealers are less inclined to carry a full line of Pioneer products because of the lack of a Pioneer price-restrictive cooperative advertising program. In light of Pioneer's competitors' use of programs that Pioneer cannot offer and the resulting injury caused to Pioneer's ability to attract and keep dealers, Pioneer has made a threshold showing of an affirmative need for paragraph I.6. to be deleted.

The reasons in favor of a modification to delete paragraph I.6. outweigh the reasons not to modify the order. The Commission reopened and modified the Magnavox order in 1990 to delete similar provisions relating to the restrictions on cooperative advertising allowances.[10] In making that decision, the Commission followed the

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[10] The Commission, among other things, deleted paragraph I.H. from the Magnavox order, which read as follows:

> I.H. Threatening to withhold or withholding earned cooperative advertising credits from dealers for the reason that they advertise its products at retail prices other than established or suggested retail prices.

The Magnavox Company, 78 FTC 1183, 1189 (1971).

reasoning in its 1987 decision to vacate the order in *The Advertising Checking Bureau, Inc.*, 93 FTC 4 (1979). The 1979 Advertising Checking Bureau, Inc. order had prohibited the respondent from auditing cooperative advertising programs that required dealers to advertise at a specified price, or not to advertise at discount prices, as a condition of receiving advertising allowances or credits. In support of its determination to set aside The Advertising Checking Bureau, Inc. order, the Commission relied on the Supreme Court's decisions in *Continental T.V., Inc. v. GTE Sylvania, Inc.*, 433 U.S. 36 (1977) and *Monsanto Co. v. Spray-Rite Service Corp.*, 465 U.S. 752 (1984), noting, among other things, that those decisions "make it clear that the rule of reason should be applied in determining whether non-price vertical restraints unreasonably restrain competition and violate the antitrust laws." *The Advertising Checking Bureau, Inc.*, No. C-2947, 109 FTC 146 (1987).[11] The Commission also noted that "[t]he fact that a distributional restraint may have an incidental effect on resale prices is not by itself enough to condemn the practice as *per se* unlawful." *Id.* With respect to price-restrictive cooperative advertising programs specifically, the Commission held that such programs "would not by themselves constitute agreements to fix resale prices." *Id.* Moreover, the Commission recognized that price restrictive cooperative advertising programs are in fact "likely to be procompetitive . . . in most cases . . . by . . . channeling the retailer's advertising efforts in directions that the manufacturer believes consumers will find more compelling and beneficial . . . [t]his, in turn, may stimulate dealer promotion and investment and, thus, benefit interbrand competition." *Id.* at 3.[12]

In conjunction with the Commission's decision to set aside the order in The Advertising Checking Bureau, Inc., the Commission also announced that it had withdrawn its 1980 policy statement regarding price restrictions in cooperative advertising programs, which had stated the Commission's intention to challenge as *per se*

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[11] Of course, Sylvania did not change the *per se* rule against resale price maintenance, the conduct that the orders against Magnavox and Pioneer were designed to end.

[12] The Commission set aside The Advertising Checking Bureau, Inc. order on public interest grounds.

unlawful cooperative advertising programs restricting reimbursement for the advertising of discounts. The Commission announced its new policy as to price restrictions in cooperative advertising programs as follows:

> The Commission now concludes that price restrictions in cooperative advertising programs, standing alone, are not *per se* unlawful. The *per se* rule applies to conduct that is so plainly anticompetitive that it is conclusively presumed to be unreasonable without an elaborate inquiry into competitive effects. Cooperative advertising programs that restrict reimbursement for the advertising of discounts do not appear to fall into this category . . . .

6 Trade Reg. Rep. (CCH) ¶ 39,057.

This change in Commission policy is further supported by recent court decisions. In *in re Nissan Antitrust Litigation*, 577 F.2d 910 (5th Cir. 1978), *cert. denied*, 439 U.S. 1072 (1979), the court held that agreements that withhold cooperative advertising allowances from dealers that advertise discounted prices are analyzed under the rule of reason. Additionally, the Supreme Court's recent decision in *Business Electronics Corp. v. Sharp Electronics Corp.*, 485 U.S. 717 (1988), supports the Commission's decision. That decision sought to draw a clear line between vertical restraints concerning price, which are *per se* illegal, and non-price vertical restraints, which are judged under the "rule of reason standard," by holding that an agreement or conspiracy between a manufacturer and a complaining retailer to terminate a discounter because of his price cutting was not sufficient to constitute conduct which is *per se* unlawful unless the agreement included some agreement on price or price levels.

The approach followed by the Commission in the 1990 Magnavox Modification and in adopting the new cooperative advertising policy by setting aside the order in The Advertising Checking Bureau, Inc. is equally applicable to Pioneer's request that the Commission set aside paragraph I.6. of the order. This provision prohibits price restrictions that Pioneer might want to impose on its dealers in connection with its cooperative advertising programs. Such restrictions may not necessarily be part of an illegal resale price maintenance scheme and have now been recognized as reasonable in many circumstances. Of course, any cooperative advertising program

implemented by Pioneer as part of a resale price maintenance scheme would be *per se* unlawful and would violate paragraph I.l. of the order.

Pioneer has further shown that setting aside this provision is not likely to result in Pioneer's engaging in unlawful conduct. The markets for most of the consumer electronic products sold by Pioneer appear to be competitive and fragmented with numerous competitors. *See* Petition Memo at Mark Smith Affidavit; and 1990 Magnavox Modification at 9. In those markets, Pioneer's use of price-restrictive cooperative advertising programs, without further agreement on the price or price levels to be charged by retailers, is not likely to restrict interbrand competition or reduce output. It is unlikely that the competitors in any of the unconcentrated markets would exercise market power through collusive activities because, as the Commission recognized, "collusion is unlikely to be successful in an unconcentrated market." *TEAC Corp. of America*, 104 FTC 634, 635 (1984).[13] Moreover, there have been numerous new entrants into all the markets for consumer electronic products since the Commission issued the order in this case,[14] and there has been an influx of new products made by a number of manufacturers, *e.g.*, CD players, laser disc players, large screen projection televisions.[15] Thus, "the absence of barriers to entry is also likely to prevent successful collusion." *Id.* at 637. Setting aside the order's restrictions on Pioneer's adoption and implementation of price-restrictive cooperative advertising programs would allow Pioneer to compete more effectively to the benefit of the consumers of Pioneer's electronic products.

To the extent that price-restrictive cooperative advertising conduct -- now allowed by the removal of in paragraph I.6. pursuant to this Order Modifying Order -- might be in furtherance of an

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[13] *See* 1990 Magnavox Modification at 9 ("The markets for most of the consumer electronic products sold by Magnavox appear to be competitive and fragmented and have numerous competitors, none of which have a controlling market share.").

[14] *See* Petition Memo at 17 (citing to the 1990 Magnavox Modification). Additionally, Pioneer states that Onkyo and Denon have entered the markets since the Commission entered the order in 1975.

[15] In the projection screen television market, Pioneer's principal competitors are Sony, Mitsubishi, Magnavox, Hitachi, RCA and Zenith.

unlawful scheme to fix resale prices, such conduct would be prohibited by the other provisions of the order. The Commission disagrees, however, that paragraph I.2. also should be modified.[16] The Commission addressed this specific concern in the 1990 Magnavox Modification. In deleting the cooperative advertising restriction paragraph in the Magnavox order, which was nearly identical to paragraph I.6. of this order, the Commission did not disturb the language of paragraph I.B. of the Magnavox order which prohibited Magnavox from "[f]ixing, establishing, controlling, maintaining . . . the retail prices at which its dealers may advertise, promote, offer for sale or sell its products." 78 FTC at 1189. In granting Magnavox the right to have restrictions in its cooperative advertising programs, the Commission stated that it would:

> not construe the remaining portions of the modified order to prohibit Magnavox from establishing and maintaining cooperative advertising programs that included conditions as to the prices at which Magnavox offered consumer electronic products, so long as such advertising program were not a part of a resale price maintenance scheme.

1990 Magnavox Modification at 10. For those reasons, the Commission need not modify paragraph I.2. of the Pioneer order to make the deletion of paragraph I.6. effective.

For the above reasons, therefore, the Commission has determined that Pioneer has demonstrated an affirmative need to reopen the order, and that the reasons to set aside paragraph I.6. of the order outweigh any reasons to retain it. *See Lenox Inc.*, Docket No. 8718, 111 FTC 612 (1989), Order Granting in Part and Denying in Part Request to Reopen and Modify.

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[16] Pioneer requests that the Commission delete the bracketed words from paragraph I.2.:

> Fixing, establishing, controlling or maintaining the prices at which dealers may [advertise, promote, offer for sale] or sell respondent's products.

Petition at 1.

VI.

The Modifications Concerning Paragraphs I.2., I.5., I.8. and Most of I.10.

Pioneer has requested that the order be modified to allow it to, among other things, fix the prices at which its products are advertised, refuse to deal with a dealer who does not enter into an agreement to advertise products at the established or suggested resale price and obtain dealers' promises on the prices they will advertise for Pioneer's products. Additionally, Pioneer requests relief from the prohibition on threatening, intimidating, coercing or delaying shipments to a dealer who advertises Pioneer products at prices other than those Pioneer deems appropriate.[17] For the reasons discussed in Section IV, above, the Commission has determined that Pioneer has not shown changed conditions of law or fact that require reopening the order to modify these provisions. Also, for the reasons discussed, below, Pioneer has failed to show that it would be in the public interest to modify these provisions.

Pioneer has not Demonstrated that the Modifications are in the Public Interest.

Pioneer has failed to show the threshold injury required under the public interest standard. Even if Pioneer had made that showing, Pioneer failed to show that the reasons for modifying these provisions outweigh the reasons for not modifying them.

Pioneer has Failed to Show an Affirmative Need for the Modifications.

Under the public interest standard for modification of paragraphs I.2., I.5., I.8. and most of I.10., Pioneer has not shown an affirmative

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[17] *See* Footnote 5, above, for the modifications Pioneer seeks.

need for the requested modifications.[18] Pioneer has not shown that its competitors use similar advertising restrictions and sanctions or that it is harmed by any such program. Although Pioneer has shown that its inability to employ some price-restrictive advertising program may be causing competitive injury, Pioneer has not demonstrated that it needs to institute MAP programs that require the fixing of advertised prices and that explicit agreements are required to remedy the alleged erosion of its dealer base.[19] Pioneer, therefore, has not made a satisfactory showing of harm from the existing provisions and has not satisfied its burden of demonstrating why modification of the order would serve the public interest.

Moreover, Pioneer has not demonstrated that the use of a price-restrictive cooperative advertising program would not adequately address its competitive concerns. Pioneer's Petition is unclear whether removal of the cooperative advertising restriction would be sufficient to remedy the alleged harm. Pioneer asserts that it should not be penalized for not gaining information on how its competitors enforce their MAP programs. Nevertheless, neither should Pioneer be rewarded for failing to meet its burden to make the adequate showing of need. Based upon Pioneer's submission, the information gained from the Commission's analysis of this Petition, and the Commission's determinations in the 1990 Magnavox Modification, Pioneer has not met its burden of showing an affirmative need for the reopening and modification of paragraphs I.2., I.5., I.8. and most of I.10.

Even if Pioneer had Shown an Affirmative Need, the Reasons Against Such a Modification Outweigh the Reasons for a Modification.

Even if Pioneer had shown an affirmative need for the reopening, the reasons against modifying the order outweigh those in favor of a

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[18] Pioneer has shown, however, that it is in the public interest for paragraph I.10. to be modified to remove the prohibitions on Pioneer unilaterally terminating a dealer for failing to follow a suggested advertised price. *See* Part VII of this Order Modifying Order.

[19] In contrast, in the area of cooperative advertising restrictions, Pioneer has presented some evidence of its competitors' practices to demonstrate its competitive injury.

modification. Paragraphs I.2., I.5., I.8. and most of I.10. prohibit actions that, if used in the context of resale prices, as opposed to advertised prices, could be prohibited as *per se* unlawful resale price maintenance agreements depending on whether the conduct was found to be part of an agreement or conspiracy to fix resale prices at some level. In *United States v. Colgate & Co.*, 250 U.S. 300 (1919), the Supreme Court held that a manufacturer can unilaterally announce its resale prices in advance and refuse to deal with those who fail to comply. Court decisions, however, have found coercion or threats by a manufacturer against a discounting retailer, even in the absence of complaining third-party retailers, to form the basis of *per se* unlawful resale price maintenance agreements. For example, in *Isaken v. Vermont Castings, Inc.*, 825 F.2d 1159 (7th Cir. 1987) (Posner, J.) *cert. denied*, 486 U.S. 1005 (1988), the court found a manufacturer's threat to mix up a retailer's orders if the retailer did not raise prices to have resulted in an implicit, yet nonetheless *per se* unlawful, agreement.

Similarly, fixing advertised prices, entering into advertised price agreements with dealers, sanctioning dealers that fail to enter into advertising agreements and threatening, intimidating or coercing dealers that do not comply with suggested advertised prices are all conduct which, depending on the circumstances, could fall within the *per se* ban. Although advertising price arrangements standing alone may not be *per se* unlawful, restrictions on advertising similar to those identified in paragraphs I.2., I.5., I.8. and most of I.10. may come dangerously close to or be used in conjunction with resale price maintenance activities. If the MAP agreements are such that they are used to gain the "retailers' adherence to its suggested retail price," *United States v. Parke, Davis & Co.*, 362 U.S. 29 (1960), it is possible for them to be part of the *per se* illegal combination. In Parke, Davis & Co., Parke, Davis believed that selling at a discount would be deterred if all advertising of discount prices was discontinued. The Court noted that the agreement not to advertise prices was part of the combination that contained the price agreement. *Business Electronics Corp. v. Sharp Electronics Corp.*, 717 U.S. at 735 (citing Parke, Davis). Although the conduct relating to advertising proscribed by paragraphs I.2., I.5., I.8. and most of I.10. may fall outside the *per se* ban, the very purpose of such "fencing-in"

provisions is to steer a company found to have violated the law away from activities which could reasonably be found to constitute unlawful conduct.[20] Pioneer has not shown that the danger of such agreements leading to resale price maintenance no longer exists.

The advertising restrictions in this case are part of the order's core resale price maintenance prohibitions, unlike the restrictions on cooperative advertising programs in paragraph I.6. It is reasonable for the Commission to deny the proposed modifications at this time to avoid the possibility of Pioneer using the freedom to fix all advertising prices -- through agreements, coercion, intimidations or sanctions -- as a way to circumvent the resale price maintenance prohibitions of the order. Pioneer alleges that advertising plays a big part in whether and at what price audio and video electronics products are ultimately sold. Pioneer asserts that mass media advertising is very important for the consumer in making his choice of electronics products (Smith Aff. at ¶ 7). Pioneer also strongly asserts that consumers make decisions as to the quality of electronics products by virtue of their advertised prices. Because of the importance of advertising in this market, allowing Pioneer to fix advertised prices by agreement, to sanction dealers for non-compliance, or to intimidate or coerce dealers into complying with suggested advertised prices could be a precursor or a part of a resale price maintenance agreement.[21]

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[20] *See Federal Trade Commission v. Ruberoid Co.*, 343 U.S. 470, 473 (1952), where the Supreme Court affirmed the Federal Trade Commission's authority to use fencing-in provisions in orders to prevent illegal practices in the future:

> In carrying out this function the Commission is not limited to prohibiting the illegal practice in the precise form in which it is found to have existed in the past. If the Commission is to attain the objectives Congress envisioned, it cannot be required to confine its road block to the narrow lane the transgressor has traveled; it must be allowed effectively to close all roads to the prohibited goal, so that its order may not be by-passed with impunity.

[21] The Commission recently included restrictions on advertising, similar to those in the Pioneer order, in the *Nintendo of America, Inc.* order, Docket No. C-3350 (November 14, 1991). The advertising agreements, in that case, were part of an overall resale price maintenance scheme. Pioneer argued in its Petition Memo that Nintendo is different from the Pioneer case because Nintendo, unlike Pioneer, has the ability to interfere with interbrand pricing because of its high market share. The Commission

Accordingly, this issue raises enough of a question to deny the modification, especially because Pioneer has not shown that its alleged competitive injury cannot be remedied by setting aside paragraph I.6., and modifying paragraph I.10. as discussed in Part VII of this Order Modifying Order.[22] Because of the on-going competitive concerns about these arrangements and because Pioneer failed to make a showing of an affirmative need for these modifications, the Commission has denied Pioneer's request to modify the order as to paragraphs I.2.,[23] I.5., I.8. and most of I.10.

VII.

Pioneer has Shown that Paragraph I.10. Should be Modified to Allow Pioneer to Terminate Dealers Who Advertise Below a Suggested Advertised Price

Paragraph I.2. of the order prohibits Pioneer from fixing, establishing, controlling or maintaining advertised prices. Under paragraph I.3. of the order, Pioneer may suggest a resale price for its home electronics products. Additionally, nothing in the order prohibits Pioneer from suggesting an advertised price for its home electronics products. Paragraph I.10., however, prohibits Pioneer from:

> Terminating, threatening, intimidating, coercing, delaying shipments, or taking any other action to prevent the sale of respondent's products by a dealer because said dealer has advertised or sold, is advertising or selling, or is suspected of advertising or selling such products at other than prices that respondent may deem to be appropriate or has approved.

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is not persuaded, however, that advertised price agreements in home electronics products could not be used in furtherance of resale price maintenance agreements.

[22] The Commission considers, as part of the modification decision, whether the particular modification sought is appropriate to remedy the identified harm. *See* 1990 Magnavox Modification at 5.

[23] In the 1990 Magnavox Modification, the Commission did not remove, nor did Magnavox seek removal of, its prohibition on fixing, establishing, maintaining or controlling the retail prices at which its dealers may advertise, promote, offer for sale or sell its products (Paragraph I.B.).

Pioneer's Petition requests the removal of the advertising restrictions in paragraph I.10. As discussed in Section VI, above, the Commission has determined that Pioneer has not made a showing sufficient to warrant a modification of paragraph I.10. to remove the prohibition on threatening, intimidating, coercing, delaying shipments, or taking any other action to prevent the sale of Pioneer's products by a dealer because the dealer has advertised or is advertising Pioneer home electronics products at a price other than that suggested by Pioneer. Pioneer has made a showing, however, that it would be in the public interest to modify paragraph I.10. to remove the prohibition on Pioneer terminating a dealer for not following a suggested advertised price.

Other than the termination of a dealer, the conduct in paragraph I.10. involves conduct that if engaged in with regard to resale prices could be considered resale price maintenance, and with regard to suggested advertised prices could be sufficiently close to resale price maintenance that it could lead to or be used as part of a resale price maintenance scheme.[24] Instead of granting Pioneer's request to delete the term "advertising" from paragraph I.10., the Commission believes that it is in the public interest for paragraph I.10. to be modified to delete the word "terminating" only as it relates to advertising.[25]

Pioneer alleges that it is losing dealers who will supply a full line of its products, *i.e.*, the products are widely distributed but also thinly distributed.[26] Because of constant sales, Pioneer dealers are not likely to recover much of a profit on each item and, as a result, the dealers are not inclined to invest in Pioneer inventory, promotions and pre-sale services on Pioneer products.[27]

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[24] *See* 1990 Magnavox Modification at 12, fn. 20 ("The remaining part of subparagraph (T) will continue to prohibit Magnavox from harassing, threatening, or coercing its dealers (all actions which still may lead to agreements and which therefore remain unlawful)."). *See also* discussion in Section VI of this Order Modifying Order.

[25] The Commission, however, is issuing an Order to Show Cause why the order should not be further modified to remove the restriction on Pioneer to unilaterally terminate a dealer for not following suggested resale prices.

[26] Petition Memo at Smith Aff. at ¶ 8.

[27] Petition Memo and declarations attached thereto.

It is not unreasonable for Pioneer to want to protect the pre-sale services of its products, especially the high-end products and the new products through a plan that allows Pioneer to terminate a dealer who does not follow suggested advertised prices. Unilaterally terminating a dealer for advertising below suggested prices is less competitively threatening to interbrand competition than unilaterally terminating a dealer for failing to follow a suggested resale price. The latter, of course, is explicitly allowed under the teachings of Colgate, Monsanto and Sharp. Allowing Pioneer unilaterally to terminate a dealer for not following a suggested advertised price, however, does not venture nearly as close to resale price maintenance behavior as would granting Pioneer's request for modifications of paragraphs I.2., I.5., I.8. and most of I.10. Modifying those provisions would allow Pioneer to engage in conduct that is not unilateral and, instead, enter into agreements on advertised prices which could, depending on the circumstances, fall within the *per se* ban.

The Commission, therefore, has determined that it is the public interest to modify paragraph I.10. to remove the restrictions on Pioneer terminating a dealer for not following suggested advertised prices. *See Colgate, Sharp, Monsanto*, and *Lenox, Inc.*, Docket No. 8718, 111 FTC 612 (1989). To the extent that the conduct being allowed by the modifications might be in furtherance of an unlawful scheme to fix resale prices, such conduct would continue to be prohibited by the other provisions of the order.

VIII.

The Commission Issues an Order to Show Cause to Allow Pioneer to Terminate Dealers Who Sell Below a Suggested Resale Price

The Commission is also issuing an Order to Show Cause why paragraph I.10. of the order should not further be modified so that Pioneer would not be prohibited from unilaterally terminating a dealer who sells Pioneer home electronics products at a price other than the suggested resale price. If this modification is to be made, an Order to Show Cause is necessary because Pioneer's Petition did not request this additional modification. The Commission generally will not use show cause proceedings to grant broader relief than requested

by a respondent, and respondents have no right to obtain an Order to Show Cause.[28] However, an Order to Show Cause is appropriate in this case given the particular showings made by Pioneer and the similarities between this case and the modification of the Magnavox order in 1990.

In this case the Commission has already considered the language of paragraph I.10. in deciding Pioneer's requested changes to the scope of that paragraph concerning unilateral dealer terminations for not following suggested advertised prices. Pioneer's showing in support of its request to remove the prohibition allowing it unilaterally to terminate a dealer for not following suggested advertised prices also strongly supports a finding that it would be in the public interest to remove the prohibition on terminating a dealer for failing to follow suggested resale prices. Pioneer has shown that its dealer base has been depleted and that those dealers carrying its products generally do not provide pre-sale and post-sale services suggested by Pioneer.

The change intended in the show cause proceeding is consistent with, and similar to, the modification made to the Magnavox order in 1990. Magnavox directly competes with Pioneer in most electronics markets and alleged similar competitive problems. Because of these particular factors, and because the conduct to be allowed is lawful under the Colgate doctrine, the Commission believes it is appropriate in this particular situation to grant somewhat broader relief than Pioneer has requested.[29] The Commission's reasoning in Magnavox is equally applicable in this case:

> This modification will allow Magnavox to announce its resale prices for consumer electronic products in advance and refuse to deal with any dealer who fails to comply. It should therefore enable Magnavox to protect its full-service dealers from the activities of "free-riding" dealers and encourage its full-service dealers to provide the

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[28] Respondents' route to request relief through petitions to reopen and modify is set out in Section 5(b) of the Federal Trade Commission Act and Section 2.51 of the Commission's Rules of Practice.

[29] *See* "Order Reopening and Modifying Order Issued September 26, 1978, and Order to Show Cause," *Interco Inc., et al.*, Docket No. C-2929, 110 FTC 153, 156 (1988).

promotion and sales-related services that it believes are necessary to market Magnavox consumer electronic products efficiently. This modification retains all the order's provisions that prohibit Magnavox from engaging in resale price maintenance. The Commission may invoke them if Magnavox engages in conduct that goes beyond what is lawful under Monsanto.

1990 Magnavox Modification at 12 (emphasis added). Consistent with the 1990 Magnavox Modification, the modification of paragraph I.10. -- to allow termination both for not following suggested advertising or sales prices -- is in the public interest. The unique circumstances of this case, therefore, have created a situation in which it is appropriate for the Commission not only to grant the requested modification of paragraph I.10. regarding unilateral termination of dealers not following suggested advertised prices, but also to issue an Order to Show Cause why the order should not also be modified to allow unilateral termination for not following suggested resale prices.

IX.

Conclusion

Accordingly, *It is ordered*, That this matter be reopened and that the Commission's modified order in Docket No. C-2755 be, and hereby is, modified, as of the effective date of this order, as follows:

(a) Paragraph I.6. of the order is deleted; and

(b) Paragraph I.10. of the order is modified to delete the word "terminating" as it relates to advertising, and paragraph I.10. is rewritten in two parts as follows:

Threatening, intimidating, coercing, delaying shipments, or taking any other action (other than terminating) to prevent the sale of respondent's products by a dealer because said dealer has advertised, is advertising, or is suspected of advertising such products at other than prices that respondent may deem to be appropriate or has approved; or

Terminating, threatening, intimidating, coercing, delaying shipments, or taking any other action to prevent the sale of respondent's products by a dealer because said dealer has sold, is selling, or is suspected of selling such products at other than prices that respondent may deem to be appropriate or has approved.

X.

Order to Show Cause

It is further ordered, That respondent Show Cause why paragraph I.10. should not be additionally modified to read as follows:

Threatening, intimidating, coercing, delaying shipments, or taking any other action (other than terminating) to prevent the sale of respondent's products by a dealer because said dealer has advertised or sold, is advertising or selling, or is suspected of advertising or selling such products at other than prices that respondent may deem to be appropriate or has approved.

In accordance with Section 3.72 of the Commission's Rules of Practice, 16 CFR 3.72, respondent has thirty (30) days from the date of service of this order to file an answer to this Order to Show Cause or be deemed to have accepted the action proposed herein.

Commissioner Azcuenaga concurring in the result.

IN THE MATTER OF

TEXAS BOARD OF CHIROPRACTIC EXAMINERS

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3379. Complaint, Apr. 21, 1992--Decision, Apr. 21, 1992

This consent order requires, among other things, the Texas licensing Board to repeal existing rules that prohibit truthful, nondeceptive advertising, and certain types of solicitation, and also prohibits respondent from adopting similar rules or policies in the future. In addition, respondent is prohibited from taking or threatening disciplinary action against any person or organization that advertises truthfully.

Appearances

For the Commission: *Gary Kennedy* and *Thomas Carter.*

For the respondent: *Frank Knapp, Jr.*, Assistant Attorney General, Austin, TX.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the Texas Board of Chiropractic Examiners has violated Section 5 of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues this complaint, stating its charges in that respect as follows:

RESPONDENT

PARAGRAPH 1. Respondent Texas Board of Chiropractic Examiners ("the Board") is organized, exists and transacts business under the laws of the State of Texas, and has its principal office and place of business at Building C, Suite 245, 1300 East Anderson,

Austin, Texas. The Board is subject to the Commission's jurisdiction pursuant to Section 5 of the Federal Trade Commission Act.

PAR. 2. The Board is composed of nine members who are appointed by the governor to staggered six-year terms. Six of the members must be chiropractors who have practiced continuously in Texas for at least five years prior to their appointment to the Board, and the members must continue to practice chiropractic while on the Board. The other three members must be individuals who are not associated with the health care profession. Tex. Civ. Code Ann. Art. 4512b, Sections 3(b) and (c). Board members spend a relatively small percentage of their time on Board matters, and compensation is limited to a per diem and transportation allowance for days of actual service. Tex. Civ. Code Ann. Art. 4512b, Section 11(c).

PAR. 3. The Board has exclusive authority to license chiropractors in Texas. It is unlawful to practice chiropractic in Texas without first obtaining a license from the Board. Tex. Civ. Code Ann. Art. 4512b, Section 5(a). The Board is authorized to adopt rules and regulations necessary for the performance of its duties. Tex. Civ. Code Ann. Art. 4512b, Section 4(a). The Board is also authorized to refuse to issue a license to, or to suspend or revoke an existing license of, any person found guilty of any of sixteen enumerated offenses. Tex. Civ. Code Ann. Art. 4512b, Section 14(a).

TRADE AND COMMERCE

PAR. 4. Except to the extent that competition has been restrained as alleged herein, and depending on their geographic location, chiropractors in Texas compete with one another, and with a majority of the members of the Board.

PAR. 5. The acts and practices described below are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act.

STATE POLICY CONCERNING
CHIROPRACTIC ADVERTISING AND SOLICITATION

PAR. 6. The State of Texas has no articulated policy to restrict chiropractors from engaging in truthful, nondeceptive advertising. Section 14(a) of the Texas Chiropractic Act, however, authorizes the Board to impose two sorts of restrictions on truthful, nondeceptive advertising. Section 14(a)8 authorizes a ban on truthful, nondeceptive claims of professional superiority, and Section 14(a)16 authorizes a ban on solicitation of patients by use of case histories of patients of other chiropractors. Otherwise, under Section 17b of the Act, "The Board may not adopt rules restricting . . . advertising by a person regulated by the Board except to prohibit false, misleading, or deceptive practices by the person."

UNLAWFUL BOARD CONDUCT

PAR. 7. The Board combined or conspired with its members or others, or acted as a combination of its members or others, to restrain competition among chiropractors by preventing them from disseminating truthful, nondeceptive information in their advertising and solicitation. In furtherance of this combination or conspiracy, the Board has engaged in the following acts or practices, among others:

(A) Adopted and maintained Rules of Practice that declared the following to be unprofessional conduct:

1. Making damaging statements about another licensee or group of licensees (Rule 75.1(1));
2. Using such terms in advertising as "most modern," "scientific," "latest procedures," "best equipped," or "any other like words or phrases" (Rule 75.1(3)); and
3. Soliciting patients by demonstrating chiropractic "in public places" (Rule 75.1 (5)).

(B) Adopted and maintained Rules of Practice that prohibit chiropractors from using any form of public communication that:

1. Contains self-laudatory statements (Rule 77.2(1));

2. Contains statistical data or other information based on past performance or prediction of future success (Rule 77.2(3));

3. Contains testimonials about or endorsements of chiropractors, or utilizes case histories of chiropractors' patients (Rule 77.2(4)); or

4. Contains statements that are intended or are likely to attract patients by the use of showmanship or self-laudation, including but not limited to the use of drawings, illustrations, animations, portrayals, dramatizations, slogans, jingles, music, lyrics, pictures or photographs, or sensational language or format (Rule 77.2(5)).

(C) Adopted and maintained a Rule of Practice that specifies that advertising must be "dignified" and can only contain twelve categories of information (Rule 77.3).

CONSUMER AND COMPETITIVE INJURY

PAR. 8. The combination or conspiracy and the acts and practices described above have restrained and continue to restrain competition unreasonably and to injure consumers by, among other things:

(A) Depriving consumers of the benefits of vigorous competition among chiropractors;

(B) Depriving consumers of truthful, nondeceptive information about the fees, services, and products offered by chiropractors;

(C) Preventing chiropractors from engaging in truthful, nondeceptive advertising about their fees, services and products; and

(D) Preventing chiropractors from engaging in truthful, nondeceptive solicitation.

PAR. 9. The acts and practices described above constitute unfair methods of competition and unfair acts or practices in violation of Section 5 of the Federal Trade Commission Act. The acts and practices, or the effects thereof, are continuing and will continue in the absence of the relief requested.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondent named in the caption hereof, and the respondent having been furnished thereafter with a copy of a draft of complaint which the Dallas Regional Office proposed to the Commission for its consideration and which, if issued by the Commission, would charge the respondent with violation of the Federal Trade Commission Act; and

The respondent, its attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondent of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondent that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondent has violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, and having duly considered the comments filed thereafter by interested persons pursuant to Section 2.34 of its Rules, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Texas Board of Chiropractic Examiners is organized, exists and does business under and by virtue of the laws of the State of Texas, with its office and principal place of business located at Building C, Suite 245, 1300 East Anderson, Austin, TX.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondent, and the proceeding is in the public interest.

ORDER

I.

It is ordered, That for the purposes of this order, the following definitions shall apply:

A. "*Board*" shall mean the Texas Board of Chiropractic Examiners, its members, officers, agents, representatives, employees, successors, and assigns.

B. "*Disciplinary action*" shall mean: (1) a refusal to grant, or the revocation or suspension of, a license to practice chiropractic in Texas; (2) a refusal to admit a person to examination for a license to practice chiropractic; (3) the issuance of a formal or informal warning, reprimand, censure, or cease and desist order against any person or organization; (4) the imposition of a fine, probation, or other penalty or condition; or (5) the initiation of an administrative, criminal, or civil court proceeding against any person.

C. "*Person*" shall mean any natural person, corporation, partnership, governmental entity, association, organization, or other entity.

II.

It is further ordered, That the Board, directly or indirectly, or through any device, in or in connection with its activities in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from:

A. Prohibiting, restricting, impeding or discouraging any person from providing information about any chiropractic product or service, including (i) publishing or advertising, or (ii) soliciting or attempting to solicit patients. The practices from which the Board shall cease and desist include, but are not limited to:

(1) Adopting or maintaining any rule, regulation, policy, or course of conduct that prohibits or seeks to prohibit chiropractors from advertising or solicitation;

(2) Taking or threatening to take any disciplinary action against any chiropractor for advertising or solicitation; or

(3) Declaring it to be an illegal, unethical, unprofessional, or otherwise improper or questionable practice for any chiropractor to advertise or solicit patients.

B. Inducing, urging, encouraging or assisting any non-governmental person to take any action that if taken by the Board would be prohibited by part II A above.

Provided that, nothing contained in this part shall prohibit the Board from formulating, adopting, disseminating and enforcing reasonable rules or taking disciplinary or other action, to prohibit (1) practices that the Board reasonably believes to be false, misleading or deceptive within the meaning of Section 17b of the Chiropractic Act of Texas, (2) any truthful, nondeceptive advertising or solicitation that the Board reasonably believes to be subject to prohibition by the Board pursuant to a Texas statute, (3) uninvited, in-person solicitation of actual or potential patients who because of their particular circumstances are vulnerable to undue influence.

III.

It is further ordered, That the Board shall:

A. Distribute by first-class mail a copy of the announcement attached hereto as Appendix A, a copy of this order and a copy of the accompanying complaint in the following manner:

(1) Within thirty (30) days after the date this order becomes final, to each person licensed to practice chiropractic in Texas as of such date and to each person whose application for, or a request for reinstatement of, a license is pending on such date; and

(2) For five (5) years after the date this order becomes final, to each person who applies for a license to practice chiropractic in Texas within thirty (30) days after the Board receives such application;

B. Within thirty (30) days after the date this order becomes final, remove or revise Rules 75.1(1), 75.1(3), 75.1(5), 77.2(1), 77.2(3), 77.2(4), 77.2(5), and 77.3 of the Rules and Regulations of the Board and any other provision of the Rules and Regulations of the Board and any policy statement or guideline, provision, interpretation, or statement that is inconsistent with Part II of this order;

C. Notify the Federal Trade Commission at least thirty (30) days in advance if possible, or otherwise as soon as possible, of any change in the Board's authority to regulate the practice of chiropractic in Texas that may affect compliance obligations arising out of this order, such as the complete or partial elimination of that authority, the complete or partial assumption of that authority by another governmental entity, or the dissolution of (or other relevant change in) the Board;

D. Within sixty (60) days after the date of service of this order, submit to the Federal Trade Commission a written report setting forth in detail the manner and form in which the Board has complied and is complying with this order; and

E. For a period of five (5) years after this order becomes final, maintain and make available to the Commission staff for inspection and copying upon reasonable notice, records adequate to describe in detail any action taken in connection with the activities covered by Parts II and III of this order, including but not limited to any advice or interpretations rendered with respect to chiropractors engaging in advertising or solicitation.

APPENDIX A

ANNOUNCEMENT

As you may be aware, the Federal Trade Commission has issued a consent order against the Texas Board of Chiropractic Examiners that became final on [date]. The order provides that the Board may not prohibit chiropractors from engaging in truthful, nondeceptive advertising or solicitation.

As a result of the order, the Board may not (1) adopt or maintain rules, regulations or policies that prohibit truthful, nondeceptive advertising or solicitation; (2) take or threaten disciplinary action against any person or organization that so advertises or solicits; or (3) declare it to be illegal, unethical, unprofessional, or otherwise improper or questionable for persons to engage in truthful, nondeceptive advertising or solicitation. The order also prohibits the Board from encouraging any person or organization to take actions that the order prohibits the Board from taking.

The order does not affect the Board's authority to prohibit advertising that is likely to deceive or mislead the public, nor does the order affect the Board's authority to prohibit the advertising of professional superiority or the advertising of the performance of professional services in a superior manner. In addition, the order does not prevent the Board from disciplining licensees for engaging in such advertising. The order also does not restrict the Board's ability to prohibit uninvited, in-person solicitation of actual or potential patients who because of their particular circumstances are vulnerable to undue influence.

For more specific information, you should refer to the FTC order itself. A copy of the order and the accompanying complaint is enclosed.

_____

(Title)

Texas Board of Chiropractic Examiners

IN THE MATTER OF

NU-DAY ENTERPRISES, INC., ET AL.

CONSENT ORDER, ETC., IN REGARD TO ALLEGED VIOLATION OF SECS. 5 AND 12 OF THE FEDERAL TRADE COMMISSION ACT

Docket C-3380. Complaint, Apr. 22, 1992--Decision, Apr. 22, 1992

This consent order prohibits, among other things, a Washington corporation, its owner, and an officer from making false and unsubstantiated claims concerning their diet program, and from misrepresenting that any program length television commercial ("infomercial") they produce is an independent program and not a paid advertisement; and requires a disclosure message, within the first 30 seconds of any infomercial that is 15 minutes long or longer, and in addition, every time ordering information is presented, a disclosure that the infomercial is a paid advertisement.

Appearances

For the Commission: *Timothy T. Hughes* and *John C. Hallerud.*

For the respondents: *Robert E. Armstrong, Gronek & Armstrong*, Chicago, IL.

COMPLAINT

The Federal Trade Commission, having reason to believe that Nu-Day Enterprises, Inc., HealthComm, Inc., corporations and Jeffrey S. Bland, individually and as an officer of Nu-Day Enterprises, Inc., and HealthComm, Inc., hereinafter sometimes referred to as respondents, have violated provisions of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, alleges:

PARAGRAPH 1. a. Respondent Nu-Day Enterprises, Inc., is a Washington corporation with its office and principal place of business located at 5800 Soundview Dr., N.W., Gig Harbor, Washington.

b. Respondent HealthComm, Inc. is a Washington corporation with its office and principal place of business located at 5800 Soundview Dr., N. W., Gig Harbor, Washington. HealthComm, Inc., owns and controls Nu-Day Enterprises, Inc.

c. Respondent Jeffrey S. Bland is an officer and director of Nu-Day Enterprises, Inc., and of HealthComm, Inc. He formulates, directs and controls the acts and practices of these corporations. At all times material herein, respondent Jeffrey S. Bland has formulated, directed and controlled the acts and practices of Nu-Day Enterprises, Inc., and HealthComm, Inc., including the acts and practices herein after set forth. Respondent Jeffrey S. Bland's address is the same as that of the corporate respondents Nu-Day Enterprises, Inc., and HealthComm, Inc.

PAR. 2. Respondents have been engaged in the business of offering for sale, selling, advertising, or distributing dietary programs and food products, as "food" is defined in Section 15 of the Federal Trade Commission Act, such as the "Nu-Day Diet Program," the "Nu-Day Meal Replacement Formula" and "Nu-Day Herbulk" food products; and have participated in, and assisted others in the creation and dissemination to the public of 30 minute, program-length television advertisements for such food products.

PAR. 3. Respondents' acts and practices, including those alleged in this complaint, have been, and are, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 4. Typical and illustrative of the statements made in respondents' advertisements, but not including all such statements or advertisements, are the following statements from the television commercial entitled "The Perfect Diet":

(a) "Amazing true stories of people like yourself losing 20, 30, 50 pounds or more, safely, quickly and naturally."

(b) "What the Nu-Day program allows us to do is to tune up that heat-producing machinery so that the fat is not stored for a rainy day that never comes. Rather, it's lost as body heat -- and that is what we call efficient metabolism. So really, we're inducing efficient metabolism."

(c) "A revolutionary new concept in weight loss. A diet that actually raises your metabolism, causing your body to burn off excess fat, quickly, safely and naturally. . . . Now this diet's available to you at home without a doctor's prescription -- just call

1/800/225-6400, toll free -- that's 1/800/225-6400. A 14-day supply of Nu-Day is only $59.95 and comes with a 100 % money back guarantee."

(d) "So we said, you know, we need to really examine what is going on physiologically. What about their metabolism? Can we roll back their metabolism to that younger age when they could eat more and gain less weight? And that led us ultimately on a search which finally arrived at this Nu-Day product and program that we are going to be talking about -- that I believe has, uh, really heralded a major breakthrough in metabolic management -- getting a person so that their body will in fact work the way it should to maintain proper body weight."

(e) "In the cell we have different little organelles, these are these little things like the nucleus of the cell in the center, which is like the brain of the cell. These little pink units are called mitochondria -- and they're like the lungs or spark plugs of the cell -- they burn up the energy -- and you know, as a person tends to age, what happens is these mitochondria take a siesta, they go to sleep and they don't effectively convert food to energy anymore. We tend to store that energy as fat for a rainy day that never comes. So really what the Nu-Day program -- is to try to help activate those mitochondria. Get them to work right. Get them back to the point where they will convert efficiently food and energy and burn off that fat."

(f) "and well in excess of 100,000 clinical trials have been evaluated with people that have been on this diet and the responses that we are getting here are remarkable . . ."

(g) Standing in front of three canisters, a small box, an audio tape and a booklet, the announcer describes the product: "Developed by Dr. Jeffrey Bland, one of the nation's leading nutritional biochemists, the Nu-Day metabolic weight management system is an easy to use, two-part program. First, the Meal Replacement Formula provides your body with all its basic nutritional needs, using the highest quality ingredients available. Second, Nu-Day Herbulk, the natural appetite suppressant, provides fiber and cleanses the digestive system. Nu-Day contains no narcotic appetite suppressants. It's composed of 100 percent natural ingredients and doesn't contain any drugs, stimulants or preservatives. The Nu-Day metabolic weight management system is fully explained in this complete, easy to follow booklet which also gives you meal suggestions so you can enjoy a delicious variety of real foods. Also this audio cassette, which features Dr. Bland as he answers the most commonly asked questions of people using the Nu-Day program."

PAR. 5. Through the use of the statements referred to in paragraph four, and other statements not specifically set forth herein, respondents have represented, directly or by implication, that:

(a) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" alter human metabolism so that the body will burn more calories than the body was burning prior to following the program or eating the food products.

(b) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" alter human metabolism so that weight lost while following the program or eating the food products will not return when caloric intake increases.

(c) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" alter the mitochondria in the body's cells so that the cells convert more food into energy.

(d) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" prevent the body's metabolism from slowing down to the level that it would reach on any other diet involving similar caloric intake.

PAR. 6. In truth and in fact:

(a) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" do not alter human metabolism so that the body will burn more calories than the body was burning prior to following the program or eating the food products.

(b) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" do not alter human metabolism so that weight lost while following the program or eating the food products will not return when caloric intake increases.

(c) The "Nu-Day Diet Program," "Nu-Day Meal Replacement Formula," and/or "Nu-Day Herbulk" do not alter the mitochondria in the body's cells so that those cells convert more food into energy.

Therefore, the representations set forth in paragraph five (a) through five (c) were, and are, false and misleading.

PAR. 7. Through the use of the statements set forth in paragraph four, and others not specifically set forth herein, respondents have represented, directly or by implication, that, at the time of making the representations set forth in paragraph five (a) through five (d), respondents possessed and relied upon a reasonable basis for making those representations.

PAR. 8. In truth and in fact, at the time of making the representations set forth in paragraph five (a) through five (d) respondents did not possess and rely upon a reasonable basis for making those

representations. Therefore, the representation set forth in paragraph seven was, and is, false and misleading.

PAR. 9. Through the use of the statements set forth in paragraph four, and others not specifically set forth herein, respondents have represented, directly or by implication, that the representations referred to in paragraph five (a) through five (d) are substantiated by 100,000 clinical trials conducted, in a scientifically or medically acceptable manner, on patients specifically following the Nu-Day diet program and/or taking the Nu-Day product or a substantially similar product.

PAR. 10. In truth and in fact, the representations referred to in paragraph five (a) through five (d) are not substantiated by 100,000 clinical trials conducted, in a scientifically or medically acceptable manner, on patients specifically following the Nu-Day diet program and/or taking the Nu-Day product or a substantially similar product. Therefore, the representation set forth in paragraph nine was, and is, false and misleading.

PAR. 11. By and through "The Perfect Diet" television show, respondents have represented, directly or by implication, that "The Perfect Diet" television show is an independent consumer news program that uses interviews to report on its discovery of the Nu-Day Diet.

PAR. 12. In truth and in fact, "The Perfect Diet" television show is not an independent consumer news program. "The Perfect Diet" television show is a paid commercial advertisement. Therefore, the representation set forth in paragraph eleven was, and is, false and misleading.

PAR. 13. The dissemination of the aforesaid false and misleading representations by respondents, as alleged in this complaint, constitute deceptive acts or practices in or affecting commerce and the making of false advertisements in violation of Sections 5(a) and 12 of the Federal Trade Commission Act.

Commissioner Yao not participating.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorneys, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and

The Commission having thereafter considered the matter and having determined that it had reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent Nu-Day Enterprises, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of Washington, with its office and principal place of business located at 5800 Soundview Dr., N.W., in the City of Gig Harbor, State of Washington.

Respondent HealthComm, Inc., is a corporation organized, existing and doing business under and by virtue of the laws of the State of Washington, with its office and principal place of business located at 5800 Soundview Dr., N.W. in the City of Gig Harbor, State of Washington.

Respondent Jeffrey S. Bland, Ph.D., is an officer and director of Nu-Day Enterprises, Inc., and HealthComm, Inc. His address is the same as that of the corporate respondents.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

I.

It is ordered, That respondents Nu-Day Enterprises, Inc., a corporation, its successors and assigns, and its officers, HealthComm, Inc., a corporation, its successors and assigns, and its officers, and Jeffrey S. Bland, individually and as an officer of Nu-Day Enterprises, Inc., and HealthComm, Inc., and respondents' agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with the manufacturing, advertising, labeling, packaging, offering for sale, selling, or distributing of the dietary program or food product (also known as the "Nu-Day Program," "Nu-Day Meal Replacement Formula," "Nu-Day Herbulk," or any other substantially similar dietary program or food product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from representing, directly or by implication:

A. That any such program and/or product alters human metabolism so that the body will burn more calories than the body was burning prior to following the program or eating the product;

B. That any such program and/or product alters human metabolism so that weight lost while following the program or eating the product will not return when caloric intake increases; or

C. That any such program and/or product alters the mitochondria in the body's cells so that those cells convert more food into energy.

For purposes of this Part I a "*substantially similar dietary program or food product*" shall mean any program or product that involves reduction of caloric intake to between eight hundred and one

thousand two hundred (1,200) calories and the consumption of food supplements consisting of powdered protein and bulking agents or containing chromium or any chromium-niacin complex.

II.

It is further ordered, That respondents Nu-Day Enterprises, Inc., a corporation, its successors and assigns, and its officers, Health-Comm, Inc., a corporation, its successors and assigns, and its officers, and Jeffrey S. Bland, individually and as an officer of Nu-Day Enterprises, Inc., and Health Comm, Inc., and respondents' agents, representatives, and employees, directly or through any corporation, subsidiary, division or other device, in connection with manufacturing, advertising, labeling, packaging, offering for sale, selling, or distributing of any dietary program or food product in or affecting commerce, as "commerce" and "food" are defined in the Federal Trade Commission Act, do forthwith cease and desist from representing, directly or by implication, that any such program or product:

A. Can or will alter human metabolism so that the body will burn more calories than the body was burning prior to following the program or eating the product;

B. Can or will alter human metabolism so that weight lost during a period of caloric restriction will not return when caloric intake increases; or

C. Can or will alter the mitochondria in the body's cells so that the cells convert more food into energy;

D. Can or will prevent the body's metabolism from slowing down to the level that it would reach on any other diet involving similar caloric intake;

unless, at the time of making such representation, respondents possess and rely upon competent and reliable scientific evidence that substantiates the representation. "Competent and reliable scientific evidence" shall mean for purposes of this order such test, analysis, research, study, survey or other evidence conducted and evaluated in an objective manner by persons qualified to do so using procedures

generally accepted by others in that profession or science to yield accurate and reliable results.

III.

It is further ordered, That respondents, their successors and assigns, and their officers, agents, representatives and employees, directly or through any corporation, subsidiary division or other device, in connection with manufacturing, labeling, packaging, offering for sale, selling, distributing or advertising any food or weight control service or product in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from representing, directly or by implication, that any such product or service can or will help any consumers lose weight or maintain weight loss unless at the time of making such representation respondents possess and rely upon competent and reliable scientific evidence that substantiates the representation. "Competent and reliable scientific evidence" shall mean for purposes of this order such test, analysis, research, study, survey or other evidence conducted and evaluated in an objective manner by persons qualified to do so using procedures generally accepted by others in that profession or science to yield accurate and reliable results.

IV.

It is further ordered, That respondents, their successors and assigns, and their officers, agents, representatives and employees, directly or through any corporation, subsidiary division or other device, in connection with manufacturing, labeling, packaging, offering for sale any food, drug or device as defined in Section 15 of the Federal Trade Commission Act, 15 U.S.C. 55, selling, distributing or advertising any such product, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from making any representation, directly or by implication, regarding the performance, benefits, efficacy or safety of such food, drug or device *unless*, at the time of making such representation, respondents possess and rely upon a reasonable basis

consisting of competent and reliable scientific evidence that substantiates the representation. "Competent and reliable scientific evidence" shall mean for purposes of this order such test, analysis, research, study, survey or other evidence conducted and evaluated in an objective manner by persons qualified to do so using procedures generally accepted by others in that profession or science to yield accurate and reliable results.

V.

It is further ordered, That respondents, their successors and assigns, and their officers, agents, representatives and employees, directly or through any corporation, subsidiary division or other device, in connection with manufacturing, labeling, packaging, offering for sale, selling, distributing or advertising any dietary program or food product, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from misrepresenting in any manner, directly or by implication, the purpose, content, sample, reliability, results or conclusions of any scientific test, research article, survey or any other scientific opinion or data.

VI.

It is further ordered, That respondents, their successors and assigns, and their officers, agents, representatives and employees, directly or through any corporation, subsidiary division or other device, in connection with manufacturing, labeling, packaging, offering for sale, selling, distributing or advertising any service or product, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from creating, producing, selling, broadcasting, or disseminating, or assisting or encouraging others to create, produce, sell, broadcast, or disseminate:

A. Any commercial or other advertisement for any such product or service that misrepresents, directly or by implication, that it is an independent program and not a paid advertisement;

B. Any commercial or other advertisement for any such product or service that is fifteen (15) minutes in length or longer or intended to fill a broadcasting or cablecasting time slot of fifteen (15) minutes in length or longer that does not display visually, in a clear and prominent manner, within the first thirty (30) seconds of the commercial and immediately before each presentation of ordering instructions for the product or service, the following disclosure:

"THE PROGRAM YOU ARE WATCHING IS
A PAID ADVERTISEMENT FOR [THE PRODUCT OR SERVICE]."

Provided that, for purposes of this provision, the oral or visual presentations of a telephone number or address for viewers to contact to place an order for the product or service shall be deemed a presentation of ordering instructions so as to require the display of the disclosure provided herein.

VII.

It is further ordered, That, on the date this order becomes final, respondents shall pay thirty thousand dollars ($30,000) to the Federal Trade Commission. Respondents shall make this payment by cashier's check or certified check made payable to the Federal Trade Commission. If the Commission determines that redress is wholly or partially impracticable or is otherwise unwarranted, any such funds shall be paid to the United States Treasury. Respondents shall be notified as to how the funds are disbursed, but shall have no right to counter the manner of distribution chosen by the Commission.

VIII.

It is further ordered, That respondents Nu-Day Enterprises, Inc., and HealthComm, Inc., shall for five (5) years following service of this order, notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondents such as dissolution, assignment, or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation that may affect compliance obligations arising out of the order, or of any change in the positions or responsibilities of

Dr. Jeffrey S. Bland in regard to any corporation or subsidiary of which he is an officer.

IX.

It is further ordered, That respondent Dr. Jeffrey S. Bland shall promptly notify the Commission of his discontinuance of his present business or employment and of his affiliation with a new business or employment engaged in the manufacturing, labeling, packaging, offering for sale, selling, distributing or advertising of any foods, dietary programs, or publications relating thereto, or the offering for sale, selling, distributing or advertising of any services relating to any foods or dietary programs, and, for a period of five (5) years from the date of service of this order, shall promptly notify the Commission of each affiliation with such new business or employment. Each such notice shall include his new business address and a statement of the nature of the business or employment in which he is newly engaged as well as a description of his duties and responsibilities in connection with the business or employment. The expiration of the notice provision of this paragraph shall not affect any other obligation arising under this order.

X.

It is further ordered, That, for at least four (4) years after the date of service of this order, respondents, their successors and assigns, shall maintain and upon request make available to the Federal Trade Commission for inspection and copying at a place designated by the Commission,

A. All advertisements and promotional materials subject to this order;

B. All materials relied upon as substantiation for any representation subject to this order;

C. All test reports, studies, surveys, or other materials in respondents' possession or control at any time that contradict, qualify, or call into question any representation subject to this order or that contradict, qualify, or call into question the basis upon which respondents relied for any such representation; and

D. All other materials and records that relate to respondents' compliance with this order.

XI.

It is further ordered, That respondents shall, within sixty (60) days after service of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with this order.

Commissioner Yao not participating.

IN THE MATTER OF

PETERSON DRUG COMPANY OF NORTH CHILI, NEW YORK, INC.

FINAL ORDER, OPINION, ETC., IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE FEDERAL TRADE COMMISSION ACT

Docket 9227. Complaint, Apr. 19, 1989 -- Final Order, Apr. 22, 1992

This final order grants the respondent's motion to withdraw notice of appeal and adopts the initial decision of the administrative law judge, and the order therein, which prohibits boycotts, or threats of boycotts, of pharmacy participation plans.

Appearances

For the Commission: *Karen G. Bokat, John R. Hoagland, Micheal McNeely, Kevin J. Arquit* and *Daniel P. Ducore.*

For the respondent: *Paul Kelly* and *Thomas Fink, Davidson, Fink, Cook & Gates*, Rochester, N.Y.

COMPLAINT

Pursuant to the provisions of the Federal Trade Commission Act, and by virtue of the authority vested in it by said Act, the Federal Trade Commission, having reason to believe that the Chain Pharmacy Association of New York State, Inc.; Melville Corporation; Fay's Drug Company, Inc.; Kinney Drugs, Inc.; Peterson Drug Company of North Chili, New York, Inc.; Rite Aid Corporation; and James E. Krahulec have violated the provisions of said Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint stating its charges as follows:

PARAGRAPH 1. Respondent Chain Pharmacy Association of New York State, Inc. ("Chain Association") is a corporation organized, existing and doing business under and by virtue of the

laws of the State of New York, with its principal office located at 17 Elk Street, Albany, New York.

PAR. 2. Respondent Chain Association is an association composed of the following individual member firms: Brooks Drugs Inc., 15 Sabin St., Pawtucket, RI; Carl's Drug Company, Success Drive, Box 203, Rome, NY; CVS, One CVS Drive, Woonsocket, RI; Duane Reade, 4929 Thirtieth Place, Long Island City, NY; Fay's Drug Co., 7245 Henry Clay Blvd., Liverpool, NY; Genovese Drug Stores, 80 Marcus Dr., Melville, NY; Kinney Drugs, Inc., 29 Main St., Gouverneur, NY; The Kroger Co., 1014 Vine St., Cincinnati, OH; Peterson Drug Co., 68 Main St., P.0. Box 166, Oakfield, NY; Revco D.S., Inc., 1925 Enterprise Parkway, Twinsburg, OH; Rite Aid Corp., P.0. Box 3165, Harrisburg, PA; Supermarkets General Corp., 301 Blair Rd., Woodbridge, NJ; Super X Drugs Corp., 1933 Victory Blvd., Staten Island, NY; Walgreen Co., 200 Wilmont Rd., Deerfield, IL. Chain Association's members are engaged in the business of the retail sale of prescription drugs.

PAR. 3. Respondent Fay's Drug Company, Inc. ("Fay's") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal offices located at 7245 Henry Clay Boulevard, Liverpool, New York. In 1986, the retail sale of prescription drugs accounted for a significant portion of the sales of the 110 to 120 pharmacies that respondent Fay's operated in New York State.

PAR. 4. Respondent Kinney Drugs, Inc. ("Kinney") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal offices located at 29 Main Street, Gouverneur, New York. The retail sale of prescription drugs accounts for a significant portion of the sales of the approximately 23 pharmacies that respondent Kinney operates in New York State.

PAR. 5. Respondent Melville Corporation ("Melville") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal offices located at 3000 Westchester Ave., Harrison, New York. CVS (a/k/a CVS Pharmacies or Consumer Value Stores), with principal offices located at One CVS Drive, Woonsocket, Rhode Island, is a division of Melville. In 1986, the retail sale of prescription drugs accounted

for a significant portion of sales of the approximately 115 pharmacies that respondent Melville operated under the CVS name in New York State.

PAR. 6. Respondent Peterson Drug Company of North Chili, New York, Inc. ("Peterson") is a corporation organized, existing and doing business under and by virtue of the laws of the State of New York, with its principal offices located at 68 North Main Street, Oakfield, New York. The retail sale of prescription drugs accounts for a significant portion of the sales of the approximately 18 pharmacies that respondent Peterson operates in New York State.

PAR. 7. Respondent Rite Aid Corporation ("Rite Aid") is a corporation organized, existing and doing business under and by virtue of the laws of the State of Delaware, with its principal offices located at Railroad Ave. and Trindle Road, Shiremanstown, Pennsylvania. In 1986, the retail sale of prescription drugs accounted for a significant portion of the sales of the approximately 260 pharmacies that respondent Rite Aid operated in New York State.

PAR. 8. Respondent James E. Krahulec is an individual and was employed by respondent Rite Aid as Vice-President, Government and Trade Relations in 1986 in respondent Rite Aid's principal offices at Railroad Ave. and Trindle Road, Shiremanstown, Pennsylvania.

PAR. 9. Except to the extent that competition has been restrained as alleged herein, members of respondent Chain Association have been and now are in competition among themselves and with other pharmacy firms and other health care providers in the state of New York.

PAR. 10. Respondents' general businesses or activities, and the acts and practices described below, are in or affect commerce, as "commerce" is defined in the Federal Trade Commission Act, 15 U.S.C. 45.

PAR. 11. Respondent Chain Association is, and has been at all times relevant to this complaint, a corporation organized for the profit of its members within the meaning of Section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

PAR. 12. Customers often receive prescriptions through health benefit programs under which a third-party payer compensates the pharmacy for the prescription according to a predetermined formula. The New York State Employees Prescription Program is a prescrip-

tion drug benefit plan made available by the State of New York to its employees, its retirees, certain other persons, and their dependents. There were approximately 500,000 beneficiaries covered by the Employees Prescription Program in 1986. Since July 1, 1986, The Equitable Life Assurance Society of the United States has insured the Employees Prescription Program, and PAID Prescriptions, Inc., a wholly-owned subsidiary of Medco Containment Services, Inc., has administered it.

PAR. 13. Pharmacies are solicited to participate in the Employees Prescription Program. Pharmacies that participate in the Employees Prescription Program accept as payment in full a reimbursement of the ingredient cost of the drug and a professional fee for dispensing the drug. The Employees Prescription Program provides a formula for determining the reimbursement of the ingredient cost of drugs dispensed.

PAR. 14. Absent collusion between or among pharmacy firms, each pharmacy firm would decide independently whether to participate in the Employees Prescription Program, and the State of New York would enjoy the benefits of competition among pharmacy firms.

PAR. 15. In May 1986, PAID Prescriptions, Inc. formally solicited pharmacy participation in the Employees Prescription Program under terms to become effective on July 1, 1986. Among the proposed terms were changes in the reimbursement level for ingredient costs, an increase in the professional fee, and the offer of additional reimbursement for the use of generic drugs. The proposed terms were intended to reduce the price the State paid for the Employees Prescription Program, and thus minimize costs, and yet to offer reimbursement high enough to attract a sufficient number of participating pharmacies to ensure that Employees Prescription Program beneficiaries would have adequate access to medication.

PAR. 16. In 1986, respondents Melville, Fay's, Kinney, Peterson, and Rite Aid ("respondent pharmacy firms") participated in many prescription drug benefit plans offered by third-party payers, including the Employees Prescription Program as it existed prior to July 1. Each respondent pharmacy firm purchased prescription drugs at a cost which on average was below the Employees Prescription Program's proposed level of reimbursement for ingredient costs. Each respondent pharmacy firm would have suffered a significant

loss of customers had its competitors participated in the Employees Prescription Program at a time when it was not participating.

PAR. 17. Even before PAID formally solicited pharmacy participation in the Employees Prescription Program, New York State began to inform pharmacists' associations of the proposed terms. In or before March 1986, respondent Chain Association became aware of the proposed terms of the Employees Prescription Program, and, in response, communicated to members that the extent to which pharmacies participated in the Employees Prescription Program could affect state officials' consideration of the reimbursement level. Respondent Chain Association held meetings at which some respondent pharmacy firms informed other pharmacy firms that they would not participate in the proposed Employees Prescription Program. Respondent pharmacy firms communicated information regarding their own intentions concerning participation in the Employees Prescription Program to other pharmacy firms. Respondent Chain Association and respondent Krahulec communicated, to Chain Association members and other pharmacy firms, information regarding the intentions of Chain Association members and other pharmacy firms concerning participation in the Employees Prescription Program. Through these exchanges of information and other acts, and through the activities of respondent Chain Association and respondent Krahulec, respondent pharmacy firms and other pharmacy firms agreed to refuse to participate in the Employees Prescription Program at the proposed reimbursement level, for the purpose of increasing the level of reimbursement offered by the State of New York under the Employees Prescription Program.

PAR. 18. Respondents have restrained competition among pharmacy firms by conspiring among themselves and others, or by acting as a combination, to increase the price paid to participating pharmacies under the Employees Prescription Program and to deny to the State the benefits of competition.

PAR. 19. The combination or conspiracy and the acts and practices described above have unreasonably restrained and continue unreasonably to restrain competition among pharmacists and pharmacies in New York, and have injured consumers in the following ways, among others:

A. Price competition among pharmacy firms with respect to third-party prescription benefit plans has been and continues to be reduced;

B. The State of New York was coerced into raising the prices paid to pharmacies under the Employees Prescription Program; and,

C. The State of New York has been and continues to be forced to pay substantial additional sums for prescription drugs provided to Employees Prescription Program beneficiaries, including approximately seven million dollars for the eighteen-month period beginning on July 1, 1986.

PAR. 20. The combination or conspiracy and the acts described above constitute unfair methods of competition in or affecting commerce in violation of Section 5 of the Federal Trade Commission Act. The combination or conspiracy, or the effects thereof, are continuing, will continue, or will recur in the absence of the relief herein requested.

Commissioners Azcuenaga and Machol voted in the negative.

STATEMENT OF COMMISSIONER MACHOL CONCERNING ISSUANCE OF CHAIN PHARMACY ASSOCIATION COMPLAINT

The case as presented to the Commission was a very complex one, both factually and legally. It alleged a conspiracy among the Chain Pharmacy Association, a number of drugstore chains operating in New York State, and an executive of one of the chains, to coerce the State into raising proposed prescription drug payments to pharmacies under its employee benefit program by threats of refusal to participate in that program.

Each of the pharmacies and pharmacy chains eligible to participate in the program, of course, was free to make its own decision on whether to agree to do so or to threaten to withhold participation. Liability, under the law we administer, would attach only to conspiracy or collusion in reaching such decisions.

Further, the Noerr Pennington line of cases in the Supreme Court teaches us that even commercial enterprises may not be held accountable under the antitrust laws for conspiring or colluding to exercise their right to petition governments, a right protected under the First

Amendment. Though this area of the law is itself complex, it is clear that many of the activities in which the parties engaged in this case were thus protected.

As to the activities alleged in this case which would not be protected by Noerr, the information we received clearly contained no "smoking gun" evidence of conspiracy. We could find the necessary "reason to believe" that a violation had occurred only on the basis of circumstantial evidence. But, in the Matsushita/Monsanto line of Supreme Court cases, we are taught that an inference of conspiracy must be supported by at least some significant evidence of activity which was logically consistent only with conspiracy. That is, if the activity of each member of an alleged conspiracy was wholly consistent with its pursuit of its unilateral self-interest, that inference must fail.

In my view, the inference in this case -- on the information available to support issuance of a complaint -- fails for that reason. I believe -- again on this information -- that it was in the independent interest of each chain pharmacy to threaten to refuse to participate in the program unless prices were raised, because, if the threat had failed to achieve a price increase, the pharmacy could then have reversed itself and participated. The costs of such a strategy were very limited; the potential gains were very large.

It seems clear that the parties to the alleged conspiracy exchanged a good deal of information. It seems very doubtful that it can be established that they conspired with respect to their decisions to threaten non-participation, however, because they did not need to. Their conversations appear to me to have taken place in the context of protected lobbying activity; their actions seem to have been entirely consistent with their individual economic self-interest; and there simply was not sufficient evidence from which I could find reason to believe in the existence of an unlawful conspiracy.[1]

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[1] Should I have occasion to review this matter following a proceeding before an Administrative Law Judge, I will of course reconsider the factual issues presented solely on the basis of the adjudicative record.

INITIAL DECISION BY

MORTON NEEDELMAN, ADMINISTRATIVE LAW JUDGE

MAY 17, 1991

I. STATEMENT OF THE CASE

The Commission's complaint, which was issued on April 19, 1989, charges a combination or conspiracy in violation of Section 5 of the Federal Trade Commission Act. The complaint centers on an attempt by New York State to reduce the reimbursement received by pharmacies participating in the state's prescription drug plan which benefited some 500,000 public employees, retirees, and their dependents. According to the complaint, the five named pharmacy chains, an executive of one of these chains, a trade association, and unnamed other pharmacy firms had allegedly combined or conspired to refuse to participate in the state's reduced-rate reimbursement initiative. These acts are said to have coerced New York into increasing the reimbursement rate, and to deprive the state of the benefits of competition.

Of the five pharmacy chains named in the complaint -- Fay's, Kinney, Melville (a parent of the CVS chain), Rite Aid, and Peterson -- all but Peterson consented to the entry of a cease and desist order. The one individual named, James E. Krahulec (an officer of Rite Aid), also consented as did the trade association, Chain Pharmacy Association of New York State (CPA). Three other pharmacy chains (Brooks, Carls, and Genovese) consented to the entry of cease and desist orders prior to the issuance of formal complaints. The respondents named in the complaint, and the pre-complaint consenters are treated herein as alleged conspirators.

Peterson vigorously maintains that it has not participated in any illegal combination or conspiracy. Its answer dated May 25, 1989, denies the substantive allegations of the complaint and raises the affirmative defense of the Noerr-Pennington doctrine.

In the prehearing state, both sides were allowed extensive discovery, including a protracted deposition period. Complaint counsel's case-in-chief was heard between December 3 and

December 14, 1990. The defense case was presented during the week of December 17. A motion to receive uncontested rebuttal exhibits was granted on January 16, 1991, and the record was closed for the receipt of all evidence on January 31. During the hearings, complaint counsel and counsel for Peterson were given full opportunity to be heard and to examine and cross-examine the witnesses. The parties filed their main briefs and proposed findings on February 25. Answers to proposed findings and reply briefs were filed on March 18, 1991.

After reviewing all the evidence, as well as proposed findings and briefs submitted by the parties, and based on the entire record, including my observation of the demeanor of witnesses, I make the following findings of fact:[1]

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[1] Proposed findings not adopted in the form or substance proposed are rejected as either not supported by the entire record or as involving cumulative, immaterial, or irrelevant matters.

The following abbreviations are used throughout in citing to the record:

CX (Complaint counsel's Exhibits)

RX (Respondent's Exhibits)

Testimony is cited by the name of the witness, followed by transcript page as in Rosenberg 1885-87.

The appearances of the witnesses were as follows:

Name	Called By	Testimony Pages
Priscilla E. Feinberg (New York State)	Complaint Counsel ("C.C.")	350-577
Stephen B. Kavanaugh (New York State)	C.C.	581-735
Thomas Hartnett (New York State)	C.C.	801-982
Paul Wutz (Blue Cross of Western New York)	C.C.	989-1078
David T. Painter (FTC Accountant)	C.C.	1082-1498
Leonard J. De Mino (Natl. Ass'n of Chain Drugstores)	Respondent ("Resp.")	1560-1604
John T. Kelley (formerly, Natl. Ass'n of Chain Drugstores)	Resp.	1606-1649

II. FINDINGS OF FACT

A. *Identity Of Respondent And The Alleged Conspirators*

1. Peterson Drug Company of North Chili, New York, Inc. (hereinafter "Peterson" or "respondent") is a New York corporation with its headquarters located at 68 North Main Street, Oakfield, New York. In 1986, Peterson was the corporate umbrella for 15 affiliated corporations that operated 18 drugstores under the "Peterson" trade-name. Peterson owned four of the stores outright, and it controlled at least 51% of the stock in the affiliated corporations that owned the other 14. The 18 Peterson stores were located in the small Western New York communities of Newfane, Genesco, Williamsville, Akron, Snyder, Chili, Brockport, Bath, North Chili, Albion, Lockport, Wellsville, Chafee, Ontario, Derby, Alden, Perry, and Penfield.[2]

2. For all practical purposes, Gerald Rosenberg, President of Peterson, represented respondent during the entire course of dealings relevant to this proceeding.[3]

3. Peterson is the smallest chain named in the Commission's complaint. In 1986, Rite Aid (New York State's largest chain) had about 260 drugstores, CVS approximately 100, Fay's between 110 to 120, and Kinney 23.[4] Of the other alleged conspirators, Genovese

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Walter J. Floss, Jr. (former New York State Senator)	Resp.	1653-1698
Gerald R. Rosenberg (President, Respondent Peterson)	Resp.	1103-1920

[2] Complaint and Peterson's Answer ¶ 6; Rosenberg 1709-10, 1723, 1755; CX's 16 "I", J, 682A, B, 2070Z-20, Z-21; RX 275. Aspects of the relationship between the Oakfield headquarters and the individual drugstores particularly relevant to this proceeding are treated in Finding 70.

[3] Rosenberg 1715-16, 1718-21, 1745-53, 1776-86; CX's 2Z-240-Z-241, 16K, Z-112, 725J-L. Rosenberg is President of each of the affiliated Peterson corporations except for the corporate entity controlling the Newfane store. CX 726B.

[4] Complaint ¶'s 3-7 and Answers; CX's 9Q, 12J,K, 23M,N, 154A-P, 181A, 2062Z-70.

owned 75 stores, Brooks (a subsidiary of Adams Drugs) about 60 to 70, and Carls 42 or 43.[5]

4. James E. Krahulec is the only individual named in the Commission's complaint. He was Rite Aid's Vice President for Government and Trade Relations (*i.e.*, the company's principal lobbyist)[6] and played a key role in the conduct challenged by the complaint.[7]

5. Chain Pharmacy Association ("CPA") is a New York State not-for-profit corporation organized in 1984 to advance the common business interests of its pharmacy members by lobbying state legislators and officials. In 1986, the founding members of CPA were 12 pharmaceutical chains doing business in New York State (Peterson, Brooks, Carls, CVS, Rite Aid, Fay's, Genovese, Kinney, SupeRx Drugs, Duane Reade, Revco, and Walgreen) and the pharmacy operations of Supermarkets General and Kroger, two supermarket chains.[8]

6. The members of CPA competed against each other in the sale of pharmaceutical prescriptions, nonprescription drugs, and the myriad nondrug items sold by drugstores.[9] Peterson's chief competitors in 1986 were Fay's, Rite Aid, and CVS.[10]

7. CPA had no staff of its own. Essentially, the work of the association was carried out by its Executive Director, Peter Zimmerman, a retained trade association expert.[11] Zimmerman and Krahulec

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[5] CX's 822A, 1212, 1989D, 2249L, 2250"O", 2252"O", P, 2254L-N, 2269G.

[6] Complaint ¶ 8 and Krahulec Answer; CX's 20H, J, K, U-W, 2194"I".

[7] *See* Findings 55-59, 74-81.

[8] Complaint ¶ 2 and CPA Answer; Kelley 1612, Rosenberg 1715-16; CX's 2"I", J, N, "O", 20U, V, 41E-G, 2199H, 2248Z-26, 2249Z-42, 2252N. Revco owns Carls, but decisions respecting participation in PAID I and other matters relevant to this proceeding were left to the management of the subsid 2251Z-71. Kroger owned SupeRx until December 1986. CX 2266K. Supermarkets General operated pharmacy departments in its "Pathmark" supermarkets as well as its free-standing "Heartland" and "Pharmacity" drugstores. CX's 1305B, 2191Z-264.

[9] Complaint ¶'s 2 and 9 and Answers; CX's 6Z-2-Z-4, 7V, 18Z-67, 22U, 2060L, 2062Z-21-Z-25, 2189Z-64, Z-65, 2206Z-9, Z-10, 2269G.

[10] CX 2070Z-55.

[11] CX's 2H, "I", J, M, 2199G.

of Rite Aid carried the workload for the pharmacists during the events described herein.[12]

8. The object of the alleged conspiracy, PAID I, and its eventual successor PAID II, were third party prescription plans whose implementation involved a stream of interstate commerce flowing from consumers and pharmacists in several states,[13] to an administrator located in New Jersey,[14] and then back to the pharmacists for reimbursement for the cost of pharmaceuticals manufactured throughout the United States.[15] While most of Peterson's pharmaceuticals were purchased from a New York distributor, its nonprescription business involved a substantial volume of purchases from out-of-state suppliers.[16] Moreover, prescription and nonprescription business are closely linked, and this connection was deeply implicated in the alleged scheme since the pharmacists knew that if PAID I went forward without their participation, they stood to lose both segments of a drugstore's trade.[17] Respondent has not pressed the issues of interstate commerce or the Commission's jurisdiction.[18]

B. *NYSEPP And The Development Of PAID I*

9. New York State in its capacity of employer has ultimate responsibility for a prescription drug program (New York State Employee Prescription Program or "NYSEPP") that is part of the

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[12] *See* Findings 54-59, 74-81.

[13] Although NYSEPP members are concentrated in New York, the plan also covers state employees and retirees who live outside of New York as well as the out-of-state pharmacies enrolled in the plan in order to serve these out-of-state members. Feinberg 360, Kavanaugh 614.

[14] Feinberg 371-72, Kavanaugh 614.

[15] Feinberg 354, 473-74; CX 2070Z-24. The flow of commerce (or, if you will, the interruption in the flow of commerce) continued as PAID was compensated by the state for administering the plan. Feinberg 459, Kavanaugh 614.

[16] CX 725M.

[17] *See* Findings 42-52.

[18] Respondent Peterson's Reply To Complaint Counsel's Proposed Findings Of Fact at 327-330 (March 18, 1991).

package of employee and retiree health benefits the state has negotiated with the principal unions.[19]

10. In 1986, NYSEPP insured approximately 500,000 public employees, retirees, and their dependents.[20]

11. The Governor's Office of Employee Relations (OER) was the state agency charged with responsibility for bargaining with the unions over the public employees' health benefits package including NYSEPP, the prescription drug component. OER shared with the state's Department of Civil Service and Budget Department responsibility for designing a NYSEPP program that met the terms of the negotiated health package.[21] The plan was actually administered by Civil Service.[22]

12. NYSEPP in its various configurations (PAID I, PAID II, and their predecessor) was a third party program. Instead of paying the prevailing retail price for a prescription, a state employee or retiree, who was enrolled in the plan, presented a card and was charged only a small co-payment fee. The participating pharmacy submitted the claim to a third party payer (the plan administrator in the case of PAID I) for processing and reimbursement of the cost of pharmaceutical ingredients. In addition, the administrator paid the pharmacies a dispensing or professional fee. The plan administrator, in turn, was reimbursed by an insurer who ultimately looked to the state for payment in the form of the premium expense New York incurred for its employees.[23] The plan was said to have cost the state roughly $104 million in 1986.[24]

13. Almost from its inception in 1980, the cost of NYSEPP had grown by leaps and bounds, far exceeding the rise in the medical

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[19] Feinberg 358-60.

[20] Feinberg 359-60. In addition to state employees, NYSEPP covers participating local (town, county, and school district) employees. Feinberg 359.

[21] Feinberg 355-58, Kavanaugh 582-84.

[22] Kavanaugh 582, 584.

[23] Feinberg 358-59, Kavanaugh 584-85, 589, Wutz 1006, Painter 1405. For its part in this process, the state paid the administrator 50 cents per claim. Feinberg 459, Kavanaugh 614.

[24] CX 1763A.

consumer price index. Between 1980 and 1983 alone, the cost to the state for NYSEPP premiums rose from $25 million to $90 million with no end in sight.[25] These runaway costs were mainly attributable to an aging population of insureds (with a concomitant increase in usage) and rising pharmaceutical prices.[26]

14. The tripartite division of functions in the administration of NYSEPP between New York State, an insurer, and an administrator, in no way diminished the overriding role of the state as the prime mover for a cost-containment initiative. The premiums that New York as a purchaser of health insurance benefits paid to the insurer on behalf of its public employees was a function of the ingredient reimbursement costs anticipated and actually experienced by the insurer. With these mounting costs in mind, OER began considering potential cost-containment strategies as early as 1984.[27]

15. The cost-containment initiative eventually adopted by the state centered around the concept of a reduction from Average Wholesale Price ("AWP"). AWP is the wholesale list price for each drug item. It is either suggested by the manufacturer or developed by the publishers of commonly-used industry sources such as the Red Book, Blue Book, or Medispan.[28] Although the AWP purports to show the average price which pharmacists are paying, it is universally acknowledged in the industry that drugstores purchase most of their pharmaceuticals at steep discounts off AWP and that these discounts reflect a firm's volume of purchases.[29] Peterson, for example, during 1985 and the first half of 1986, believed that it

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[25] Feinberg 363-64, Kavanaugh 589, 604-05, 668, 682-83, Hartnett 973; CX's 1763A, B, 1785F; RX 254"I".

[26] Feinberg 495-98; CX's 1763A, B, 1785, 2262Z-212. Another frequently cited cause of rising prescription prices is the reluctance of doctors to prescribe generic substitutes for branded drugs. CX 1763B.

[27] Feinberg 363-64, 457-58, 485, 571-72, Kavanaugh 589, 605, 667-68, Wutz 1006, 1015-16; CX's 732A, 1084A, 1785F, 1868Z-6-Z-13, 2257Z-51, 2262Z-108; RX's 86A, 131A, 134D, 142B, 254"I".

[28] Painter 1092-93; CX's 2062Z-115, Z-116, 2069Z-44.

[29] Feinberg 372-375, 379, Kavanaugh 604-05, 696, Hartnett 815, Wutz 1022; CX's 6U,V, 1685H, 1759C, 1760A, 2257X,Y, 2268Z-14, Z-15; RX's 97A, 2038, 254Z-31, Z-35.

purchased from its main wholesale supplier at AWP minus 14%.[30] Studies had shown that industry-wide the average discount off AWP was 16%, and still larger discounts were available to the big chains.[31] Thus Fay's purchased pharmaceuticals at approximately AWP minus 21%,[32] Brooks at between AWP minus 16% to AWP minus 18%,[33] CVS at about AWP minus 21%,[34] Genovese at between AWP minus 16% to AWP minus 22%,[35] Kinney at AWP minus 20%,[36] and Rite Aid at AWP minus 21%.[37] Carls must have acquired pharmaceuticals at comparable discounts since its warehouse was billing its own stores at AWP minus 15%.[38]

16. PAID I, the cost-containment plan based on a reduction from AWP that was eventually selected by OER and the other state agencies charged with responsibility for NYSEPP, was adopted following an administrative process in which the depth of the state's commitment to cost-containment and its lack of alternatives, prevailed over pharmacist opposition to being singled out as the main target for this economy drive. (Findings 17 to 33.)

17. The experience of NYSEPP's 1980-86 administrator (and joint-underwriter), Blue Cross of Western New York ("BCWNY"), was reviewed. BCWNY, which was well aware of the availability of sharp discounts off AWP, had tried to reduce costs by setting the reimbursement rate at actual acquisition cost plus a $3.00 dispensing

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[30] Rosenberg 1766; CX 725D. The rate of discount increased to AWP minus 15% after July 1, 1986. Rosenberg 1887-88; CX's 679A, 725D, 2070S.

[31] CX's 1084D, 1533A-Z-19, 2257X, Y.

[32] Based on Fay's pharmaceutical purchases for NYSEPP prescriptions filled between February l, 1986, and January 31, 1987. Painter 1433-34; CX's 2203Z-14, Z-15, 2317A-D, 2324.

[33] CX 2252V.

[34] CX's 2189Z-219, 2191Z-22, Z-23, Z-94, Z-95, Z-105, Z-106, Z-110, 2268Z-21.

[35] CX 's 2247Z-7, Z-23.

[36] Based on Kinney's pharmaceutical purchases for NYSEPP prescriptions filled between January 1, 1986, and December 31, 1986. CX's 2318, 2319. *See* Painter 1433-34 for the calculation made to arrive at the discount off AWP.

[37] CX's 2200Z-60-Z-63, Z-113, Z-114, Z-238, Z-239.

[38] CX 2251W.

fee. It was virtually impossible, however, for BCWNY to determine actual acquisition costs. The source of this difficulty was made readily apparent on the record which shows that for the purpose of filing claims with BCWNY, Peterson was billed by its wholesale supplier at full AWP although its actual costs were much lower.[39] Resigned to the futility of even attempting to monitor such creative bookkeeping, BCWNY eventually departed from the actual acquisition cost formula, and by 1983 settled on a sliding scale reimbursement rate based on discounts off AWP (a tamper-proof benchmark) of 1% to 9% for independents and 12% for chains.[40] At these discounted reimbursement rates, BCWNY had no difficulty in obtaining a full array of providers as virtually all New York pharmacies participated in NYSEPP.[41]

18. OER also surveyed what other employers, both public and private, were doing about cost-containment. Experts were consulted.[42] An examination of a 1984 U.S. Department of Health and

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[39] Feinberg 360-61, Kavanaugh 584-85, 676-77, Wutz 994-95, 998-1000, 1003-04, 1014-15, 1022, 1031-32; CX's 359A, 1084D 1372B-G, 2070Z-41, 2261"O", 2261Z-19, Z-20, Z-53, Z-54, 2268Z-20, Z-21. This practice nicely illustrates the fictive quality of full AWP. Peterson's wholesale supplier offered respondent two options in billing: a choice between an invoice showing both the full AWP and the discount, or one with full AWP only, followed later by a separate credit for the discount. The full AWP- separate credit option -- Peterson's choice -- was specifically designed for use when a third party administrator audited the drugstores in search of actual acquisition costs. Rosenberg 1732-33, 1889-91, 1916-17; CX's 1372C, 2070S-Y. Peterson's practice was by no means unique. BCWNY knew that pharmacists and wholesalers "have been joining forces to beat our system" (CX 2267Z-212), but there was little it could do about it. CX's 2267Z-213, Z-214. *See also* CX's 1372B-G.

[40] Wutz 994-95, 999-1000, 1005-06; CX's 878E, 1372A-G, 1836Z-22, 2267Z-92-Z-108, 2268V; RX 254Z-36. This formula applied to both BCWNY's NYSEPP and non-NYSEPP (*i.e.*, "community") plans. The two plans had a small dispensing fee differential -- 20 cents higher for NYSEPP -- until January 1986. Wutz 993-95, 1005; CX's 878B, E, 942B, 2267Z-132, Z-133.

[41] Feinberg 391, Wutz 1037-38; CX's 2267Z-88, Z-89, Z-114, Z-115, Z-122, Z-123, 2268Z-1.

[42] Feinberg 376-78, Kavanaugh 696, Wutz 1014-15; CX 1763B; RX 258"I".

Human Services report confirmed the prevalence of large discounts off AWP.[43]

19. Conceivably New York might have settled on a plan that could have had a more serious impact on retail pharmacists than a reduction in the ingredient reimbursement rate. The state, for example, might have provided prescription coverage for its employees through a single chain, a designated group of preferred providers, or through mandatory use of mail order.[44] There is no evidence, however, that these alternatives were seriously pursued in 1986.

20. The review described in Findings 17 to 19 led to the conclusions that New York was not doing enough to keep prescription costs in check and that its options for doing more were limited. Determined, nevertheless, to set in motion a cost-containment initiative, OER sent out a "Request For Proposal" ("RFP," in the jargon of the bureaucracy, is a notice that a program is open for bids) on January 22, 1985. The RFP directed that bids should provide for ingredient cost reimbursement at the lesser of 90% of actual acquisition cost or usual and customary charges. The dispensing fee was to be $2.60 per prescription.[45]

21. In response to this first cost-cutting initiative, PAID Prescription, Inc. ("PAID") a New Jersey-based third party plan administrator (but not insurer) submitted a bid which met the OER target of AWP minus 10%. Based on its limited but successful experience with reduced-rate plans, PAID assumed that a plan of the size of NYSEPP would have no difficulty in attracting an adequate array of participants at the AWP minus 10% rate.[46] The first RFP, however, was withdrawn in late 1985. As respondent would have it, the RFP was withdrawn because OER, anticipating widespread pharmacy rejection, beat a hasty retreat from the less than AWP formula, thus proving that it was a non-starter. While the record shows that pharmacy opposition was already apparent when the first

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[43] CX's 1533B, C, 1759E.

[44] Kavanaugh 684-88, Hartnett 926-27; CX's 1084B, 1989A.

[45] Kavanaugh 605, 671; CX's 1868A-Z-27, 2260"I"; RX's 258"O", P.

[46] RX's 257M-"O".

RFP was withdrawn,[47] there is no evidence that the state had decided at that time to abandon the less than AWP formula. As far as this record will allow, the first RFP was withdrawn because it was proposed on the assumption that the state legislature would pass an enabling law allowing New York to function as its own insurer of NYSEPP. This legislation never passed.[48]

22. The second RFP was announced on December 5, 1985. Unlike the first, no specific reduction from AWP was targeted. Instead, OER said that it was aiming for the control of costs through the use of generic drugs and mail order, but the AWP issue was left open as the RFP merely requested that bidders explore other cost containment possibilities.[49]

23. There were six responses to the second RFP. In this round, the PAID bid was a joint effort of Equitable Life Assurance as the insurer and PAID (Equitable's subcontractor) as the administrator. The PAID-Equitable bid was grounded on AWP minus 5% for both chains and independents. But after the bid was accepted, the reimbursement formula was changed by the state (a combined effort of OER, Civil Service, and Budget) to AWP minus 12% for chains and AWP minus 8% to 2% for independents depending on volume. A professional or dispensing fee of $2.75 to $3.00 (depending on the availability of 24-hour service, deliveries, and patient profiles) was to be added to each prescription. The bid also included a generic drug component and a direct mail provision. This essentially was PAID I.[50]

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[47] CX's 2262"I", J; RX's 107A-J.

[48] Kavanaugh 591-92; CX 2261Q.

[49] Feinberg 374-75; CX's 1785A-Z-64, 2261Z-27, 2262J.

[50] Feinberg 376, 378, 389, Kavanaugh 594; CX's 1084A-D, 1562A, 1759A-D, 2257Z-20, Z-21, 22595, 2260R, S, 2261Z-47, 2262Z- 07, Z-108; RX's 257Z-6-Z-8. The RFP specifically reserved New York's prerogative of requiring the selected contractor to modify or make additions to its proposal in order to meet the state's specifications. CX 1785G. As it happens, the reimbursement rate adopted by the state was in line with the bid of Empire Blue Cross/Blue Shield, which had recommended AWP minus 12% for chains and a sliding scale for independents. Feinberg 384, 518-19, Kavanaugh 595-96; CX's 1566Z-12, 1836T, 2222C, 2261Z-34, Z-36.

24. The entire state bureaucracy concerned with NYSEPP recommended the selection of Equitable Life Assurance as the insurer, PAID as the administrator, and PAID I as the reimbursement formula. Since the state retained discretion as to the reimbursement formula, the final selection was mainly based on an assessment of the educational and administrative capabilities (*i.e.*, the ability to inform members about the plan, to process "plastic," and to fulfill the mail order component) of the highest-ranked bidders.[51]

25. PAID I definitely was not endorsed by the representatives of the pharmacy community. They not only were opposed to its substantive provisions but they also perceived a lack of good faith on the part of the state in the very process by which the PAID I formula was developed and eventually adopted. Although OER had met with pharmacists for the purpose of hearing their grievances against the less than full AWP formula and to consider alternative cost-cutting strategies, the pharmacists felt that their complaints and suggestions had been given short shrift.[52] Nevertheless, there is no suggestion in the record that the state was not fully apprised of the pharmacists' views.[53] They advanced arguments in opposition to PAID I, which had been made at the first intimation that the state might adopt a less than full AWP formula, and which were to be repeated until the demise of this cost-cutting initiative in late June 1986. (Findings 26 to 32.)

26. According to the pharmacists, just as their costs of dispensing drugs were rising, their margins would be unfairly squeezed by the proposed discount off AWP.[54] While the pharmacists had little in the way of concrete support for their arguments -- Peterson, for example,

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[51] Feinberg 363-71, Kavanaugh 594, 596-600, 607, 696; CX's 1084A, 1562A-D, 1563A-D, 1914A-H; RX's 64A-D. The selection of PAID may also have been influenced by the large number of New York pharmacies it already had on line for its non-NYSEPP third party plans. Feinberg 369; RX 64D.

[52] Hartnett 853-72, Rosenberg 1746-47, 1773-76; CX's 2T, Z-48-Z-53, Z-82, Z-83, Z-265, Z-266, 5Z-11, Z-18, 53B, C, 732A, B, 733A, B, 1876B, C, 2069Z-138, 2261Z-55, Z-66; RX's 6A, B, 106A-C, 108A, B, 183A-C, 198A-K, 203A, B, 315A-C.

[53] *See* Hartnett 978.

[54] Rosenberg 1752, 1757-60, 1768; CX 1685G.

in 1986 did not know its actual costs for filling a prescription[55] -- there is no dispute that the confrontation between the state and the pharmacists came down to the issue of how much of the pharmacists' profits, as reflected in their ability to purchase at discounts off AWP, were to be captured by the state.[56] From New York's perspective the

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[55] Rosenberg 1878-79; CX's 16Z-23, 2070H.

[56] Feinberg 571-72, Kavanaugh 613, Hartnett 858-59, Wutz 1022; CX 732A; RX 107G. No claim was made by any proponent of the less than full AWP formula that dispensing fees were intended to cover all the costs incurred by a pharmacy in filling a prescription. *See* Feinberg 478-81, 574-76, Kavanaugh 693-95, Wutz 998-99, 1020-23. Although the PAID I dispensing fees (a $2.75 basic fee and $3.00 for full service pharmacies) were higher than the schedule used by BCWNY in administering NYSEPP prior to PAID I (Feinberg 389, 574, Wutz 1021; CX's 1685G, H, 1759C, 2261Z-47), it is fair to conclude on this record that the actual cost of dispensing drugs was higher than the amount generally allowed in any third party plan. *See* CX's 16Z-22, Z-23, 2200Z-256-Z-281; RX's 107F, G, 325A-Z-148. There is little, however, in the record to suggest that the level of the dispensing fee was the motivating cause for the pharmacists' anti-PAID I animus, and an argument along these lines would be difficult to sustain given the proof that in the face of competition, pharmacists were willing to waive or discount a comparable amount -- insurance co-payment fees -- in order to retain valuable prescription business. Kavanaugh 609; CX's 7Z-22, Z-23, 11Z-34, Z-35, Z-153-Z-158, 2061Z-82, Z-83, 2062Z-19, Z-20, 2064Z-12, 2069Z-143, 2070Z-14, 2189Z-30, Z-31, Z-212-Z-214, 2196Z-75, Z-76, 22065, T, 2207Z-34, Z-35, 2261Z-21, Z-22; RX 107"I". As indicated in Note 192, *infra*, several of the alleged conspirators believed that there were profits to be made in PAID I notwithstanding low dispensing fees; moreover, even modest profits from this prescription business would have generated very profitable front-end trade. *See* Findings 42-51. Neither the litigants in this case nor anyone involved in the state-pharmacists dispute has made a useful calculation as to how various factors -- discounts off AWP, waiver of co-payment fees, package sizes, dispensing fees, generic drug incentives, volume of prescription business represented by the plan, additional front-end business attributable to a third party plan -- interact on bottom-line drugstore profitability. *See, e.g.* Feinberg 504-05, Kavanaugh 693, Rosenberg 1809-13; CX's 6"O", P, Z-7, Z-12, Z-24, 13Z-37, 16Z-23, 2070Z-54, 2189Z-202, Z-203; *see also* Painter 1478-81. As far as one can tell from this record, even with respect to only one part of this equation -- the cost of pharmaceuticals -- discounts off AWP may just be the starting point of any inquiry since prices at the wholesale level are also influenced by cash payment discounts, large size package reductions, free goods, seasonal specials, rebates, price increase adjustments, and buy-ins. CX's 2260Z-106-Z-111. In short, all that the record shows is that the state wanted the pharmacists to contribute, in the form of a discounted rate for ingredient reimbursement, some part of their profits -- as reflected in the ability of drugstores to purchase at the less than AWP rate -- to

use of a reimbursement formula based on a discount off AWP, not only interjected an incentive for pharmacies to compete against each other in seeking even greater discounts from manufacturers, but it also gave the state a direct stake in the outcome of that competition.[57]

27. The pharmacists expressed deep resentment over being targeted for the state's cost-containment initiative while powerful pharmaceutical manufacturers were left unscathed.[58] Moreover, from the pharmacists' viewpoint the difference between AWP and their actual costs was a hedge against inflation since it represented a relatively fixed percentage of the increasingly high prices charged by these same manufacturers.[59]

28. The state was challenged by the pharmacists about its proposed distinction between chains and independents as the basis for the PAID I formula.[60]

29. The state was also questioned about the very definition of a "chain" for purposes of the sliding scale reimbursement formula.[61] Despite some uncertainty in this area, the Peterson stores were told as early as May 1986 that they would be treated as independents and thus entitled to compensation at the rate of AWP minus 2%, 5%, and 8% (the sliding scale for independent stores depending on volume) rather than the flat rate of AWP minus 12% for chains.[62] And while the state may have contributed to pharmacist confusion by vacillating between several definitions of a chain depending upon such consi-

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reducing the cost of NYSEPP, and the pharmacists were not especially receptive to this notion. Feinberg 486, 571-72, Kavanaugh 603-07, 613, 622; CX's 732A, B; RX's 107G, 254Q, R, 257Z-7-Z-13, Z-25.

[57] Kavanaugh 625-26, 632-33, 683-84, 697, 700.

[58] Feinberg 497-98, Rosenberg 1757-58; CX's 20Z-157, 733A, 2199Z-220, Z-235. In one sense, however, PAID I did target brand name drug manufacturers since it included a generic incentive. *See* Note 72, *infra*, and 23Z-59, Z-60.

[59] RX 107G.

[60] Feinberg 400, 515-16, Rosenberg 1759; CX's 10L, 812, 2303A. Note, however, that Fay's did not believe this distinction was unfair. CX's 9Z-26, Z-27.

[61] Rosenberg 1753; CX's 2Z-26-Z-28, 2069Z-135, 2070Z-56, Z-57, 2199Z-220, Z-235.

[62] CX's 15X, Y, 711; RX's 260Z-31, Z-32, Z-103, Z-104.

derations as number of stores, common ownership, and the use of central billing,[63] there is no evidence that either the state or PAID wavered in its classification of Peterson during the entire relevant time period. To the contrary, by June its status as a series of independents had been specifically confirmed.[64]

30. Going beyond the reimbursement level, PAID I was opposed by the pharmacists because it contained a direct mail component.[65] As the retail pharmacists would have it, mail-order pharmacy posed a medical danger to patients who, in the absence of a pharmacist to monitor misuse, might possibly ingest conflicting drugs.[66] To the state officials responsible for meeting the cost of third party plans, the retail pharmacists' argument was a red herring since the plan had installed multiple checks to insure safety.[67] Besides, mail order sales were essentially confined to "maintenance prescriptions" -- the drugs

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[63] Feinberg 410, 516-18, 531-32, Rosenberg 1821-24; CX's 2Z-26-Z-28, Z-89, Z-90, 16Z-117, 728A, 733A, 1989A; RX's 260Z-103, Z-104.

[64] Rosenberg 1824, 1874, 1876; CX's 728A, B, 2070Z-57. Although the record shows that the Peterson stores had been designated as independents in May, 1986, and that this determination had been confirmed prior to June 10 (Feinberg 410), Rosenberg claimed at trial that it was not until June 15 or 16 that he was certain of his status as a series of independents. Rosenberg 1821-24; CX's 16Z-29, 2070Z-57. Under Rosenberg's timetable, it would mean (a) that Peterson was prepared on June 12 to participate in PAID I (if its competitors had done likewise) notwithstanding the possibility that it would have been reimbursed at the chain rate of AWP minus 12% (*see* CX 681A), and (b) on June 18 when the Akron store departicipated (*see* Finding 69), Rosenberg knew that Peterson would be treated as an independent to be reimbursed at AWP minus 2% to AWP minus 8%. Rosenberg 1876.

[65] Feinberg 399-400, Kavanaugh 623-24, 689-90, Hartnett 858-59, Rosenberg 1757-58, 1768-69; CX's 1685G, 2199Z-177. A sore point with the pharmacists was the designation of a company affiliated with PAID as the exclusive mail-order distributor. CX's 2092A, 2204Z-238; RX 97B.

[66] CX's 2Z-3-Z-5. The depth of this concern is suspect since two chains, Fay's and Rite Aid, operated mail-order departments, while another, CVS, had submitted a bid of its own for the NYSEPP mail-order business. CX's 11Z-38, 20Z-39, 1914A, 2189Z-259-Z-324, 2262Z-134, Z-135. *See also* CX 2202Z-132, notes of a CPA meeting, in which CVS reported: "MAIL ORDER: After a long discussion it was decided that the committee could not oppose the concept because of the number of members who are or would be involved with mail order."

[67] Kavanaugh 709-12, Hartnett 882-83. *See also* CX 1720B.

which doctors prescribed without any time limit in order to stabilize chronic conditions such as arthritis, hypertension, or heart disease.[68] The pharmacists more or less conceded that the sale of maintenance drugs was a readily identifiable segment of the overall prescription universe, and argued alternatively that loss of this business adversely affected other sales since it reduced the frequency of pharmacy visits.[69] Despite opposition by pharmacists to mail-order sales, they have participated in NYSEPP plans that had such provisions both before and after PAID I.[70]

31. Another source of pharmacy opposition to the NYSEPP cost-cutting initiative was the prospect that the same approach might be used in Medicaid or other New York State plans, especially EPIC (Elderly Prescription Insurance Council), New York's prescription plan for the elderly.[71]

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[68] RX's 97B, 312C. The state's experience both before and after the adoption of the various PAID formulae was that about 10% of all prescriptions were filled through the mail. Feinberg 379-83, Kavanaugh 611; CX's 1718A, 1763D; RX's 95D, 97B.

[69] Kelley 1618, Rosenberg 1757-58, 1768-69; CX's 16Z-11, 24Z-19, 2199Z-235.

[70] Feinberg 362, Kavanaugh 623-24. The addition of a mail-order component to the NYSEPP plan underwritten by Blue Cross/Blue Shield had not caused any retailer defections. CX's 1373, 2180, 2267Z-164, 2268P, Q.

[71] Feinberg 500-04, Rosenberg 1769, 1802; CX's 2Z-113, Z-123, Z-124, Z-138, Z-139, 3Z-51, Z-52, 5Z-56, Z-57, Z-60-Z-63, 20Z-10, Z-12, Z-23, Z-36, Z-109, Z-137, Z-173, 24Z-21-Z-24, 492, 681A, 733B, 2070Z-67, Z-68, 2193Z-14, Z-15, 2194Z-40, 2199Z-157, Z-158, Z-235, 2204Z-15, 2250Z-38-Z-41.

32. All in all, there was little in PAID I that the pharmacists liked except for the concept of a generic drug incentive[72] and a provision for rapid claim reimbursement by the administrator.[73]

33. The arguments made by the pharmacists did not persuade the state to relax its cost-containment initiative, and on March 7, 1986, OER awarded the NYSEPP contract in the form of PAID I to the PAID-Equitable team.[74]

C. *July 1 And The Pressure On The State*

34. On March 26, 1986, OER informed CPA that effective July 1, 1986, PAID I would go into effect.[75] With this starting date in mind, PAID began soliciting pharmacies on May 5, 1986. A formal solicitation was used since this was a new plan, some pharmacy opposition was anticipated, and state officials had to be certain that there were a sufficient number of drugstores on line by the July 1 starting date to service the huge number of NYSEPP members whose

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[72] Generic drug programs are designed to reward pharmacists for steering customers to generics as substitutes for the more expensive but doctor-prescribed branded items whose patents have expired. A generic drug component was supported by the pharmacists. Feinberg 385, Kavanaugh 613, Hartnett 973-74; CX's 2Z-5, 2-39, Z-44, Z-46, 11Z-39, 20Z-32-Z-34, 2194Z-15, 21992-14, Z-15, 2261Z-24, Z-25, 2262Z-71, Z-72; RX's 95L-N. Under PAID I, pharmacies were to be paid 25% of the difference between the costs of the generic and brand name drugs, with a minimum reimbursement of 75 cents. The co-pay was reduced from $2 for branded to $1 for generics. Feinberg 384-85, Kavanaugh 611-13; CX's 1084B, C, 1974B. Even with respect to the generic component, the pharmacists were dissatisfied with PAID I. They thought they should receive the generic incentive on all refills and not merely the initial prescription since they had converted the consumer to the use of the substitute. Rosenberg 1816-17; CX 812. Incentives aside, the pharmacists knew that generics were generally more profitable for them than branded drugs. CX's 16Z-9, 18Z-25, Z-26, 2061Z-172, 2196Z-11-Z-13, 2200Z-238, 2201Z-42, Z-43, 2207M, N, X-Z-2, 2267Z-19.

[73] CX's 1084C, 1185P, 2254Z-16, Z-11; RX's 107"I", 122B, 254Z-26.

[74] Kavanaugh 597-600, Hartnett 880; CX's 1563A-D.

[75] Feinberg 394-95; CX's 380B, C.

non-deferable prescriptions had to be filled.[76] Moreover, the use of a solicitation procedure was necessary in order to determine which discount off AWP in the sliding scale formula was to apply.[77]

35. Despite the organized pharmacy community's opposition to PAID I, and notwithstanding some uncertainty about having an adequate number of drugstores on line by July 1, the early favorable response of several chains to the solicitation (Findings 36 to 40) eased the pressure of the July 1 starting date as both state and PAID officials believed that countervailing competitive pressures would soon force others to sign up.[78]

36. On May 13, 1986, the Peterson drug store in Akron, New York, informed PAID that it would participate in PAID I.[79]

37. On May 15, PAID was told by Kinney that it intended to participate in PAID I.[80]

38. On May 16, Fay's submitted a notice of its intention to participate in PAID I.[81]

39. Carls signed up for PAID I on May 22.[82]

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[76] Feinberg 391-92, Kavanaugh 603-04, 622, 695, Hartnett 858, 920-21; CX's 2261Z-55, Z-56; RX's 1, 106B, C, 107A-C 257Z-7-Z-16, Z-25, Z-26, Z-126. While some pharmacy opposition had manifested itself prior to the solicitation, the state did not anticipate that participation would be any different from the level achieved under the existing plan administered by BCWNY. Feinberg 394. An indication of what would constitute an adequate panel can be seen from the performance standard in the state's second RFP. If the winning administrator did not have on line 80% of the pharmacies in each New York county, it was subject to financial penalties. Feinberg 390-92, 391, 520, Kavanaugh 602-03; CX's 2257Z-12, Z-13, Z-24, Z-25, 2260N-P, 2261Z-31-Z-33, 2262X; RX's 254Z-55, 260Z-116. After the state changed the reimbursement rate (*see* Finding 82), PAID was still certain that an adequate panel would participate and it did not seek to renegotiate the penalty clause. Feinberg 392; CX's 2257Z-25, Z-26, 2260Z-39-Z-41; RX's 257Z-12, Z-126, Z-127.

[77] CX's 2257Z-154, 2258Z-12, Z-13; RX's 260Z-7, Z-8.

[78] Kavanaugh 623, 626-28; RX's 254Z-117, Z-118.

[79] CX 711.

[80] CX 491.

[81] CX 368B.

[82] CX 1147H.

40. By the end of May, about half of all New York chains had enrolled in PAID I,[83] and just prior to June 10, approximately 40% of the some 3800 pharmacies in the state had signed up.[84]

41. The significance of this early trend toward participation was made apparent by the tone of a May 27 meeting between OER and the pharmacy community as represented by CPA (Zimmerman), Rite Aid (Krahulec), Peterson (Rosenberg), Fay's, and Kinney. The state officials said that they would not retreat from PAID I, citing in support of their position the encouraging level of participation already achieved and the incongruity of a protest led by firms, some of which had already signed up.[85] The pharmacists left the May 27 meeting with the impression that not only was the state determined to go forward with PAID I, but that similar reduced-rate formulas for other state-sponsored plans were in the offing if PAID I survived.[86]

D. *July 1 And The Pressure On The Pharmacists*

42. The intransigence of the state, as shown during the May 27 meeting, must have confirmed for the alleged conspirators the significance of any early signs of participation. Given the size of NYSEPP as well as the pattern of consumer purchases of prescriptions -- consumers tend to return to the same pharmacy for all prescriptions, and they purchase their non-prescription items at the same pharmacy where their prescriptions are being filled -- the

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[83] CX's 1989C, D, 2260Z-l. *See also* CX's 1180, 1305A, B, 1306, 2094, 2258Z-29.

[84] CX's 1079A-C, 2251Z-116, Z-111; RX 259Z-2H.

[85] Feinberg 401-03, Rosenberg 1112-14; CX's 2Z-92, Z-102, 10M, 14Z-25, 16Z-44-Z-46, 20Z-161, Z-162, Z-164, Z-165, 2069Z-136, Z-137, 2070Z-59, 2257Z-52. Because the pharmacies were enrolling at the rate of 100 to 200 a day, state officials expected that participation would reach the level achieved under the Blue Cross-administered NYSEPP. Feinberg 394, 533, Kavanaugh 617-18. The state officials may also have been heartened by-PAID's own first-hand but limited experience with discounts off AWP, which showed that plans based on such formulas had no difficulty in obtaining an adequate panel of pharmacists. Feinberg 392, Kavanaugh 615; CX's 2260J, K, R, S, Y-Z-l, 2262Z-103, Z-104, Z-111-Z-115; RX's 257"O", 258"O"-Q, Z-111-Z-119, 260P.

[86] CX's 2Z-91, Z-92, Z-105, 5Z-11, Z-18, 733A, B, 2069Z-138.

pharmacists and the state knew that if New York went forward with the plan on July 1, it would have been perilous for any firm to stay out of PAID I (assuming its competitors were in) for fear of loss of not only the substantial NYSEPP prescription business itself ("back-end business" which includes prescription refills), but also the loss of the "front-end" (health, cosmetic and other non-prescription) patronage of some 500,000 NYSEPP members.[87] Moreover, the prospects for departicipation must not have appeared especially sanguine since pharmacists generally believed that it was in their own self-interest to enroll in high volume third party plans despite low reimbursement rates. (Findings 43 to 51, and 85 to 88.)

43. The direction of the pharmacy business is toward the use of third party plans.[88] By 1986, these plans accounted for close to 44% of Peterson's prescription business and about 47% of Rite Aid's New York prescription volume.[89]

44. The correlation between prescription and nonprescription business and the relation of both to third party plans was such that Genovese automatically accepted all of these plans except for so-called "capitation" arrangements.[90] It was Genovese's aim to fill every prescription it could because it operated on a rule-of-thumb that each prescription generated $15 to $20 in front-end sales.[91] NYSEPP, which was second only to Medicaid as a source of Genovese's prescription business, accounted for $7.2 million of that

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[87] Feinberg 511-12, Kavanaugh 623, 627, 628, 703, Rosenberg 1805-06, 1885-87; CX's 2Z-121, Z-122, 6Z-47, Z-84, 16Y-Z-2, 160M, 1127D, 1685H, 2070Z-52-Z-54, Z-88, 2252Z-65(1), Z-66, 2254Q,R, 2260Z-23, Z-24, Z-39, 2261Z-43.

[88] Painter 1406; CX's 160N, 1127B, 2061Z-224; RX's 11B, 325C.

[89] CX's 16R, 24Z-13, Z-14, 683A-C, 699A-C. The Peterson percentage is especially impressive given Rosenberg's general distaste for all third party plans. Rosenberg 1712-13; CX 2070Z-53. Third party plans accounted for between 30% to 40% of the prescription business of Brooks, Carls, CVS, Fay's, and Genovese. CX's 6Z-83, 11Z-1, 2061Z-224, 2248H, 2250"O", P, 2252Z-22, Z-33. For Kinney, third party plans offered a significant potential for sales growth. CX's 2061Z-224.

[90] CX's 2247Z-42, Z-43, Z-46, Z-47, 2248F, 2249Z-7, 2297R. "Capitation" plans pay the pharmacy a fixed amount per patient each month regardless of the number of prescriptions filled. CX's 2247Z-42, Z-43, Z-46, Z-47.

[91] CX's 2247S, T 2248J, 2249Q, Z-7, Z-19.

chain's sales revenues, and in the words of one Genovese official: "You are talking about $7.2 million a year with respect to this plan. No way can you walk away from 7.2 million."[92] Thus it was inconceivable that Genovese would be the only pharmacy in its area not participating in a plan that had far fewer members than NYSEPP.[93] Genovese further conceded that prior to attending the June 10 "Pharmacy Day" rally (*See* Findings 58, 59), it had assumed that it would be participating in PAID I.[94]

45. Brooks made a calculation that was similar to Genovese's -- for each prescription dollar spent, a customer spent another on non-prescription items.[95] A company official said that the effect on Brooks would be "devastating"[96] if it stayed out of PAID I while its competitors participated; reflecting, undoubtedly, the fact that in areas where state employees were concentrated, NYSEPP accounted for about half of Brooks' third party business, and in other areas between 15% and 20%.[97] This view of the significance of third party plans even carried over to those perceived as having unfavorable ingredient reimbursement rates. As one Brooks official put it:

> Well, you have got to look at competition. I mean, this is the whole key in this. If my competitor across the street is in the plan, I may be forced by market conditions to go into it, even though I dislike it and under normal conditions would not go into it.[98]

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[92] CX 2249Z-28; *see also* CX's 1056A, B, 1057, 2249Z-21. The importance of NYSEPP to Genovese can be seen in the effect of even a short delay in its acceptance of the plan. After the demise of PAID I and before it accepted PAID II, Genovese could measure the loss of prescription patronage in the hundreds of customers. CX's 2249Z-67, Z-78, Z-79, Z-250.

[93] CX 2249Z-20.

[94] CX 2249Z-46.

[95] CX's 2252Z-6, Z-7, 2254Q, R.

[96] CX 2252Z-71; *see also* CX 2252Z-66.

[97] CX's 2252Z-33, Z-34. The areas included Albany where Brooks was a major factor. CX's 2252Z-1, Z-2.

[98] CX's 2252Z-3, Z-4.

46. Because prescriptions generated front-end sales, Fay's participated in third party plans even when it knew that the plans would not cover its variable costs. This policy was adopted in order to increase store traffic and spread costs.[99] Given the size of NYSEPP, any decision by Fay's not to participate was expected to have an especially adverse effect in Albany and other key markets of this firm.[100] Thus Fay's originally informed PAID that though it was opposed to the less than full AWP formula, it would have to participate in NYSEPP because of the number of consumers at stake.[101]

47. The position of Carls was uncomplicated. Third party plans, even unprofitable third party plans, brought customers into its store and if their principal competitors (Fay's and Rite Aid) had signed up for PAID I, Carls would have done the same for fear that the same customers would walk out for good.[102] NYSEPP was second only to Medicaid in size and importance for Carls,[103] and it was inconceivable that this chain would not have participated in a program of this size.[104] Apart from PAID I, Carls had never declined to participate in any third party plan.[105]

48. NYSEPP was vital to CVS. This chain filled 4 million prescriptions in New York State in 1985, almost one million of which were for state employees.[106] Moreover, CVS market research had revealed that the average prescription customer spent 40% more on

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[99] CX's 11Z-19-Z-21, 2060Z-23, Z061Z-157-Z-159, 2062Z-3, Z-6-Z-13, Z-136-Z-142, 2069Z-17, Z-18. The only third party plan which Fay's had turned down was a "capitation" plan. CX's 11Z-26, Z-27, 2062Z-14, Z-15 and *see* Note 90, *supra*.

[100] CX's 8Z-17, 11Z-21, Z-30, Z-58, Z-80, Z-81, Z-99, Z-100, 2062Z- 4-Z-6, Z-113, Z-114, 2203Z-28, Z-30, 2322A-C. *See also* Kavanaugh 627.

[101] CX 2259Z-40.

[102] CX's 2206Z-9, 2250X, Z-6, Z-82-Z-85, Z-96, Z-97, 2251Z-13, Z-18, Z-29, Z-95-Z-98.

[103] CX's 2250Z-17-Z-19, Z-24-Z-26, 2251Z-34, Z-36, Z-37, 2291.

[104] CX's 2251Z-53, Z-54.

[105] CX 2206Z-15.

[106] CX's 5Z-67, 6Z-82, Z-83, Z-86, Z-81, 7Z-32, 7-45, Z-46, Z-105.

front-end merchandise than a non-prescription customer and visited the store more than twice as often.[107] Accordingly, CVS knew that if it did not participate in PAID I and its competitors did, this would have a serious direct impact on its market share.[108] Apart from PAID I, CVS had never declined to participate in any third party plan.[109]

49. Because of the trend toward third party plans, Kinney viewed participation in these arrangements as contributing significantly toward increasing prescription sales, a goal it had set not only for the drug volume itself, but also for the direct impact of prescription sales on its nonprescription business.[110] For all practical purposes Kinney participated in all third party plans,[111] and the sheer size of NYSEPP -- only Medicaid was larger -- dictated that Kinney had to participate in this plan.[112]

50. As late as June 12, and in the midst of the activities in opposition to PAID I, Rosenberg told his stores that Peterson's refusal to participate was contingent on its competitors doing the same. Rosenberg signed the PAID I forms and kept them in his office ready to be submitted if his competitors participated in the plan. Rosenberg knew that any chain participating in PAID I would have a competitive advantage over nonparticipants.[113] The pattern of consumer loyalty described in Finding 42 meant that Peterson would have had

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[107] CX's 160K, M, U.

[108] CX's 6Z-44-Z-47. NYSEPP had a special significance for CVS because Albany, where many state employees are located, was its largest market. CX's 2Z-168, 5P, 6Z-2, Z-3, 7U, V. In 1986, CVS accounted for almost 35% of the Albany market, and CVS, Fay's, and Rite Aid together controlled about 60% of pharmacy sales in that area. CX's 6Z-2, Z-3.

[109] CX 2191Z-137.

[110] CX's 12Q, R, 2063Z-46, Z-47.

[111] CX's 12S, 2064P, R.

[112] CX's 13Z-2, Z-3, Z-15, Z-75, Z-76, 14Z-23, 2290.

[113] Rosenberg 1805-06, 1885-87; CX 681A. *See also* CX's 2070Z-62, Z-63 for evidence of Rosenberg's apprehension that the major chains might try to "steal a march on their competition," and Rosenberg 1770, 1852, CX's 16Z-74, Z-82, 2070Z-88, Z-89 for his anxiety about possible loss of business in college and prison towns where state employees represented a significant part of the work force.

to sign up for PAID I if its main competitors participated notwithstanding Rosenberg's distaste for "regressive percentage" plans.[114] According to Rosenberg, before the prospect of PAID I arose, "we [Peterson] had never been in a situation like this before where there was a potential that we may be non-participators in a plan."[115]

51. Even Rite Aid, which had threatened the state at an early stage of the PAID I initiative with nonparticipation, and whose Krahulec was instrumental in putting together the combined front of nonparticipation described in Findings 53 to 81, did not rule out participating should its competitors enroll,[116] Rite Aid filled 5,000 prescriptions a week under NYSEPP, and an outright decision not to participate would have adversely affected the bottom line profitability of this huge chain.[117] Rite Aid, of course, realized that fewer

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[114] Rosenberg 1885-87; *see also* Rosenberg 1742, 1744, 1805-06; CX's 16Y, Z-1, Z-2, Z-79, Z-80.

[115] Rosenberg 1901. *See also* CX's 2070Z-54. The correlation between front-end and back-end business described in Finding 42 was especially important to Peterson because of that chain's large "Love of Pete" gift departments. *See* Rosenberg 1713.

[116] In July 1985 and again on May 27, 1986, Rite Aid told OER that it would not participate in any plan that discounted the full AWP rate. Rosenberg 1756, 1759; CX's 2Z-95, Z-174, 2257Z-55; RX's 1, 257Z-47; but *see* CX 812 in which Krahulec said on May 20, 1986, "we may alternately decide to participate" as he contemplates "combined responses" to PAID I. *See also* CX's 23Z-47-42(2), 70C, 2261W, 2323C, D, for evidence that in fact Rite Aid participated in third party plans with reimbursement rates lower than PAID I; indeed, at the very time that Rite Aid made the July 1985 statement it was being reimbursed at AWP-12% in the NYSEPP areas administered by BCWNY. For this very reason, the May 27, 1986, statement did not convince Rosenberg of Rite Aid's commitment to nonparticipation since he knew that the Rite Aid was participating in the BCWNY - administered NYSEPP plan. Rosenberg 1756.

[117] CX's 19Z-40, 20Z-11, Z-12, Z-147, 22Z-64, 23Z-49-Z-51, 24Z-20, Z-79, Z-80. Note that even a short delay by Rite Aid in accepting PAID II, the successor to PAID I, meant that the chain was "hit hard" by the loss of business. CX 19Z-141. *See also* CX's 22Z-108, Z-111, Z-145-Z-147, 23Z-92, 2196Z-158, 2201Z-71, Z-73. As indicated in CX 868H third party plans had played a key role in the growth of Rite Aid's prescription business.

customers would be lost if its competitors, too, were not participating in any particular third party plan.[118]

52. The risk to the alleged conspirators if PAID I was not defeated by July 1 is shown by a June 16 Supermarkets General internal memorandum outlining the prospects for the pharmacy departments of its Pathmark stores should its competitors decide not to participate. Because a "boycott seems to be developing among chain pharmacies" Supermarkets General saw an opportunity to be exploited as it planned to advertise that the Pathmark stores would be accepting PAID I.[119] A similar strategy would have been followed by Fay's had it decided to participate while others remained on the sidelines.[120]

E. *The Zimmerman/Krahulec Invitation And The Pharmacists' Response*

53. Confronted by the prospect that New York was determined to go forward with the July 1 starting date so long as an adequate array of pharmacists seemed likely, Zimmerman of CPA and Krahulec of Rite Aid sent out clear messages to the alleged conspirators that there must be no participation. The contents, the settings, and the means used for sending these messages -- *i.e.*, by exhortations during meetings of the alleged conspirators, by adoption of a "Dear Valued Customer" device for keeping the patronage of state employees while the alleged conspirators did not participate, in response to inquiries from one pharmacist about the intentions of others, by widely circulated memos calling directly and indirectly for nonparticipation -- signaled that joint action was contemplated and invited. (Findings 54 to 81.)

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[118] CX's 24Z-79, Z-80.

[119] CX 1311. *See also* CX's 1307, 1309, 1313.

[120] CX's 2062Z-44, Z-45. *See also* CX's 24Z-45, Z-46, Z-88, Z-89 for Rite Aid's use of this strategy in 1970 to take business away from competitors who were boycotting Medicaid.

54. Zimmerman knew that if PAID I were to be defeated, it was essential that the pressure of the July 1 deadline be maintained.[121] As early as April 11, 1986, in a memo circulated to "Members of the Chain Pharmacy Association of New York State" (by its terms each member was apprised that all the others had received the same message) he signaled the Pharmacists that the key to their success lay in the vulnerability of the state to nonparticipation --

> While this formula [an alternative to PAID I] may be difficult to obtain at this late date, state officials are concerned that participation in this program by pharmacists will be threatened if economic considerations are not adequately addressed.[122]

55. Early on, Zimmerman also began to play a slightly different variation on the nonparticipation theme. He told Krahulec and other CPA members that if they signed up for PAID I, he would have difficulty lobbying against any attempt by the state to incorporate a reduced rate reimbursement formula in its insurance program for the elderly.[123]

56. As for Krahulec, he reflected on the prospect of "combined responses" as he reported on May 20, 1986, to Rite Aid officials that "I have already been informed that the independent pharmacists are extremely upset with many aspects of this program and have threatened a boycott."[124]

57. Consistent with his May 20 contemplation of "combined responses" and the receipt of a report respecting the prospects of a boycott, over the next few weeks Krahulec assumed the role he was

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[121] CX's 2Z-121, Z-122.

[122] CX 732B.

[123] CX's 2Z-113, Z-123, Z-124. Krahulec had similar concerns about the linkage of the two programs. CX's 20Z-l0, Z-11, Z-23. While Zimmerman communicated his thoughts on the anti-PAID I campaign to all CPA members, there can be little question that Krahulec was his main confidant and principal co-strategist. *See* CX's 2Z-123, Z-238, Z-239, 20Z-23, 21Z-34, Z-35.

[124] CX 812. Krahulec based his statement on Zimmerman's report that an official of PSSNY (Pharmaceutical Society of the State of New York, the state-wide association of independent pharmacists and umbrella organization for affiliated county associations, CX's 20P, Q, 2243R, S, 2246Z-18, Z-19) had told him that county associations were threatening a boycott. CX's 20Z-139-Z-141.

to play throughout the anti-PAID I campaign -- an aggressive seeker, a convenient depository, and an eager transmitter of information and advice about nonparticipation.[125]

58. The Zimmerman/Krahulec effort to achieve a solid front of nonparticipation intensified as the July 1, 1986, deadline approached. At a June 10 "Pharmacy Day" rally in Albany, Zimmerman again warned the alleged conspirators that the defeat of PAID I, and the effort to keep similar terms out of the state's plan for the elderly, would be jeopardized if any members participated.[126] A similar message was conveyed in more pointed terms to individual firms. Thus having learned that Carls had signed up to participate in PAID I, Zimmerman cautioned officials of that firm on June 10 or thereabouts that an effective lobbying effort could not be sustained if Carls remained in the plan.[127]

59. For his part, Krahulec weighed in at the "Pharmacy Day" rally with a crucial embellishment on the nonparticipation theme. He discussed with Rosenberg the use of a "Dear Valued Customer" letter, a billing stratagem designed to keep the patronage of state employees while a pharmacy was not participating in PAID I. Rosenberg responded with a request for a copy of the letter.[128] A representative of Genovese spoke with Krahulec to the same effect

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[125] CX's 12Z-29-Z-31, Z-77, Z-78, 14Z-79-Z-84, 488E, 2066Z-34-Z-36, Z-42 (Krahulec initiates a telephone conference call to Kinney and Genovese in order to determine if these chains intend to participate in PAID I. Kinney tells Krahulec and Genovese that it will not participate), 20Z-66, Z-67, Z-139-Z-141 (Krahulec passes on to Genovese, Zimmerman's report of the boycott being planned by the Westchester and Long Island pharmacists), 20Z-161 (Krahulec learns that Fay's has enrolled in PAID I), 20Z-101, Z-117, Z-118, Z-227, Z-229 (Zimmerman informs Krahulec that chains which had previously signed with PAID I, have canceled), and *see* Findings 59 and 13-81 for Krahulec's use of "Dear Valued Customer" letters and a lawyer's memo as the means for imparting and receiving participation signals. *See also* CX's 142-17, Z-78 and Findings 42-52 and 75 for evidence of the mutual interdependence of these firms and the competitive consequences of any uncertainty about each other's intentions respecting participation in a third party plan.

[126] CX's 2Z-123, Z-124, Z-138, Z-139, 2199Z-102, Z-103, 2249Z-119.

[127] CX's 2206Z-15-Z-17.

[128] Rosenberg 1807-08, 1836, 1898-99; CX's 16Z-98, Z-99, Z-102, Z-103, 2070Z-65, Z-75, Z-76.

on or about June 10.[129] There is also evidence that at the June 10 rally, Krahulec did not confine himself to one-on-one conversations about the "Dear Valued Customer" letter. Kelley, a former Washington-based chain drugstore association lobbyist who attended the June 10 meeting, testified that a reimbursement procedure for nonparticipating pharmacists was the topic of a general discussion.[130] This proffer by Krahulec of the "Dear Valued Customer" letter, and the requests for the letter that followed, meant that Rite Aid, the largest New York chain, was effectively assured that it need not sign up for PAID I in order to protect its own substantial interest in public employee business.[131] It also meant that Rite Aid, which shared its information with other firms that may have been wavering, had received a clear signal of nonparticipation; for as Krahulec put it, the use of the "Dear Valued Customer" letter was "synonymous" with a decision not to participate.[132] At the same time, Krahulec's promotion

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[129] CX 2194Z-150, Z-151.

[130] Kelley 1635-36. At one point, Kelley said that he heard such a discussion (Tr. 1635), and based upon my observation of his demeanor, as well as my review of his testimony for internal inconsistency, I find that his earlier and later attempts (Tr. 1635-36) to hedge on this point are not credible. This discussion about nonparticipation occurred at the 9:15 a.m. meeting on June 10, which Rosenberg attended. Kelley 1634-35. The "Pharmacy Day" rally was actually several meetings. At 9:15 a.m., the CPA members (including Rosenberg), met in the basement of Albany's University Club. CX's 14Z-39, Z-40, 16Z-55, 725J,K, 2069Z-165- Z-167, 2203Z-75. Krahulec spoke at this early meeting. CX 2203Z-77. Later that day, the CPA membership and members of PSSNY, the sponsor of "Pharmacy Day," rallied in a hearing room of the Legislative Office Building where still additional appeals for nonparticipation were made. CX's 2244Z-153-Z-155, 2278A, B. PAID I was also the subject of a June 10 luncheon conversation involving Rosenberg, Owens of Kinney, and Zurek of Carls. CX's 14Z-50, Z-51, Z-127-Z-129, 2206Z-75, 2250Z-131.

[131] Krahulec routinely passed along information about participation in PAID I to the Rite Aid officials who had ultimate responsibility for deciding whether to enroll in the plan. CX's 18Q, 20Z-127, Z-145, Z-242, 2204Z-49. And despite Krahulec's public pronouncements of nonparticipation, Rite Aid kept in reserve the alternative of participation should its competitors waiver. *See* Note 116, *supra*.

[132] CX's 2194Z-157, Z-158 and *see* Findings 57, 59, 73-81 for evidence that Krahulec played the role of purveyor of information about participation throughout the anti-PAID I campaign.

of the "Dear Valued Customer" approach must have been reassuring to a competitor like Rosenberg who left the "Pharmacy Day" rally with the understanding that Rite Aid itself would not be participating.[133] It is also apparent that the other alleged conspirators left Albany on June 10 similarly reassured. (Findings 60 and 61.)

60. Two days after the "Pharmacy Day" rally, Charles Owens, the Kinney representative at the June 10 meeting, told his company officials --

> I spent Tuesday, June l0th, in Albany with our chain group.... All chains in our group and many independents have taken the position that we will not participate in the plan as it is structured now.[134]

According to Owens, the basis for his report was the statements of chain representatives who declared on June 10 that they would not participate in PAID I.[135]

61. The exact date is not clear, but sometime between June 10 meeting and June 13, Zurek of Carls reported to his company that "no one else" was participating in PAID I.[136]

62. Although Rosenberg came away from the June 10 meeting with the perception that the combined front of nonparticipation was not rock solid, he recognized that the pharmacists need only hold together for the few weeks remaining before the July 1 starting date. In a June 12 report to the Peterson stores, Rosenberg gave the following account of the June 10 meeting:

> There were representatives from many chains -- Rite Aid, Fays, Carls, CVS, Genovese, Brooks and Peterson Drugs. This plan which discount the AWP 12% for chains is so onerous and threatening, that the major chains are up in arms....
>
> To my knowledge, none of the above chains have signed up for the plan, however, moral fibers of their corporate executives will be sorely tested in the next few weeks. I have not sent in any signed contracts as yet, and I can assure we will not be the first. It is my intention to have all the contracts signed and held here in

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[133] Rosenberg 1901-03; CX 16Z-99.

[134] CX 492.

[135] CX's 14Z-64, Z-69. *See also* CX's 14Z-59, 2066Z-33.

[136] CX's 2206Z-21, Z-22, Z-111.

the office, unless we are forced to commit ourselves to the program because other chains give way.

...So far the O.E.R. has stonewalled the situation, but we believe that if they do not get the signed contracts within the next few weeks, something will crack open....[137]

63. Rosenberg denied that he ever discussed Peterson's participation or nonparticipation with the alleged conspirators. According to his recollection, these subjects never came up on June 10.[138] As shown in Finding 58, however, there is convincing evidence that Zimmerman spent June 10 urging the CPA members, including Peterson, to adopt a unified position on participation. Contemporaneous or nearly contemporaneous accounts of what occurred on June 10 strongly support the conclusion that Zimmerman's efforts bore fruit. (Findings 60 and 61.) There is also evidence that in response to Zimmerman's exhortations there were explicit avowals of nonparticipation by some firms.[139] While there is no proof that Rosenberg made such a public pledge, his denial that the subject even came up is contradicted by CX 681A (*See* Finding 62). According to Rosenberg, this June 12 report to his stores merely reflected what he surmised from the large turnout of important and unhappy drugstore executives.[140] But the plain language of the document itself indicates not only that he heard some discussion on June 10 respecting participation, but that what he heard related to a common scheme ("...we [emphasis added] believe that if they do not get the signed contracts within the next few weeks, something will crack open"). Rosenberg

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[137] CX 681A. According to Rosenberg, the report reflected information obtained on June 10. Rosenberg 1798; CX's 2070Z-64, Z-65. *See also* Rosenberg 1803 and CX's 2070Z-62, Z-63, for additional evidence that Rosenberg had doubts about the long-range willingness of the major chains to deny themselves the competitive benefits to be derived from participation in NYSEPP. In general, chains and independents distrust each other and both are skeptical about the other's motives. CX's 2261Z-39-Z-41.

[138] Rosenberg 1780-86, 1868-69; CX's 16Z-57, Z-58, Z-65, Z-75, Z-76, Z-77-Z-79, Z-86.

[139] *See* CX's 14Z-40-Z-44, Z-59, Z-61, Z-64, Z-65, Z-69, 2066Z-27, Z-28, Z-33. *See also* CX's 3Z-29-Z-33, Z-48, Z-49 for evidence that nonparticipation was also discussed at CPA meetings prior to June 10.

[140] Rosenberg 1787, 1802-03; CX's 16Z-17, Z-78, 2070Z-62.

himself conceded that prior to June 10 he had made no firm decision as to whether he would participate;[141] yet, as disclosed in CX 681A, only two days later he was prepared to commit his stores to nonparticipation so long as the other chains stayed out. In addition, there is no dispute that at the "Pharmacy Day" rally of June 10 Rosenberg discussed with Krahulec the "Dear Valued Customer" letter, an exchange that effectively told Rite Aid that Peterson would not be participating.[142] Moreover, Rosenberg's categorical denial that nonparticipation was discussed on June 10, or for that matter at any other time, must be weighed against the following testimony:

Q. Did you ever have conversations with any persons outside of Peterson's about what the effect of not participating by the firms would be on the terms of the plan?
A. Probably, but I don't remember specifically with whom.
Q. Why do you say probably?
A. Because being a pharmacist, I met with other pharmacists. Everybody was outraged by the plan. And it's common knowledge if you do not have people to participate in a plan, you don't have a plan.[143]

64. Within days of the June 10 rally, the alleged conspirators took steps (Findings 65 to 69) which were unprecedented but fully consonant with the Zimmerman exhortation for departicipation (Finding 58), with the Krahulec advice on how not to participate (Finding 59), and with the perception of the pharmacists (Findings 60 to 62) that a combined front of nonparticipation had been put together in Albany.

65. On June 12, Kinney withdrew from PAID I.[144] Kinney admitted outright that this decision was based on information obtained at the June 1 "Pharmacy Day" meeting.[145]

66. Fay's, too, withdrew from PAID I on June 12.[146]

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[141] Rosenberg 1882; CX 2070Z-60.

[142] Rosenberg 1898-99 and Findings 59, 75.

[143] CX 16Z-81 (Rosenberg Deposition).

[144] CX 1749.

[145] CX's 14Z-74, 488C.

[146] CX 1740.

67. On June 13, Carls withdrew from PAID I.[147]

68. By June 17, Rosenberg could confidently report to his Board of Directors that "At this point all major chains have refused to sign [PAID I participation forms]."[148]

69. On June 18, Rosenberg first learned that Peterson's Akron store had signed up, and he immediately canceled its participation in PAID I.[149]

70. Respondent Peterson went to great lengths in its attempt to establish that its departicipation of the Akron store was somehow different from what Kinney, Fay's, and Carls had done. But these differences relate to how a decision may have been made to participate, not departicipate. To begin with, respondent makes much ado about whether the Akron store had exceeded its authority by participating in the first place. What the record shows is that as a matter of corporate policy, Peterson delegated to each pharmacist-manager discretion in running all aspects of the day-to-day affairs of the 18 pharmacies. Nevertheless, the corporate headquarters kept control since it retained the supervisory reins and determined how much discretion was to be delegated to the affiliates. Under this allocation of authority, during the time period relevant to this proceeding, the pharmacists had been given control over the purchase of pharmaceutical goods, hiring and firing of employees, and broad discretion as to how best to promote the store. Moreover, each store had its own separate contract with third party administrators; submitted its own claims to these administrators; and was paid directly for those claims by the administrators. This contrasts with the method used by major chains, which ordinarily sign one contract for all of their stores and submit the claims collectively with payment going directly to the headquarters of the chain.[150] In actual practice, however, the lines of demarcation between Peterson's putative broad grant of individual store autonomy and the authority retained by the

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[147] CX 2005.

[148] CX 679A.

[149] Rosenberg 1831-33; CX's 16Z-88, 1119, 2070Z-72.

[150] Rosenberg 1708-10, 1717-24; CX's 15K, L, 16K, Z-23, Z-24, 716B, 2070Z-73, Z-74, 2268Z-208, Z-212.

Oakfield headquarters were obscure. This is illustrated by respondent's insistence that Rosenberg, acting in his capacity as supervisor of pharmacy operations, was solely responsible for negotiating the contracts with the major pharmaceutical suppliers and third party plan administrators.[151] That this claim is inconsistent with respondent's assertion that the stores were to be treated as individual entities under third party plans and were to control purchases as well as making general policy, is shown by the very fact that Akron accepted PAID I without first consulting Rosenberg.[152] But irrespective of whether the Akron store may or may not have exceeded its authority in signing a PAID I participation form, respondent's argument misses the point that the issue here is not how Akron's participation came about, but rather the circumstances surrounding Rosenberg's abrupt and unprecedented decision to departicipate. (As it happens, Rosenberg's explanation for the withdrawal of the Akron store is virtually identical with the explanation given by Carls: the sudden revelation

[151] Rosenberg 1717-21, 1724.

[152] Cory, the Akron store manager who had been with Peterson since 1958 and had been signing third party contracts for 20 years, was "confused" by the allocation of authority between him and Rosenberg. CX's 15H, M-Q. One source of this confusion may be found in Rosenberg's own account of his authority which indicates an ambivalent role rather than a hard-and-fast rule ("I took it upon myself to pay somewhat greater attention to third-party prescription programs, which were becoming more prevalent" (Rosenberg 1720)) and "It was not a hard and fast rule" CX 2070Z-73 (Rosenberg Deposition)). Even with respect to the "Akron Incident," according to Rosenberg's version at trial, he simply told the store manager that it would have been "best" to have sent the contract to headquarters. Rosenberg 1832. In further support of this shaky rationalization for departicipation, Rosenberg testified that Cory was not authorized to sign the contract because he was not an officer of Akron at that time. Rosenberg 1832. But Cory, who had been an officer at one time (CX's 15M, N, 2070Z-74), and both as an officer and as an ex-officer apparently enrolled Akron in third party plans without stirring up any great fuss (*See* CX's 16Z-36, Z-37), had never been told by Rosenberg -- that is, prior to the PAID I incident -- that he no longer had this authority. CX's 15P, Q. Against this background, it is understandable why Rosenberg's policy respecting limitations on the manager's authority had made no lasting impression on Cory. CX 15Z-22.

that the person who signed the participation form was unauthorized to do so.[153])

71. Respondent also argues that its withdrawal of the Akron store should be considered as simply an extension of its long-standing policy of resisting to the last possible moment all third party plans offering reimbursement at a rate of less than full AWP.[154] In support of this argument, respondent attaches special significance to the contract negotiated with BCWNY during the period 1983-86 for both BCWNY's "community" (*i.e.*, non-NYSEPP) and NYSEPP members. The signing of this agreement followed 2 1/2 years of haggling and threats of law suits between Peterson and BCWNY over reimbursement rates and respondent's status as a chain.[155] If it were classified as a chain, BCWNY would reimburse at a rate of AWP minus 12%. If Peterson were not a chain, the reimbursement rate would be a sliding scale between AWP minus 1% to AWP minus 9%. Peterson finally accepted a compromise rate of AWP minus 3% to minus 11%.[156] This incident tells us nothing about the existence of a scheme to defeat PAID I, and stands simply as additional proof that notwithstanding Peterson's hostility to any third party plan (and especially those premised on a reduction from AWP), it must for competitive reasons eventually accept these plans.[157]

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[153] CX Z005. Conspicuously missing from Peterson's explanation of the Akron store's "mistake" is any attempt to account for the ready acceptance of the PAID I formula by Cory, its experienced store manager. CX's 15H, M, N, 2070Z-73, Z-74. Equally odd, is Carls' explanation that it discovered its "mistake" in late May, but only decided to act on it after the June 10 rally. *See* CX 2250Z-86. As in the case of Peterson's Cory, the "unauthorized" Carls' employee had apparently enrolled in other third party plans with no sudden withdrawals upon the discovery of this technical glitch. CX's 2206Z-121, Z-122, 2250Z-80.

[154] Rosenberg 1732-42.

[155] These negotiations followed BCWNY's attempt to eliminate the problems inherent in reimbursement premised on actual acquisition cost. *See* Finding 17.

[156] Wutz 1007-09, 1016, 1038-63, Rosenberg 1732-42, 1912; RX's 23A-35B. BCWNY estimated that Peterson's average reimbursement rate was AWP minus 5.3%. RX 30C.

[157] *See* Findings 42, 43, 50 and Wutz 1074, Rosenberg 1886, 1910; CX's 2070Z-45, 2267Z-124, Z-125, 2268Z-41.

72. With the exception of one "capitation" plan (*See* Note 90), none of the alleged conspirators had ever before withdrawn from a third party plan after they had already enrolled.[158] New York State and the PAID administrators had never before experienced the phenomenon of pharmacies signing up to participate in a plan and then withdrawing a short time later.[159] Even one of the alleged conspirators acknowledged that such withdrawals were unprecedented.[160]

73. The Zimmerman/Krahulec campaign for a solid front of nonparticipation did not end with the June 10 "Pharmacy Day," or the departicipation of Fay's, Kinney, Carls, and Peterson that followed. Picking up on Krahulec's "Pharmacy Day" invitation, the alleged conspirators made certain that they were all using the same chosen instrument of nonparticipation -- the Rite Aid "Dear Valued Customer" letter first revealed by Krahulec on "Pharmacy Day." (Findings 74 to 78.)

74. The text of the Rite Aid prototype read as follows:

Dear Valued Customer:

Your prescription drug benefit was changed. According to a notification we received, it is now underwritten by Equitable Insurance and administered by Paid Prescriptions. This change has not altered the value we place on servicing your prescription needs and we would like to continue doing so.

Although we have met and expressed our concerns to the people responsible for your health care, no change was made. This necessitates a change in the procedures for billing. Our Rite Aid pharmacist will complete a billing form for you to obtain reimbursement. Upon mailing the billing form to your union office (Emphasis in original), you will be reimbursed for your expenses.

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[158] CX's 11Z-26, Z-27, 488G, 725D, 2063Z-86, Z-87, 2203Z-121, 2206Z-15, Z-125, 2247"O", 2250Z-22, 2297R.

[159] Feinberg 416-17; CX's 2258Z-84, Z-85, Z-102, Z-103, 2259 Z-55, Z-56, Z-91, Z-127-Z-129, 2260Z-19, Z-20, 2262Z-146, Z-147, 2267Z-114, Z-115; RX 259Z-28. In addition to the alleged conspirators, departicipation letters were submitted by Wegmans and several other chains. CX's 2097, 2255Z-87. Wegmans discussed participation and departicipation with Fay's (CX's 2092A, 2255Z-63-Z-65, Z-72, Z-73) but the plans of this chain were not forwarded to Krahulec since Wegman's "is not a member of the group." CX 20Z-227. *See also* CX 2255K.

[160] CX 2203Z-121.

Governor Mario M. Cuomo may be contacted at State Capitol, Albany, NY 12247 (518) 455-2800; and, Thomas F. Hartnett, Director, Governors Office of Employee Relations, State of New York, Agency Building #2, Albany, NY 12223, (518) 474-6988.

We agree this is cumbersome. Please let your officials know you want this changed. If assistance is required, please do not hesitate to let us know.[161]

75. The common adoption of the "Dear Valued Customer" letter is convincing proof that the alleged conspirators have reached a cozy understanding about nonparticipation for otherwise its use makes no economic sense whatsoever. (Rosenberg's assumption that the other chains would be using the "Dear Valued Customer" letters simply because they would not want to turn customers away,[162] is but a small part of the story.) By the terms of PAID I, if a NYSEPP member had a prescription filled at a participating pharmacy, the consumer merely paid a small co-pay fee. If, however, the same prescription were to be filled at a nonparticipating pharmacy, the member would have to pay up front the store's regular retail price, and eventually would only be reimbursed for the amount that the pharmacy would have received had it participated -- that is, the wholesale price as appropriately reduced from AWP under the PAID I formula.[163] It was so unlikely that NYSEPP members would have accepted such a disparity in the cost of their drugs that CVS, Fay's, and Rite Aid recognized that they would have lost business if they adopted such a device while their competitors participated in PAID I.[164] As for respondent's contention that the consumer advice contained in the "Dear Valued Customer" letter was readily available in the state's own consumer information pamphlet, this, too, is way off the mark. The "Dear Valued Customer" letter was a devious marketing strategy which promised NYSEPP members "you will be reimbursed for your expenses" but artfully concealed the unfavorable terms of that reimbursement. The New York pamphlet, on the other hand, correctly informed these consumers that if they used any nonparticipating pharmacy they

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[161] CX 816B.

[162] CX's 16Z-101, Z-102.

[163] Kavanaugh 631-33; CX 681A; RX 295C.

[164] CX's 23Z-88, 24Z-79, 2187Z-3, Z-4, 2189Z-72, 2203Z-143, Z-144.

would receive the reimbursement amount due to the pharmacy had the pharmacy been a participant. It was for this reason that the state's pamphlet concluded, "This procedure means that when you have a choice, you should use a participating pharmacy"[165], hardly the advice contained in the "Dear Valued Customer" gimmick of the nonparticipating alleged conspirators. Rosenberg, of course, knew that a NYSEPP member who filled a prescription at a nonparticipating Peterson store would only be reimbursed in part, but his version of the "Dear Valued Customer" letter makes no such disclosure.[166] Furthermore, since Peterson's prescription volume was not growing, and competition had already forced price reductions,[167] it is implausible that Rosenberg would have adopted the "Dear Valued Customer" scheme unless he was certain that Peterson would not be confronted by the threat of even more serious price competition in the form of participating drugstores offering to fill NYSEPP prescriptions at no cost except for the small co-pay fee.[168] What's more, the "theory" behind the "Dear Valued Customer" device was that the NYSEPP members who were forced to seek reimbursement on their own would be so inconvenienced -- to say nothing of their out-of-pocket losses -- that they would complain to the state and demand a change in the program.[169] Again, it is inconceivable that the alleged conspirators would risk incurring the ire (and possible irreparable loss) of these valuable prescription customers unless they were certain that no competitors would be offering the hassle-free,

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[165] CX 2245Z-198.

[166] Compare Rosenberg 1898 with CX 727B.

[167] CX's 2070Z-35,Z-54. *See also* Rosenberg 1710, 1742-43 for respondent's acknowledgment that its prescription prices must be in the ballpark in order to retain even its loyal customers.

[168] There is no evidence in the record that when the "Dear Valued Customer" letters were adopted that the alleged conspirators knew or could have anticipated that once the program started the state would relent and for the first month or two hold their employees harmless by reimbursing them for the full amount spent even though they used a nonparticipating pharmacy. *See* Kavanaugh 632 and CX's 2249Z-139-Z-142.

[169] Kelley 1635-36. *See also* Hartnett 937; CX's 5Z-75, Z-76.

and largely cost-free drugs that would have been available from PAID I participants.

76. On or about June 12, 1986, Krahulec sent Rosenberg a copy of the "Dear Valued Customer" letter, and later that month they had a telephone conversation about how it was supposed to work.[170] In anticipation of its use on July 1, Rite Aid itself put the "Dear Valued Customer" device in place in its own stores on June 19.[171] On June 24, Rosenberg dispatched to the Peterson stores a "Dear Valued Customer" letter modeled after Krahulec's prototype. In a memorandum accompanying the letter, Rosenberg instructed the Peterson stores, first, to collect the regular cash price from the NYSEPP members, and then to tell these customers that they should seek reimbursement from PAID. Consistent with the evidence that the "Dear Valued Customer" device would not have been adopted unless there was an understanding that a solid front of nonparticipation had been put together (Finding 75), Rosenberg reassured his drugstores that they would not be alone. He wrote, "It is a cumbersome procedure, but is essentially what the major chains will be doing come July 1, 1986 if there is no signed contract." The same memorandum also observed that as of June 24, "Rite Aid, CVS, Fays, Carl's, Genovese, Pathmark, Wegman's, Kinney, and Peterson's have not signed up for the program."[172]

77. On June 25, 1986, CVS informed its store that the chain would not be participating in PAID I and a customer letter was on the way.[173]

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[170] Rosenberg 1836, 1898-1901; CX's 16Z-99, Z-102, Z-103, 725L, 2070Z-75, Z-76, Z-96, Z-97, 2194Z-144-Z-147, Z-157, Z-158, 2204Z-36, Z-37.

[171] CX 818. On the same day or the next, Kinney, Rite Aid, and Genovese held a conference call during which the question of participation in Paid I was discussed. CX 12Z-29-Z-31. During this conference call there was a discussion of how to bill customers if a drugstore did not participate. CX 488E.

[172] CX 727A. *See also* Rosenberg 1835-36, 1897-1901, CX's 727B, 2070Z-75. The "Dear Valued Customer" letter was placed on the pharmacy counter of Peterson's Akron store for distribution to its customers (CX's 2265Z-3, Z-14); in addition, there is evidence that state employees were informed that Peterson would not accept the NYSEPP plastic card. CX 2265Z-19-Z-23, Z-33.

[173] CX's 122-124B.

78. On June 23, 1986, Kinney informed its drugstores not to accept PAID I cards on July l. They were instructed to fill prescriptions of state employees for the usual cash amount only and then to give these NYSEPP members receipts "so they can collect from the carrier."[174] On June 26, Kinney further instructed its stores to use an attached "Dear Valued Customer" letter that was identical to the Rite Aid prototype.[175] On or about the same time, similar instructions were transmitted to Genovese, CVS, and Brooks stores.[176]

79. With the July 1 starting date of PAID I just a few days off, Krahulec and Zimmerman added still another wrinkle to their campaign for a solid front of nonparticipation. CPA retained a law firm which prepared the following memorandum:

POINTS TO CONSIDER IN CONNECTION WITH
A POSSIBLE PHARMACY PROTEST OF OER PLAN

1. A short (lasting no more than a week) protest in which pharmacies individually and voluntarily decline to enroll in the OER plan as a means of expressing their disapproval of the plan.
2. The sole purpose of the protest to be to send a clear message to the Governor, the Legislature, and the public that the OER plan is unfair to pharmacies and therefore also unfair to state employees.
3. OK to discuss purpose and nature of protest with independent pharmacies' trade association and ask them to discuss it with their members; also OK, either through trade association or directly (by letter or phone call), to invite independent pharmacies to voluntarily and individually protest the OER plan (in the same or a different manner).
4. No pressure on any pharmacy to make the protest (or take any other action) and no retaliation against anyone who chooses not to protest.
5. OK to announce protest to customers; OK -- indeed desirable -- to explain why OER plan is unfair: dispensing fee too low, mail order not safe for patients, AWP minus percentage cuts too deep, etc.
6. Announcement should say that many stores and the CDANYS and independents have been meeting with OER and legislators, trying to see the Governor, held the Albany rally, etc., and that the protest is to underscore and emphasize the same issues as presented at those meetings, etc.

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[174] CX 494.

[175] CX's 495A, B.

[176] CX's 122, 123, 124A, 1221, 1222, 2308, 2309, 2310. Carls' "Dear Valued Customer" letter is dated July 1 (CX 2273) but the date of its preparation and transmittal to the drugstores is not clear. *See, e.g.*, CX 2206Z-132.

7. Protest should be widely publicized, for example with a press release which calls on Governor and Legislature not to allow pharmacies to be treated so unfairly.
8. OK to state in press release that, given the onerous terms of the OER plan, many pharmacies declined to participate in the plan quite apart from the protest, and presumably would not participate in the plan even after the protest ended.
9. Announcement and press release should emphasize that pharmacies acted individually and voluntarily to protest OER plan.[177]

80. CPA's law firm sent the memo to Krahulec on June 26 with the notation, "Feel free to circulate this letter and attachment to anyone you wish."[178] Every member of CPA eventually was sent a copy, and Krahulec admitted that prior to July 1, he discussed the memorandum with several CPA members.[179] The lawyer who wrote the memo was prepared to repeat its message of a nonparticipation "protest" at a June 27 Lake Placid convention[180] attended by Rosenberg and the other alleged conspirators.[181]

81. While the lawyer's memo speaks of individual and voluntary action, the actual use to which it was put was just the opposite.

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[177] CX's 2204Z-232, Z-233 [Emphasis in original]; *see also* CX's 20Z-136, 21J-L, Z-37, Z-38, 2204Z-64, Z-65, Z-231, 2263M, Z-23 for Krahulec's role in the preparation of the lawyer's memo. Krahulec, an attorney and pharmacist (CX 20"I"), gingerly avoided the use of the word "boycott" while probing in this "sensitive" area. CX's 20Z-135, Z-136. The reference to "CDANYS" (presumably Chain Drugstores Association of New York State) probably should have read "CPA" for Chain Pharmacy Association. The confusion undoubtedly traces to the law firm's long-standing representation of the National Association of Chain Drugstores (NACDS) and its only recent retention by CPA. *See* CX 2263L

[178] CX 2204Z-230.

[179] CX's 21Q, Z-95, Z-96, 2204Z-42, Z-70, Z-230. Rosenberg's claim that he never received the document (CX's 16Z-108, Z-109) was not reconciled with his admission that he was on the CPA mailing list and regularly received all CPA mailings. Rosenberg 1749; CX's 16Z-12, Z-13, Z-124, Z-125.

[180] CX's 21Z-37, Z-38. The Lake Placid meeting was the annual convention of PSSNY whose support in the form of a state-wide "stoppage" by the independents was being sought by Zimmerman and Krahulec. CX's 20Z-263, 21Z-6, Z-1, Z-22, Z-23, 2154B, 2204Z-96, 2244Z-49, Z-242, Z-257, 2246Z-146-Z-149, Z-155.

[181] CX's 2070Z-79, 2263Z-5-Z-29, Z-52. By the time the lawyer repeated his message on June 27, PAID I had been withdrawn. Feinberg 435-37.

Krahulec forwarded the memo to Adams Drugs (parent of Brooks) on June 26 with a covering letter in which he reported that the chains were indicating their displeasure with PAID I by refusing to sign up for the plan. Krahulec then told Brooks that "the pharmacists' remedy is to refuse to take the contract."[182]

F. *The State Capitulates*

82. With the departicipation of the early enrollees, with those still participating intimating that their commitment was "soft," and without the major chains on board as a leverage for encouraging participation by their competitors, New York caved in on June 26 and abandoned PAID I.[183] PAID II, the successor plan, set the reimbursement rate at full AWP for independents and AWP minus 5% for chains.[184] After some initial uncertainty, and after first checking with each other about their plans, all the major chains finally accepted PAID II by July 4.[185]

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[182] CX's 20Z-317-Z-324; *see also* CX's 20Z-269-Z-271, 2204Z-69.

[183] Feinberg 410-26, 429, 451-52, 468-69. Kavanaugh 618, 630-31, Hartnett 828, 847-49, 929-32, 980-81; CX's 1685G-"I", 2261Z-43, 2262Z-180, Z-181; RX's 254Z-92, Z-117, Z-118. To succeed, PAID I did not need all of the some 4,000 New York pharmacies. The crucial consideration was the availability of pharmacies in areas where state employees were concentrated. Kavanaugh 617. In addition to its own reports of departicipation and the rumors of a less than steadfast commitment by those still enrolled, the state received letters from NYSEPP members forwarding reports of impending departicipation. CX's 1684, 1692B, 1695B, C, 17008, D, 1703B, 1802B, 1803G, 2055B-E; RX's 254Z-68, Z-69, Z-96, Z-97. *See also* Hartnett 982.

[184] Feinberg 431-32, 456; CX 1675A; RX 117A.

[185] CX's 2066Z-42, 2247Z-48, 2270A-D; RX-312A. As could be expected, first in line for PAID II were the independents since they ended up with full AWP. Rosenberg 1845; CX's 16Z-119, Z-121, 2070Z-83, Z-84, 2257Z-128. Once the independents (and firms like Peterson classified as a series of independents under NYSEPP) accepted PAID II (*see* Rosenberg 1845; CX 16Z-119), the chains fell into line (CX's 16Z-121-Z-123, 19Z-172, 24Z-85-Z-87, 2070Z-82-Z-84, 2201Z-61, 2253Z-27, Z-28, 2254Z-89, Z-90), although several (Brooks, CVS, Duane Reed, Fay's, Genovese, Kinney, Carls, and Rite Aid) had contemplated a legal challenge to the two-tier reimbursement schedule retained in PAID II. CX 181A.

83. The cost to the state of the retreat from PAID I has been estimated at approximately $7 million.[186]

G. *The Reasonableness Of PAID I*

84. Both sides made extravagant claims about the inherent reasonableness or unreasonableness of the PAID I rates of reimbursement. To respondent, it was "a rotten plan."[187] In complaint counsel's view, since PAID I was at least as profitable or even more profitable than other plans that had been accepted (however reluctantly) by respondent and the other alleged conspirators, its rejection is overwhelming proof of concerted action taken contrary to individual self-interest. There is warrant in the record for several factual findings which may lie between the positions of both advocates. (Findings 85 to 88.)

85. New York State was not alone in advancing the notion of reductions from AWP as a cost-containment policy but relatively few third party plans had broken away from the full AWP formula.[188] Those plans which had used reductions from AWP had experienced no dearth of providers. To illustrate, Rite Aid, Fay's, Carls, Genovese, Kinney, and CVS had participated in the BCWNY-administered NYSEPP (*i.e.*, the pre-PAID I program) at a rate of reimbursement that was the same as PAID I.[189] As for Peterson, it eventually accepted a BCWNY-NYSEPP rate that was comparable to the rate it would have received under PAID I.[190]

86. Theoretically, a pharmacy firm may go through the exercise of weighing various considerations in evaluating third party plans such as the importance of the plan in a particular locality and its contribution to over-all profits.[191] As far as this record will allow,

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[186] Feinberg 456-58; CX 1675A.

[187] CX 16Z-80.

[188] Hartnett 914, Painter 1427-28; CX's 732A, 1633C, 1760D, 2262Z-198; RX 107G.

[189] Kavanaugh 696; CX 70C.

[190] *See* Findings 29, 71.

[191] *See* Rosenberg 1741-42; CX's 6Z-6, Z-24, 2251Z-18, 2252Z-2, Z-9, Z-10, 2254Z-15.

however, none of the alleged conspirators made such a detailed evaluation of PAID I.[192] The absence of these studies may be explained by the universal availability of discounts off AWP (*See* Finding 15) and the facts recited in Findings 42 to 52, which establish that such review is largely unnecessary because of the importance attached to third party plans and the correlation between front-end and back-end business. These considerations mean that even low profit plans are usually accepted, and almost irrespective of profit no firm can afford to stay out of any third party plan if its competitors participate.

87. Any claim that PAID I was destined to fail from the start flies in the face of what actually happened. The plan got off to a good start when Kinney, Carls, Fay's, Peterson's Akron store and many others agreed to participate.[193]

88. Complaint counsel put on an elaborate demonstration of the profitability of the PAID I plan as compared to other third party plans in which Peterson, Brooks, Carls, CVS, Fay's, Genovese, Kinney, and Rite Aid had participated. Fairly summarized, this evidence shows that the alleged conspirators participated in few reduced-rate third party plans, but that each had enrolled in at least one (including NYSEPP as administered by BCWNY) that resulted in gross margin percentages (gross margin divided by total reimbursement) equal to or less than those projected under PAID I.[194] More germane to this case is the uncontroverted proof that drugstores ordinarily do not reject third party plans irrespective of the modest profit levels involved, and that if their competitors had participated, Peterson and

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[192] Rosenberg 1812; CX's 5Z-50, 6Z-25, Z-106, 7Z-41, 13Z-l, Z-2, Z-37, 16X, 19Z-39, Z-40, 2070Z-18, Z-52, Z-53, 2189Z-136, 2206Z-118, Z-119, 2207Z-18, Z-19, 2254Z-25. Note, however, that CVS had reached the general conclusion that PAID I would have been profitable (CX 6Z-37), Genovese had no basis for believing it would not be (CX's 2249Z-34, Z-35), and Rite Aid assumed that participation in plans paying AWP minus 12% had been profitable (CX 23Z-19).

[193] *See* Findings 35-40.

[194] Painter 1089, 1093-1100, 1163, 1300, 1347, 1352-53, 1384-85, 1397-98, 1412-16, 1423-31; CX's 2317A-2319, 2321, 2323A-2327, 2331, 2334-2336. The gross margin of a third party plan is total reimbursement received (sum of the ingredient reimbursement plus dispensing fee) less the cost of the drugs dispensed. Painter 1096.

the other alleged conspirators definitely would have participated, notwithstanding their obvious preference for higher rather than lower profit margins.[195]

H. *Noerr-Pennington*

89. Throughout the period 1985 to mid-1986, the alleged conspirators and other pharmacists were engaged in a vigorous campaign of lobbying to defeat the state's cost-containment initiative as embodied in PAID I. These lobbying activities reach a crescendo at the "Pharmacy Day" rally in Albany on June 10, 1986. And both before and after "Pharmacy Day" there were meetings with state legislators, petitions to the Governor, and the development of a favorable press image for the pharmacists' cause.[196] While the lobbying was successful in generating political pressure,[197] there is no credible evidence that this is what caused the state to cave in on PAID I. All the persuasive evidence is to the contrary. OER and the other NYSEPP administrators anticipated that the pharmacists would marshal support in Albany. But there were countervailing pressures to be considered -- for state officials knew that every increase in payments to the prescription plan must of necessity mean that funds were taken from some other program, which in turn would produce its own political heat. The highest-ranking state official directly involved with NYSEPP testified unequivocally that PAID I was not withdrawn in reaction to the pharmacists' political clout, but rather because state officials believed that they were the victims of a

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[195] *See* Findings 42-51.

[196] Rosenberg 1787-91; CX's 2Z-125, Z-141, Z-142, Z-155, 16Z-55, Z-56, Z-60, Z-61; RX's 149A-C, 165-171A, 185A-187A. Any post-hearing claim that Rite Aid's "Dear Valued Customer" contrivance described in Findings 59, 73-78 was part of this lobbying effort would be contrary to the record. Rosenberg testified: "I didn't send the letter out thinking of it as a lobbying effort." Rosenberg 1897.

[197] Feinberg 433-34, 553, Kavanaugh 625, Hartnett 943-51; RX's 133E, F, 134E-G, 309F-"I".

pharmacy boycott, and irrespective of their beliefs, in fact there were an insufficient number of drugstores on line by July 1.[198]

III. DISCUSSION

A major and rapidly escalating expense facing New York State is the cost of the prescription drug component of its employee-retiree health insurance plan. In order to meet this problem, the state, in conjunction with its health plan insurer (Equitable Life Assurance) and the plan's administrator (PAID Prescription, Inc.), announces that as of July 1, 1986, pharmacies will be reimbursed for prescription ingredients at a rate representing a sharp reduction from what the state plan has paid in the past. Since it is well-known that pharmaceuticals are purchased by practically all drugstores at steep discounts from the published Average Wholesale Price (AWP), New York proposes in effect that a portion of the discount be transferred to the state in the form of a reimbursement rate for ingredients of AWP minus 12% for chains and AWP minus 2% to minus 8% (depending on the pharmacy's prescription volume) for independents. This is the so-called PAID I plan, which is at the heart of this case.

The state's proposal outrages the pharmacists who view the plan as an especially arbitrary attack on their profit margins. Led by CPA, their trade association, and Rite Aid, the largest chain in New York, the pharmacists organize an aggressive campaign to defeat PAID I. During the course of the campaign, and as the deadline for its implementation approaches, New York is suddenly confronted with a severe erosion in the number of pharmacies willing to participate in the plan. Because of this pressure, the state knuckles under to the pharmacists' demands, and retreats to PAID II, which eliminates most of the discounts off AWP as the basis for reimbursement. With the defeat of PAID I and the pharmacists' acceptance of PAID II, the prescription component of the New York's health insurance plan goes

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[198] Hartnett 801-02, 807-11, 828, 830-31, 851-52, 897-98, 969, 978-80; *see also* Feinberg 415-17, 427-34, 452-54, 553-54. The cause of the state's retreat from PAID I -- an inadequate array of pharmacists -- was in accord with the expectations of Rosenberg who believed that the plan would be changed if not enough providers signed up. Rosenberg 1801; CX 16Z-80. *See also* CX 16Z-97, Z-98.

forward but with a substantially scaled-back cost-containment initiative.

The complaint herein raises the issue of whether there was an agreement or understanding among the pharmacies, including respondent Peterson, which amounted to a combination or conspiracy to boycott New York State in order to defeat PAID I.[199] In addressing this issue, one cannot be oblivious to the obvious: conspirators rarely put their agreements or understandings into writing, and at trial there is bound to be a denial that any explicit oral assurances were given. With these observations in mind, the issue here, as in most conspiracy cases, is whether an inference of an illegal agreement or understanding may fairly be drawn from the conduct of the alleged conspirators. *Norfolk Monument v. Woodlawn*, 394 U.S. 700, 703-04 (1969); *United States v. Paramount Pictures* 334 U.S. 131, 142 (1948); *American Tobacco Co. v. United States*, 328 U.S. 781, 809-10 (1946).

An examination of the context of the state-pharmacists conflict shows that with the announcement of PAID I substantial uncertainties arose for both buyer and sellers. On the buyer's side of this market confrontation, New York State was facing the prospect that with the arrival of July 1, it would have to cope with a serious personnel problem if an insufficient number of pharmacies were not in place to service the non-deferrable prescription needs of its employees and retirees. As it happens, the state could have reasonably anticipated that the interdependence of the pharmacists' decision-making would have lead to an adequate array of pharmacies once several chains had dedicated their acceptance of PAID I soon after the plan was announced. Or to put it somewhat differently, the perceived need of drugstores to participate in third party plans in order to advance or

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[199] The complaint charges that the alleged combination or conspiracy constitutes an unfair method of competition in violation of Section 5 of the Federal Trade Commission Act. 15 U.S.C. 45(a)(1) (1988). Unfair methods of competition within the meaning of Section 5 have been held to include the combinations and conspiracies which are among the restraints of trade that violate Section 1 of the Sherman Act. *FTC v. Cement Institute*, 333 U.S. 683, 694 (1948). At no point in this proceeding have complaint counsel contended that an allegation of combination or conspiracy brought under a Section 5 complaint is different from an identical Sherman 1 civil charge.

protect their own economic self-interest would ordinarily have given the state enough participants to get the plan off the ground. From the pharmacists' perspective, there was apprehension that the pressure on the state of the July 1 deadline would be dissipated if they did not maintain a solid front of nonparticipation. There is no dispute that given the well-established pattern followed by consumers in having their prescriptions filled (*i.e.*, consumers tend to return to the same pharmacy for all their drugs, and usually purchase their nonprescription items at the same drugstore where their prescriptions are being filled), Peterson and the other alleged conspirators knew that if their major competitors participated, and New York went forward with the plan, it would have been perilous for any firm to have stayed out of PAID I for fear of permanent loss of not only the substantial NYSEPP business itself, but perhaps even more important, the loss of the lucrative "front-end" (*i.e.*, nonprescription) patronage of some 500,000 consumers. Finally, the pharmacists were concerned that the survival of PAID I might serve as a precedent for any future attempts to reduce prescription reimbursement rates in other state-sponsored health plans.

The antitrust laws are neutral on the merits of these conflicting tensions, and there is no bar to a vigorous campaign aimed at stopping PAID I that took the form of petitioning or lobbying. But neither the Sherman Act nor the Federal Trade Commission Act will tolerate a resolution of this kind of market confrontation by the contrivance of an agreement or understanding to withhold services. I infer just such an agreement or understanding aimed at PAID I from the following:

1. Zimmerman of CPA, Krahulec of Rite Aid, and the other conspirators, including Peterson, knew that if PAID I were to be defeated, the pharmacists had to keep the pressure on the state of the July 1 starting date. This could only be done if a solid front of nonparticipation was maintained. The conspirators were well aware, as explained earlier, that should this objective not be achieved before July 1, the defeat of PAID I would be unlikely since (a) no drugstore (chain or independent) could afford to stay out of the plan if its competitors participated, and (b) in the independent pursuit of their own self-interest, pharmacies tend toward participation in third party

plans, even so-called low-reimbursement third party plans which may adversely affect their prescription profits.

2. Zimmerman and Krahulec conveyed to the conspirators the message that a solid front of nonparticipation prior to July 1 must be achieved in order to defeat PAID I. The contents, the settings, and the instruments used for this communication -- *i.e.*, during a June 10 meeting of the CPA membership, in the proffer of a "Dear Valued Customer" letter, by widely circulated memoranda discussing nonparticipation, and through a lawyer's paper calling for a short "protest" in the form of nonparticipation -- signaled that common action was contemplated and was being solicited.

3. The Zimmerman-Krahulec invitation for nonparticipation before July 1 was acknowledged and tacitly accepted when the conspirators, including Peterson, adopted the "Dear Valued Customer" letter, a tricky and cumbersome billing stratagem designed to retain state employee business while not participating in PAID I. Minimally, each request for the letter effectively told Rite Aid that it had an assurance that the inquiring firm would not join PAID I, or if it had already signed up that it would take steps to departicipate. As the depository of these assurances, Rite Aid could then convey to any chain reliable information about the intent of its competitors, an important consideration in a market characterized by interdependent decision-making. In addition, once Rite Aid received requests for the "Dear Valued Customer" letter, this meant that the state's largest chain was itself assured that it need not sign up for PAID I in order to protect its own substantial interest in public employee business.

4. The main objective of the conspirators was a short-term combination that would hold together until July 1 and thereby not unduly test the underlying distrust the pharmacists may have harbored against each other. But the "Dear Valued Customer" letter also constituted the conspirators' alternative strategy for maintaining the pressure should New York decide to go forward with PAID I after July 1. Since this gimmick would not have worked in markets where there were participating pharmacists, its common adoption clearly contemplated that direct competitors would not be participating while they jointly used a slippery promise of full reimbursement in an effort to retain the patronage of state workers.

5. That the solicitations from Zimmerman and Krahulec were accepted and thereafter were effective in putting a boycott in place is further shown by the sudden and unprecedented withdrawal of several conspirators -- again including Peterson -- from PAID I after first indicating in one form or another that they would participate. These withdrawals came after Zimmerman exhorted the CPA members not to participate, after Krahulec extolled the virtues of his "Dear Valued Customer" letter, and after the conspirators left Albany on June 10 with the impression that a combined front of nonparticipation had been put together.

The pattern of conduct described above comes within the "invitation-acceptance" rubric of *Interstate Circuit v. United States*, 306 U.S. 208 (1939). Interstate, a first-run film exhibitor, demanded on pain of nonrenewal of license agreements that film distributors set a minimum evening admission charge of twenty-five cents for first-run film exhibitors and prohibit outright the subsequent showing of the same films as part of a double feature. Interstate's threat was contained in copies of a single letter that named all eight distributors as addressees. There was no evidence of any direct agreement among the distributors. In due course, however, each distributor acceded to Interstate's demands in several key localities. On these facts, the Supreme Court concluded:

> It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce . . . and knowing it, all participated in the plan.[200]

On the way to this conclusion, the Supreme Court stressed several factors: (1) an invitation for joint action which created a mutual awareness of the plan; (2) parallel acceptance; (3) deviation from previous business practice; and (4) the interdependence of the decisions. On the last point the Court said:

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[200] 306 U.S. 208 at 226-27.

Each was aware that all were in active competition and that without substantially unanimous action with respect to the restrictions for any given territory there was risk of a substantial loss of the business and good will of the subsequent-run and independent exhibitors, but that with it there was the prospect of increased profits. There was, therefore, strong motive for concerted action. There was risk, too, that without agreement diversity of action would follow.[201]

The Interstate rationale was followed in *United States v. Foley*, 598 F.2d. 1323 (4th Cir. 1979), *cert denied*, 444 U.S. 1043 (1980), where an inference of conspiracy was allowed on facts similar to the instant case. Foley, a Washington area real estate broker, invited his competitors to dinner and announced that he did not care what his guests were going to do, he was about to raise his commission rate from 6% to 7%. Testimony as to what followed the host's announcement was in conflict but apparently there was a general discussion of the subject, some firms may have expressly indicated their agreement with Foley, while others at least gave that impression. After the dinner, the 7% rate began to appear, and those who stayed at 6% were reminded that no firm could maintain the 7% rate unless all held the line. Citing to the Interstate principle of invitation and acceptance, the Fourth Circuit found on these facts "ample evidence to permit the finding of a conspiracy." *Id.* at 1331.

Each element of Interstate as expounded in Foley is present in this case: invitations from Zimmerman and Krahulec, acceptance by the alleged conspirators, deviation from past business behavior, and a context in which no firm would have made a decision not to participate unless it was convinced that its competitors would do the same.

It is of no moment that Peterson may not have participated from the outset in all phases of this conspiracy. *American Medical Assoc. et al.*, 94 FTC 701, 1000 n.38, *aff'd*, 638 F.2d 443 (2d Cir. 1980), *aff'd by an equally divided Court*, 455 U.S. 676 (1982). While the record indicates that the opening gambits -- the notion of sending out an invitation to form a solid front of nonparticipation prior to and after July 1 -- originated with Zimmerman of CPA and Krahulec of Rite Aid, and that these two carried the brunt of the work, Peterson was no innocent bystander patiently waiting in the wings for the

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[201] *Id.* at 222.

larger chains to take action. Rosenberg of Peterson sought out Krahulec, and in effect acknowledged his acceptance of an Interstate invitation to boycott by (1) asking for the "Dear Valued Customer" letter, Krahulec's method for retaining state employee business while simultaneously putting into place a boycott of New York's PAID I plan, and (2) canceling the already-filed participation notice of his Akron store.

Notwithstanding the continued viability of Interstate and its progeny, it is axiomatic that cases involving the invitation/acceptance concept must now pass muster under *Matsushita Elec. Industrial Co. v. Zenith Radio*, 475 U.S. 574 (1986).[202] What the court said in Matsushita is that the permissible range of inferences from ambiguous evidence (especially if the motive to conspire is questionable) is limited by two considerations: "conduct as consistent with permissible competition as with illegal conspiracy does not, standing alone, support an inference of conspiracy" and there must be evidence "that tends to exclude the possibility that the alleged conspirators acted independently." *Id.*, at 588. While this language may bring a summary dismissal to a conspiracy case grounded solely on uniform or even parallel conduct, it does not mean that an inference of conspiracy is no longer proper merely because a respondent is able to concoct some far-fetched scenario of independent action. Again in the language of Matsushita, the issue is whether "the inference of conspiracy is reasonable in light of competing inferences." *Ibid.* As respondent would have it, this "competing inference" derives from the proposition that since nothing was to be gained from an early decision to participate in PAID I, Peterson in its own self-interest did no more than take the rational independent course of awaiting the outcome of the legitimate lobbying campaign which was under way. This argument nicely overlooks several points. To begin with, plenty was to be gained by a joint decision prior to July 1 not to participate. In this respect, unlike Matsushita, there is no question here of motive to conspire; "motive" simply being another way of saying that before an agreement can be inferred, it must be demonstrated that joint activity

[202] *Wilk v. American Medical Ass'n* (Wilk II), 895 F. 2d 352, 312 (7th Cir. 1990), *cert. denied,* 111 S. Ct. 513 (1990).

would be economically effective for otherwise there would be no point in putting together a combination. All the conspirators, including respondent, wanted to defeat the state's cost-cutting and competition-inducing initiative embodied in PAID I, and there can be no real dispute that the most effective way of doing so would be for the pharmacies to cancel already filed notices of participation or to withhold new notices of participation before July 1, and thereby force the state to increase the reimbursement rate. In contrast, the conspiratorial conduct alleged in Matsushita -- an agreement to maintain high prices in Japan in order to subsidize predatory low prices in the United States -- was not only lacking the essential ingredient of motive (*i.e.*, because of the speculation surrounding the effectiveness of predatory pricing), but the Supreme Court was also apprehensive about the anticompetitive side effects of an alleged conspiracy based mainly on evidence of rebates and price-cutting.

Second, Peterson did not sit idly by waiting for July 1. It took the unusual step of canceling a previously filed notice of participation after receiving the Zimmerman/Krahulec invitations to joint action and then indicating Peterson's acceptance by requesting the "Dear Valued Customer" letter. Moreover, this conduct occurred in a setting in which it was not in Peterson's self-interest to departicipate or not sign up additional stores unless it was convinced that its competitors would do the same.

Third, the "Dear Valued Customer" letter was not only a mechanism for signaling that a solid front of nonparticipation had been put together prior to July 1, but its common adoption contemplated that the conspiracy would continue as nonparticipating competitors put into place this device for use after July 1 as a way of keeping the prescription business of state workers.

Fourth, on the facts of this record it is implausible that a bloc of pharmacists would have departicipated or not participated in the absence of a tacit agreement. The well-established pattern in the industry is that drug stores usually sign up for third party plans and even if a particular pharmacy may disapprove of a discounted reimbursement formula it cannot allow participating competitors to garner crucial front-end business. In sharp contrast to this norm, New York State was suddenly confronted with the unexpected -- pharmacies did not sign up and those that had, departicipated after an

association meeting. This highly suspicious conduct, in the context of an intensely interdependent market and the existence of a strong motive to conspire, at least puts one on the alert for any combination-facilitating contrivances. In point of fact, no elaborate mechanism was required: all that was needed was dn exchange of signals respecting nonparticipation as the way to maintain the pressure of the July 1 starting date. These signals were provided by the Zimmerman exhortation to joint action and by Krahulec's hawking of the "Dear Valued Customer" letter. That these signals fulfilled their intended roles is shown by the unprecedented withdrawals from PAID I and the contemporaneous accounts of the June 10 meeting which reveal that the conspirators left Albany with the belief that their competitors would not be participating. It is this sequence of events which places the conduct of the pharmacists squarely back within the four corners of Interstate.

In sum, Matsushita does not say that an inference of conspiracy, reasonably drawn from the record facts, is somehow held in suspense while an endless search proceeds for a rational non-conspiratorial business explanation. Nor does Matsushita require that such an inference yield to strained arguments about the plausibility of possible independent decision making.[203] As it happens, both sides to this litigation vastly overloaded the record by their interpretation of Matsushita as inviting a sort of speculative gamesmanship as to what may or may not have happened in the absence of an agreement. Thus Peterson's alternative scenario -- essentially, a recitation of an incident, unchallenged in the complaint, of its delay in accepting another reduced-rate third party plan -- begs the question as to whether there was an implicit understanding directed at the early demise of PAID I. By the same token, since there is compelling evidence respecting Peterson's actual intent to participate in PAID I had its competitors done so, little was added to the record by the elaborate comparisons to other third party plans which so engaged complaint counsel.

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[203] *See, e.g., City of Long Beach v. Standard Oil Co. of California,* 872 F. 2d 1401, 1407 (9th Cir. 1989), amended, 866 F. 2d 246 (1989), *cert. denied,* 110 S. Ct. 1126 (1990).

As for respondent's argument that the other, legal activities engaged in by Peterson and the other conspirators somehow immunizes the illegal agreement, the Supreme Court has held that Noerr-Pennington protection applies only to petitioning, and this limited immunity is not transferrable to a commercial boycott not-withstanding the fact that both lawful lobbying and unlawful boycotting may have been directed at the same goal.[204] In other words, an implicit agreement to withhold services in order to obtain an economic advantage does not become petitioning by reason of the fact that the agreement was consummated during a campaign which clearly included lobbying aspects. *FTC v. Superior Court Trial Lawyers Ass'n*, 110 S.Ct. 768, 776-78 (1990); *Allied Tube & Conduit Corp. v. Indian Head Inc.*, 486 U.S. 492, 503-04 (1988). Superior Court Trial Lawyers Ass'n is particularly germane given the similarity in the legal tactics (lobbying, demonstrations, and publicity) used by both pharmacists and the lawyers for the indigent as part of their public campaigns to put pressure on the government.[205] But just as the lawyer's explicit agreement to boycott was isolated from these protected activities and quickly disposed of by the Supreme Court, I see no reason for reaching a different result here merely because the pharmacists' agreement to boycott happens to be implicit yet properly inferred from the record. In the same vein, an illegal boycott does not become legal lobbying by the simple expedient of saying that the lobbying would not have been credible unless the conspirators found some way of putting together a solid front of nonparticipation. Under Noerr-Pennington, lobbying means petitioning in its various forms;

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[204] The doctrine is found in *Eastern R. Conf. v. Noerr Motors*, 365 U.S. 127 (1961) (a publicity campaign by railroads aimed at securing legislation harmful to the trucking industry did not violate the Sherman Act); and *United Mine Workers of America v. Pennington*, 381 U.S. 657 (1965) (lobbying campaign by the union and large coal operators intended to persuade the Secretary of Labor to establish wage rates that would impact adversely on small mines did not violate the Sherman Act). The constitutional basis of Noerr-Pennington, *i.e.*, the right of citizens to exercise free speech and inform the government, was affirmed in *California Motor Transport Co. v. Trucking Unlimited*, 404 U.S. 508 (1912).

[205] *See Superior Court Trial Lawyers Assoc. et. al.*, 101 FTC 510, 534-543 (1984) (ALJ opinion).

it does not encompass an agreement to withhold services in order to make the petitioning effective.

Having found that there was an implicit agreement or understanding to boycott, there can be no issue of actual effects on price or the reasonableness of New York's PAID I proposal. An agreement to boycott is a naked restraint on price and output and thus constitutes a *per se* violation of the Sherman Act and the Federal Trade Commission Act. *FTC v. Superior Court Trial Lawyers Ass'n*, 110 S.Ct. 768, 774-75 (1990); *United States v. General Motors*, 384 U.S. 127, 145-48 (1966); *Klor's v. Broadway-Hale Stores*, 359 U.S. 207, 212 (1959).

Finally, the order herein goes beyond what the Commission has accepted in related consent decrees in that it prohibits respondent from soliciting any information from its competitors about their intentions respecting participation in third party plans. This is a permissible extension in a fully litigated case in which it has been demonstrated that such relief is appropriate fencing-in and reasonably related to the practices proven on the record. *FTC v. National Lead Co*, 352 U.S. 419 (1957); *FTC v. Ruberoid Co.*, 343 U.S. 470 (1952); *Siegel Co. v. FTC*, 327 U.S. 608 (1946). What has not been demonstrated is the need for, or for that matter the feasibility of, the expansive order advocated by complaint counsel. As complaint counsel would have it, respondent would be prevented from attending meetings it "expects or reasonably could expect" might relate to some discussion about participation in third party plans. Going one step further, under complaint counsel's proposed order even if respondent could not have anticipated that any hanky-panky would come up at a meeting, it nevertheless would be liable if some competitor took to the floor and happened to discuss participation. The antitrust laws of the United States do not require that the prudent businessman, on pain of incurring civil penalties, read tea leaves, or keep his fingers crossed about what his competitors may say.

IV. CONCLUSIONS

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding and over respondent Peterson.

2. The acts and practices charged in the complaint took place in commerce and affected commerce within the meaning of the Federal Trade Commission Act.

3. Respondent Peterson joined in and participated in a conspiracy to boycott New York State's Employee Prescription Program for the purpose of increasing the reimbursement paid to pharmacies under the program.

4. The conduct of respondent Peterson described above constitutes an unfair method of competition in violation of Section 5 of the Federal Trade Commission Act.

Accordingly, the following order will be issued:

ORDER

I.

For purposes of the order, the following definitions shall apply:

A. "*Peterson*" means Peterson Drug Company of North Chili, New York, Inc., its directors, officers, agents, employees, divisions, subsidiaries, successors and assigns;

B. "*Third party payer*" means any person or entity that provides a program or plan pursuant to which such a person or entity agrees to pay for prescriptions dispensed by pharmacies to individuals described in such plan or program as eligible for such coverage ("covered persons"), and includes, but is not limited to, health insurance companies; prepaid hospital, medical, or other health service plans, such as Blue Cross and Blue Shield plans; health maintenance organizations; preferred provider organizations; prescription service administrative organizations; and health benefit programs for government employees, retirees or dependents;

C. "*Participation agreement*" means any existing or proposed agreement, oral or written, in which a third-party payer agrees to reimburse a pharmacy for the dispensing of prescription drugs to covered persons, and the pharmacy agrees to accept such payment from the third-party payer for such prescriptions dispensed during the term of the agreement;

D. "*Pharmacy firm*" means any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, that owns, controls or operates one or more pharmacies, including the directors, officers, employees, and agents of such partnership, sole proprietorship or corporation as well as the directors, officers, employees, and agents of such partnership's, sole proprietorship's or corporation's subsidiaries, affiliates, divisions and joint ventures, but excludes any partnership, sole proprietorship or corporation, including all of its subsidiaries, affiliates, divisions and joint ventures, which own, are owned by, control or are under common control with Peterson. The words "subsidiary," "affiliate," and "joint venture" refer to any firm in which there is partial (10% or more) or total ownership or control between corporations.

II.

It is ordered, That Peterson, directly, indirectly or through any corporate or other device, in or in connection with its activities in or affecting commerce, as "commerce" is defined in Section 4 of the Federal Trade Commission Act, shall forthwith cease and desist from:

A. Agreeing or combining, attempting to agree or combine, or taking any action in furtherance of any agreement or combination, advocating an agreement, or organizing or cooperating with any pharmacy firm(s) to (1) boycott, refuse to enter into, withdraw from, or not participate in, any participation agreement or (2) threaten to boycott, threaten to refuse to enter into, threaten to withdraw from, or threaten not to participate in, any participation agreement;

B. For a period of ten (10) years after the date this order becomes final, stating or communicating in any way to any pharmacy firm the intention or decision of Peterson with respect to entering into, refusing to enter into, threatening to refuse to enter into, participating in, threatening to withdraw from, or withdrawing from any existing or proposed participation agreement into which Peterson and the other pharmacy firm have entered, could enter or are considering entering;

C. For a period of eight (8) years after the date this order becomes final, advising any pharmacy firm with respect to entering into,

refusing to enter into, participating in, or withdrawing from any existing or proposed participation agreement into which Peterson and the other pharmacy firm have entered, could enter or are considering entering;

D. For a period of ten (10) years after the date this order becomes final, communicating in any way to or soliciting from any pharmacy firm any information concerning any pharmacy firm's intention or decision with respect to entering into, threatening to refuse to enter into, refusing to enter into, participating in, threatening to withdraw from, or withdrawing from any existing or proposed participation agreement.

Provided that, nothing in this order shall prevent Peterson from:

(1) Exercising rights permitted under the First Amendment to the United States Constitution to petition any federal or state government executive agency or legislative body concerning legislation, rules or procedures, or to participate in any federal or state administrative or judicial proceeding;

(2) Subcontracting, preparing joint bids, or otherwise jointly undertaking with pharmacy firms to provide prescription drug services under a participation agreement if requested to do so in writing by the third party payer;

(3) Communicating to the public truthful, nondeceptive statements concerning any existing or proposed participation agreement.

III.

It is further ordered, That Peterson:

A. Provide a copy of this order within thirty (30) days after the date of this order becomes final to each officer, director, employee pharmacist, and each employee whose responsibilities include recommending or deciding whether to enter into any participation agreement, and each employee who regularly attends meetings on Peterson's behalf that include representatives of other pharmacies; and

B. For a period of five (5) years after the date this order becomes final, provide each new director and each employee who enters a

position described in paragraph A a copy of the order within ten (10) days of the date the employee or director assumes the new position.

IV.

It is further ordered, That Peterson:

A. File a verified, written report with the Commission within ninety (90) days after the date this order becomes final, and annually thereafter for five (5) years on the anniversary of the date this order becomes final, and at such other times as the Commission may, by written notice to Peterson require, setting forth in detail the manner and form in which it has complied and is complying with this order;

B. For a period of five (5) years after the date this order becomes final, maintain and make available to Commission staff for inspection and copying upon reasonable notice all documents generated by Peterson or that come into Peterson's possession, custody, or control regardless of source, that embody, discuss or refer to the decision or upon which Peterson relies in deciding whether to enter into any participation agreement in which Peterson participates, has participated, or has considered participating; and

C. Notify the Commission at least thirty (30) days prior to any proposed change in Peterson such as, assignment or sale resulting in the emergence of a successor corporation or association, change of name, change of address, dissolution, the creation, sale or dissolution of a subsidiary, or any other change that may affect compliance with this order.

ORDER GRANTING MOTION TO WITHDRAW APPEAL AND ADOPTING INITIAL DECISION

On June 7, 1991, respondent Peterson Drug Company of North Chili, New York, Inc. ("Peterson") filed a timely Notice of Intention to Appeal from the Initial Decision rendered in this matter by

Administrative Law Judge Morton Needleman.[1] Peterson thereafter sought, and was granted, an extension of time until August 6, 1991 to perfect its appeal by filing an appeal brief.

Rather than filing an appeal brief on the appointed day, Peterson filed a Motion to Withdraw Notice of Intention to Appeal. *Motion to Withdraw Notice of Intention to Appeal*, Dkt. No. 9227, ¶3 (Aug. 6, 1991). In its Motion, Peterson stated that, while "[n]othing in this motion . . . should be construed as an admission . . . to any portion of the Initial Decision," it consents to the entry of the order contained in the Initial Decision. The Motion notes as well that complaint counsel in this matter has been informed of Peterson's decision and does not oppose it.

Under Section 3.51(a) of the Commission's Rules of Practice, 16 CFR 3.51(a) (1991), the Initial Decision becomes the decision of the Commission 30 days after it is served on the parties, or 30 days after the filing of a timely notice of appeal, whichever is later, unless the appeal is perfected by the filing of an appeal brief.[2]

Because Peterson was granted an extension of time within which to perfect its appeal, more than 30 days have elapsed since the notice of intention to appeal was filed. Rule 3.51(a) does not expressly address this situation, and the Commission has therefore determined to clarify the date on which the Initial Decision becomes the decision of the Commission. The Commission has determined that Rule 3.51(a) should not apply retroactively under the circumstances which obtain here.[3] Rather, the Commission has determined that the case

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[1] The Commission's complaint in this matter, issued on April 19, 1989, named six corporations and one individual as respondents. During the subsequent course of the proceeding the other respondents entered into consent agreements, leaving Peterson as the only respondent subject to the Initial Decision.

[2] This result can also be forestalled if the Commission places the matter on its docket for review *sua sponte*, or issues an order which otherwise stays the effective date of the Initial Decision.

[3] To accord Rule 3.51(a) retroactive effect in this matter would create the curious situation in which the Initial Decision would have become the decision of the Commission on July 8, 1991, although that result could not have been known until Peterson abandoned its appeal by filing its Motion on August 6. The task of determining when compliance obligations arose would be problematic, to say the least.

should not be placed in its own docket for review, and that the Initial Decision should become effective as the decision of the Commission upon service of this order to all concerned. The precedential significance of all or any part of this decision in future Commission proceedings will depend entirely on the persuasive weight the Commission determines that it should bear in such proceedings.[4] Therefore,

It is ordered, That respondent's Motion to Withdraw Notice of Appeal be, and it hereby is, granted; and

It is further ordered, That the Initial Decision of the Administrative Law Judge in this matter, and the order therein, shall become the decision and order of the Commission effective upon completion of service of this order upon the parties.

[4] *Cf. BASF Wyandotte Corp.*, 100 FTC 261, 430 (1982).