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District Court Dismisses Tying and Bundling Claims, Holding that Medical-Surgical Distributor Failed to Show Market Power or Injury to Competition

The federal district court for the District of Kansas recently dismissed claims by a medical products distributor that two of its competitors violated the antitrust laws by using tying and bundling contracts to exclude it. *Suture Express, Inc.* v. *Owens & Minor Distrib., Inc.*, No. 12-2760-DDC-KGS, slip op. at 72–73 (D. Kan. Apr. 7, 2016) ("Op."). The court granted summary judgment for defendants, despite plaintiff's expert's opinion that the defendants' contracts resulted in below-cost prices for certain products and that the vast majority of buyers bought the bundle from defendants, rather than buying the products separately. Plaintiff could not show that defendants' contracts were unlawful, the court concluded, because defendants did not have market power and because plaintiff had failed to demonstrate any injury to competition.

Background

Medical-surgical ("med-surg") products are single-use, disposable products used by hospitals and other healthcare providers. Plaintiff, Suture Express, Inc. ("Suture Express") is a distributor of two categories of med-surg products: sutures and endomechanical ("endo") products. Suture Express competes with the defendants, Owens & Minor Distribution, Inc. ("O&M") and Cardinal Health 200, LLC ("Cardinal"), each of which distributes a full line of med-surg products in about 30 categories. Suture Express put forth evidence that, from 2007-2012, O&M's share of the market for distribution of med-surg products to hospitals nationwide ranged from 32–38% and that Cardinal's ranged from 27–31%.

Suture Express sued O&M and Cardinal in December of 2012, alleging that they had caused Suture Express to lose significant business by entering into conditional pricing contracts with customers. These contracts imposed markups on distribution prices unless the customer met market share or volume requirements. Some of the contracts also imposed markups on other med-surg products if the customer switched to another distributor, such as Suture Express, for its suture and endo products. Suture Express claimed it had lost customers as a result of these contracting practices. It also claimed that this conduct harmed hospitals that lost access to Suture Express's distribution services, which Suture Express claimed were superior.

In August of 2013, the court granted in part defendants' motion to dismiss, holding that Suture Express had failed to allege a tying arrangement that was per se illegal under Section 1 of the Sherman Act and had insufficiently pled a horizontal conspiracy between defendants. But, the court held that it was plausible to infer that defendants each had sufficient market power to coerce buyers into purchasing its med-surg

products instead of Suture Express's, even when Suture Express offered superior service and products. The court also rejected plaintiff's monopolization and attempted monopolization claims, holding that Suture Express had failed to plead monopoly power.

The Court's Summary Judgment Opinion

Both sides moved for summary judgment, seeking a judgment on whether defendants had engaged in illegal tying under the antitrust laws. The court held the elements of a tying violation to be: "'(1) two separate products or services are involved; (2) the sale or agreement to sell one product or service is conditioned on the purchase of another; (3) the seller has sufficient economic power in the tying product market to enable it to restrain trade in the tied product market; and (4) a not insubstantial amount of interstate commerce in the tied product is affected.'" *Id.* at 33 (quoting *Sports Racing Servs., Inc.* v. *Sports Car Club of Am., Inc.,* 131 F.3d 874, 886 (10th Cir. 1997)).

To show that defendants' sales of other med-surg products were conditioned on the purchase of suture and endo products—the second element of a tying claim—Suture Express relied on the opinions of Professor Einer Elhauge. Elhauge performed two tests—a "buyer behavior" test and a "discount attribution" test—each of which purported to show that defendants' bundling contracts had an illegal, coercive effect.

Under the buyer behavior test, the court determines whether "'nearly all or a very high percentage of buyers purchased the [bundle] from the defendant rather than purchasing [the tying product] from the defendant and [the tied product] from a rival.'" *Id.* at 35–36 (quoting X Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 1758a (3d ed. 2011)). Professor Elhauge applied this test by examining (1) the percentage of customers who "broke the bundle," buying suture and endo products from Suture Express and other med-surg products from defendants, and (2) Suture Express's share of sales to customers who entered into bundling contracts with defendants. He concluded that only a small percentage (3–7%) of customers broke the bundle, and that Suture Express's share of sales to customers with bundling contracts ranged from 2% to 6%. Based on these calculations, Professor Elhauge concluded that defendants' bundled discounts had the same economic effect as tying.

Plaintiff also attempted to show that defendants' contracts were coercive by relying on Professor Elhauge's application of the discount attribution test. Under this test, "the full amount of the discounts given by the defendant on the bundle [is] allocated to the competitive product." *Cascade Health Solutions* v. *PeaceHealth*, 515 F.3d 883, 906 (9th Cir. 2007).[1] The court then determines whether the "resulting

[1] Paul, Weiss Counsel Daniel A. Crane, also the Frederick Paul Furth Sr. Professor of Law at the University of Michigan Law School, has published extensively on the treatment of bundled discounts and other forms of discounting under the antitrust laws. Crane's academic work and amicus curiae brief played a prominent role in *Cascade Health Solutions*, the landmark decision on bundled discounting by the United States Court of Appeals for the Ninth Circuit.

price of the competitive product or products is below the defendant's incremental costs to produce them." *Id.* Professor Elhauge concluded that among Cardinal customers with bundling contracts, "the resulting incremental price [of suture and endo product distribution] was lower than the minimum markup 67% of the time." Op. at 38. Among O&M customers, the "resulting incremental price was lower than the minimum markup 85% of the time." *Id.*

Nonetheless, the court found that neither the buyer behavior test nor the discount attribution test was sufficient to support plaintiff's motion for summary judgment. With respect to the buyer behavior test, the court credited defendants' argument that its results are not dispositive evidence of coercion: "While these tests might persuade a reasonable jury to conclude that coercion exists, a reasonable jury also could conclude otherwise—*i.e.*, that consumer choices and preferences drive the results, not coercion from defendants' bundling provisions." *Id.* at 37.

The court also found that the discount attribution test was not dispositive, agreeing with defendants that (1) the discount attribution test has never been used to prove coercion in a Section 1 case where the defendant had less than 100% share of the market; and (2) "no court ever has applied the discount attribution test to a non-monopolist." *Id.* at 38–39. The court explained that the test examines whether defendant is selling the tied product—here, sutures and endo product distribution—at a price below cost, "which may exclude a rival who sells only the tied product," such as Suture Express. *Id.* at 39. "But, in a market without a monopolist, a seller of a full range of products has no incentive to exclude the rival who sells only the tied product because other full range sellers competing in the market still can defeat any effort to raise prices." *Id.* Here, even if defendants successfully excluded Suture Express, they would nonetheless face competition from other full line med-surg distributors.

The court also looked at evidence on the third element of the tying claim: whether either defendant had "sufficient economic power in the tying product market to enable it to restrain trade in the tied product market." Suture Express cited cases where courts found that defendants with lower market shares had market power, but the court held that it could not conclude that O&M and Cardinal had market power based on their market shares alone. The court also rejected arguments by Suture Express that the existence of bundling and tying contracts and that defendants' customers rarely "break the bundle" supported a finding of market power. It observed that bundling and tying arrangements "are fully consistent with a free, competitive market" and that "customers make business decisions to enter into contracts and then adhere to their terms does not support a finding of market power." *Id.* at 46, 48 (quotation marks omitted).

Furthermore, the court found persuasive defendants' evidence that other competitors, including a national distributor offering a full line of products, and other regional distributors, were able to gain market share despite the defendants' bundling contracts. Evidence showed that these competitors were successful at winning contracts from defendants and that they used similar bundled discounts themselves. The "summary judgment facts describe a market rife with competitive rivals who are growing and

expanding their business while Cardinal and O&M's market shares have declined or remained relatively flat." *Id.* at 49–50. Moreover, defendants' prices and profit margins had declined since 2008. On these facts, the court held that "no reasonable jury could conclude that defendants have the power to exclude competition or control price." *Id.* at 52. As a result, plaintiff's Section 1 tying claim could not pass muster, and the court granted summary judgment for defendants.

The court also concluded that summary judgment for defendants was warranted because Suture Express could not establish antitrust injury—*i.e.,* injury to competition as a whole, as opposed to a single competitor. The court found unavailing Suture Express's arguments that it "offers a superior product—'a better mousetrap.'" *Id.* at 53. "[T]he antitrust laws are not designed to protect competitors like Suture Express; instead, those laws were enacted to promote competition so that market participants could decide who had 'a better mousetrap.'" *Id.* (quoting *Brunswick Corp.* v. *Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477, 488 (1977)). Because Suture Express could not show an increase in prices or a decrease in output—the "hallmarks of anticompetitive behavior"—it failed to present a genuine issue of fact for trial that the defendants had harmed competition in the overall market. *Id.* at 54 (quotation marks omitted).

Conclusion

The district court's opinion reaffirms certain core antitrust principles, including that bundled discounts are not anticompetitive unless they result in below-cost pricing and that the antitrust laws are intended to protect competition, not individual competitors. Furthermore, under the district court's analysis, even below-cost bundled discounts do not give rise to an antitrust violation absent a showing of market power and harm to the competitive process.

In applying these principles, the district court expressed skepticism of antitrust claims by competitors who have not been as successful in the market as they desired. To credit such claims, the court observed, "could produce harm to competition." *Id.* at 63. It thus concluded: "In essence, Suture Express is asking the Court to insert itself into the market and decide which business model customers should choose when they purchase suture and endo distribution. The Court declines." *Id.*

Suture Express has noticed an appeal to the Tenth Circuit.

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This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

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