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IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF ARIZONA

United States of America, Petitioner, v. **LSL Biotechnologies, Inc.,** Respondent.	MISC. 98-7-JMR

Reply Memorandum in Support of

Petition to Enforce Civil Investigative Demand

In January 1997, the Antitrust Division of the United States Department of Justice ("the Division") opened an investigation to determine whether agreements between LSL Biotechnologies, Inc. ("LSL") and Hazera (1939) Ltd. ("Hazera") that appeared to limit in perpetuity innovation and price competition by one of the world's leading seed developers violated the antitrust laws. As part of that investigation, the Division contacted LSL, and in July 1997, sought the voluntary production of relevant documents and information. After repeated, but unmet, assurances that voluntary production would be forthcoming, the Division, in December 1997, issued a civil investigative demand ("CID") for the previously requested material and other material the ongoing investigation suggested would be relevant.

Even after compulsory process was issued, the Division received repeated promises, but little production. LSL did not claim the CID was improper, nor request any specific modifications, nor suggest that the CID was so burdensome that it would be unable to comply at all. LSL eventually provided a couple of interrogatory responses and documents from prior suits filed by LSL, but little else. When the Division tired of LSL's dissembling and proposed to perform the document search itself, LSL refused to allow the search. Left with little prospect of production, the Division filed the current enforcement petition. The Division did receive LSL's

interrogatory responses after filing the petition,[1] but LSL has steadfastly refused to produce any additional documents, even though many of them have been copied and stamped and are simply sitting in their counsel's office. See Letter from W. Kolasky to J. Read, dated May 8, 1998 (attached at 1).

LSL now attempts to avoid its obligation to produce by converting the CID enforcement proceeding into a trial on the merits, asserting all manner of "factual" defenses -- defenses presumably supported by documents LSL refuses to provide to the government. These defenses are premature. Courts have uniformly enforced CIDs even where recipients proffer legal defenses, such as statutory immunity from the antitrust laws. The reason is simple. Until the facts are developed (as opposed to asserted) and a complaint filed so the exact charges (not some hypothesized) are known, it is virtually impossible for a court to determine whether any of the conduct under investigation violates the antitrust laws. What is clear is that the information and documents requested in the CID are relevant to an assessment of whether these agreements violate the antitrust laws. Accordingly, the Court should order LSL to comply promptly.

I. The Agreements Between LSL and Hazera Are the Proper Subject of a Government Investigation, and the CID Requested Information Reasonably Relevant to That Investigation

The Division is not asking this court to decide whether the agreements between LSL and Hazera violate the Sherman Act. The Division is merely seeking enforcement of a properly-issued CID. LSL does not deny that the Division is conducting a valid civil antitrust investigation (though it questions the value of it) nor does it question the relevance of the requested material. Rather, it claims that the conduct under investigation is not illegal. Its factual defenses are premature.

The validity of a CID does not depend on whether the Division is capable of fully proving a claim prior to learning the very facts the investigation is designed to uncover. At this stage of the investigation, the Division is trying to gather information.

[1] LSL's opposition states that "the Division filed the instant Petition on May 8, 1998, the same day it received its most recent submission from LSL." See Opp. at 9. To the extent LSL's statement implies that the Division received LSL's interrogatory responses, but went ahead and filed the petition anyway without notifying the Court of LSL's response, it is wrong.

> The only power that is involved here is the power to get information from those who best can give it and who are most interested in not doing so . . . .[The government] has a power of inquisition, if one chooses to call it that, which is not derived from the judicial function. It is more analogous to the Grand Jury, which does not depend on a case or controversy to get evidence but can investigate merely on suspicion that the law is being violated, or even just because it wants assurance that it is not. When investigative and accusatory duties are delegated by statute to an administrative body, it, too, may take steps to inform itself as to whether there is a probable violation of the law.[2]

In issuing an administrative subpoena, such as a CID, the Division's "inquiry is not limited by the forecast of the probable result of investigation."[3] Nor is the Division required to "propound a narrowly focused theory of a possible future case."[4] In fact, it is possible that the Division may conclude that the facts uncovered by its investigation and the applicable law do not constitute a violation of the antitrust laws. If that is the case, the Division will not file a complaint. Because the purpose of an investigation is to gather facts upon which a decision to file a complaint may be based, the conduct under investigation need only fall "within the authority of the agency."[5]

Given the Division's broad investigative powers, further Division inquiry would be improper only if LSL established that there is absolutely no possibility that the LSL-Hazera agreements could violate the antitrust laws, regardless of what facts an investigation revealed. See Blue Cross and Blue Shield v. Bingaman 1996-2 Trade Cas. (CCH) ¶71,600 at 78,233 (N.D. Ohio 1996) (court must enforce CID if conduct "may possibly" violate the antitrust laws). LSL has not made the requisite showing.

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[2] United States v. Morton Salt Co., 338 U.S. 632, 642-43 (1950); see also United States v. R. Enterprises, Inc., 498 U.S. 292, 297 (1991).

[3] Oklahoma Press Pub. Co. v. Walling, 327 U.S. 186, 216 (1946).

[4] FTC v. Texaco, Inc., 555 F.2d 862, 874 (D.C. Cir.) (en banc) (emphasis in original), cert. denied, 431 U.S. 974 (1977).

[5] In re McVane, 44 F.3d 1127, 1135 (2d Cir. 1995) (quoting Morton Salt, 338 U.S. at 652); see also E.E.O.C. v. Tempel Steel Co., 814 F.2d 482, 484 (7th Cir. 1987); U.S. v. Westinghouse Elec. Corp., 788 F.2d 164, 166 (3rd Cir. 1986).

Courts have rejected efforts to set aside CIDs based on defenses to the conduct under investigation, even where the defenses are predominantly legal ones, such as statutory immunity from the antitrust laws.[6] Their reasoning is even more applicable to the instant case where LSL's defenses are purely factual. In fact, as a circuit judge, Justice Breyer stated that "factual uncertainty is precisely why [an immunity defense] ought not to be settled in a subpoena enforcement proceeding," but should wait at least until a court has an opportunity to examine the complaint. Monahan, 832 F.2d at 690. Surely LSL has prematurely chosen to argue its *factual* defenses here, if there are too many factual issues involved for courts to determine even a *legal immunity* defense at the CID enforcement stage.[7]

II. LSL's and Hazera's Agreements Raise Serious Competitive Questions, the Answers to Which Depend on a Multitude of Facts

The Division's investigation focuses primarily on two agreements between LSL and Hazera -- one made in 1987 and another in 1992. The two companies entered into an agreement in 1983 related to long-shelf life tomatoes. In 1987, after the original agreement had been in effect for several years, LSL and Hazera agreed to a no-compete clause that, among other restrictions, *indefinitely* forbids Hazera, one of the most successful tomato seed breeders in the world, from conducting any further research or development to improve (with regard to disease resistance, taste, yield, etc.) any tomato that has a long-shelf-life.[8] Then in 1992, LSL and

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[6] See, e.g., FTC v. Monahan, 832 F.2d 688 (1st Cir. 1987) (state action immunity defense no bar to enforcement), cert. denied, 485 U.S. 987 (1988); Associated Container Transportation (Australia) Ltd. v. United States, 705 F.2d 53, 59 (2d Cir. 1983) (CID enforced due to factual issues underlying act of state and Noerr-Pennington immunity claims); see also, Phoenix Board of Realtors v. U.S. Dept. of Justice, 521 F. Supp. 828, 830031 (D.Ariz. 1981) (rejecting argument that CID should be set aside because Division had entered into consent decrees permitting similar conduct in other jurisdictions).

[7] The legislative history of the amendments to the Antitrust Civil Process Act stress that:

> The scope of many antitrust exemptions is not precisely clear... . In amny [sic] cases, the applicability of an asserted exemption may well be a central issue in the case. If so, the mere assertion of the exemption should not be allowed to halt the investigation. H.R. Rep. No. 94-1343, at 11 fn. 30 (1976).

[8] The clause states, in part, "Subsequent to the termination of the agreement hereunder, Hazera shall not engage, directly or indirectly, alone, with others and/or through third parties, in the *development*, production, marketing or other activities involving tomatoes having any long-shelf-life qualities."

Hazera agreed that Hazera would *perpetually* inform LSL of every sale of tomato seeds it made in North America, including specifically the price it sold the seeds for, the customers it sold to and the quantity of seeds it sold.

The Division has learned that the major tomato seed companies compete over seed innovation. The companies are constantly trying to develop seeds that will be resistant to major diseases, will have a high tomato yield, or produce more flavorful tomatoes, firmer tomatoes, or larger, better-shaped tomatoes. Hazera and LSL provided to the marketplace the major innovation of a seed that could grow tomatoes with a longer shelf-life. With that innovation, growers no longer had to pick green tomatoes in order to get them packed, shipped and sold before beginning to rot. That innovation has helped flavorful, vine-ripened tomatoes to become more available in the United States. Under the 1987 no-compete agreement, however, United States consumers will lose all the benefits of any future Hazera research and development efforts in tomato seeds. Moreover, the 1992 price exchange agreement vastly increases the opportunity for price coordination between LSL and Hazera for long-shelf-life tomato seeds.

Contrary to LSL's suggestions, these types of agreements can violate the antitrust laws. Indeed, no-compete agreements may be illegal per se.[9] Certainly, no court has held an agreement that forever precludes a competitor from developing and bringing better products to the market to be a "reasonable restraint on trade" and thus legal. Additionally, courts have found that price exchange agreements can result in violations of the antitrust laws. Such exchanges may facilitate collusion or may undermine a competitor's incentive to cut prices secretly.[10] Whether there exists a set of facts which would ultimately make these suspect agreements legal depends upon facts which LSL uniquely has in its possession and has refused to disclose.

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[9] See, e.g., United States v. Topco Assoc., Inc., 405 U.S. 596 (1972); Blackburn v. Sweeney, 53 F.3d 825, 828-29 (7th Cir. 1995) (no-compete clause of indefinite duration in context of dissolution of joint activity held per se illegal).

[10] See, e.g., United States v. Container Corp. of America, 393 U.S. 333, 337 (1969); United States v. United States Gypsum Co., 438 U.S. 422, 443 (1978); In re Petroleum Products Antitrust Litigation, 906 F.2d 432, 446-47, 462 (9th Cir. 1980).

III. LSL's Arguments That Its Conduct Is Perfectly Legal Depend On Facts

In its attempt to show that there is no *possibility* that LSL *may* have violated any antitrust law, LSL propounds a litany of defenses in its Opposition. This litany is fundamentally deficient because each defense relies on "facts" that are not before the court and that may be proven wrong or determined irrelevant by other evidence. Indeed, the Supreme Court has reminded other courts "to resolve antitrust claims on a case-by-case basis, focusing on the 'particular facts disclosed by the record.'"[11] Thus, it is especially telling that none of the cases relied on by LSL to support any of its defenses analyzes or involves a similar factual situation -- a situation where a major innovator agrees with a competitor to permanently cease all efforts to develop improved products for the public.

LSL's first claim -- that the agreements do not harm United States consumers -- obviously depends on facts that will be gathered during the investigation.[12] The current record is far too sparse to foreclose the possible existence of harm. Indeed, LSL's only "evidence" that it is impossible for the agreements to have harmed United States consumers is that it is small.[13] LSL completely ignores, however, the size and skill of Hazera -- the one who is prevented from bringing the benefits of new, superior seeds to the market.

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[11] Eastman Kodak Co. v. Image Technical Services, Inc., 504 U.S. 451, 467 (1992) (quoting Maple Flooring Mfrs. Ass'n v. United States, 268 U.S. 563, 579 (1925)).

[12] Evidence of harm is not even necessary for per se violations of the antitrust laws. See, e.g., Northern Pacific Ry. Co. v. United States, 365 U.S. 1, 5 (1958). Contrary to LSL's claims, the agreements might be a per se violation since they may enforce Hazera's and LSL's market allocation agreements. See, e.g., Palmer v. BRG of Georgia, Inc., 498 U.S. 46 (1990) (per curiam); Northern Pacific, 356 U.S. at 5. The 1987 agreement may also be a per se illegal market allocation if it allocated to LSL all the territory in which innovative tomato seeds could be developed. See, e.g., Palmer, at 49-50 (holding allocation of an entire market or territory to one competitor per se unlawful).

[13] It appears that LSL is not as small and insignificant as its limited "facts" suggest. LSL's sales and seed operations will be performed in coordination with Seminis through a joint venture. See Letter from J. Meyer to J. Read, dated June 2, 1998 (attached at 2). Seminis is one of the largest tomato seed researchers and producers in the North America. Also, the sale of LSL's long-shelf-life tomato seeds is growing exponentially and may well be the wave of the future. See LSL's response to CID interrogatory no. 7 (showing LSL sales growth of 1432% from 1990 to the present) (attached to Leve's Decl. as Exh. 23).

Moreover, LSL's size and significance -- even if relevant -- must be considered in relation to the relevant antitrust market. Defining the relevant market is often one of the most factually intensive questions of antitrust law.[14] Only in a footnote (no. 28) does LSL acknowledge that the Division is considering whether the relevant market here is long-shelf-life tomato seeds, where LSL appears to have a large share. Indeed, one of LSL's former directors testified that the demand for quality long-shelf-life tomato seeds was inelastic, which if verified, would strongly suggest that the relevant market is long-shelf-life tomato seeds.[15] (Information requested by CID document request nos. 7 and 8 should help determine the relevant market.[16])

LSL also claims that the there is no possible antitrust violation because it had a "strong business justification" for the agreements and because they are "narrowly tailored." Again that turns on the facts, which at this point actually suggest otherwise.[17] First, the Hazera conduct that

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[14] See, e.g., United States v. E.I. duPont de Nemours & Co., 351 U.S. 377, 394-404 (1956) (ten page discussion of market definition); United States v. Engelhard, 970 F. Supp. 1463 (M.D. Ga.) (20 page factual discussion of product market definition), aff'd, 126 F.3d 1302 (11th Cir. 1997).

[15] See July 21, 1997 Dep. of Howard Marguleas at 59-60 (attached at 3); see also Times-Picayune Publishing Co. v. U.S., 345 U.S. 594, 612-13 (1953) (establishing price elasticity as the test for defining an antitrust product market).

[16] LSL's reference to the ITC determination to establish the relevant market is misplaced. That determination focused on vine-ripened and mature green tomatoes. It did not address seeds. It also did not separately analyze long-shelf-life tomatoes. Moreover, the ITC was determining if the tomatoes were "like products" under U.S. anti-dumping law not U.S. antitrust law. The ITC itself has rejected the comparison LSL proposes. See, Generic Cephalexin from Canada, Inv. No. 731-TA-423 (Prelim.) USITC Pub. 2143 (Dec. 1988) at 3, n.4 (refusing to rely on antitrust cases in defining like product.)

[17] Document request nos. 5 and 6 were designed to gather the types of information necessary to determine the validity of these defenses. Document request no. 5 seeks, among other things, documents "discussing" the two agreements under investigation. The request should capture any type of document where LSL considers the putative "strong business justification" for the agreements. LSL's proposed modification to request no. 5, however, would omit such documents. Document request no. 6 is intended to capture, in part, LSL's "discussions" of alternative ways to achieve the same goals. The Department will be in a better position to determine how "narrowly tailored" the anti-competitive aspects of the agreements are once it knows the realistic alternatives LSL considered. In its modifications section, LSL has proposed eliminating document request no. 6 entirely.

LSL alleges gave rise to the justification for the 1987 no-compete agreement (selling seeds in LSL's allocated territory), did not occur until 1991 -- four years later.[18]
Second, the ban on research and development competition covers products not protected by LSL's patent.[19] And thirdly, a ban on competitive R&D that lasts forever hardly seems narrow.[20]

Finally, LSL asserts that the Department of Justice has jurisdiction to investigate these agreements only to the extent they prevent Hazera from importing seeds into the United States. LSL's contention ignores one of the most important potential harms of the agreements -- that Hazera's 1987 agreement never to develop seeds for United States growers deprives those growers (and ultimately U.S. tomato consumers) of possible product innovations. The Division has discovered that one of the most significant tomato grower associations in the United States has already requested that Hazera develop and test seeds that would grow well in the climate of its members. Even LSL's own conduct belies its lack of jurisdiction claim. It believed the United States had sufficient jurisdiction over Hazera and the agreements under investigation to sue Hazera over them in Florida last month.[21]

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[18] See Opposition at 3. Whether Hazera actually sold its seeds in LSL's territory as LSL now claims is another open factual issue. Indeed, LSL's own president testified under oath that Hazera had not. See Nov. 4, 1992 Dep. of Yakov Ben-Zion at 49-50 (attached at 4).

[19] See Transparent Wrap Machine Corp. v. Stokes and Smith Co., 329 U.S. 637 (1947) (patentee could not require non-competition beyond the term of patent, nor as to items not covered by patent).

[20] Compton v. Metal Products, Inc., 453 F.2d 38, 44 (4th Cir. 1971) (It is "true as a general proposition that covenants not to compete which are unlimited as to space or time are invalid and unenforceable.")

[21] The fact that LSL has sued Hazera in Florida and Israel does not make the CID "unwarranted and unreasonable" as LSL claims. See Opposition at 2. LSL filed its complaints on May 14, 1998, five months after the Division issued the CID and nearly a week after the Division filed its enforcement petition. It is unthinkable that a party should be able to moot a CID simply by filing a private suit months after it has failed to comply with the CID. Moreover, concurrent private and government enforcement of the Sherman Act is commonplace. It is in fact necessary because private parties such as Hazera do not represent the interests of U.S. consumers. Finally, the very fact that LSL is suing to enforce the agreement shows that LSL believes the agreement is operational and effective.

IV. LSL Has Not Shown Undue Burden Sufficient to Compel the Court to Modify the CID in a Manner That LSL Never Even Proposed to the Division

LSL has provided the court with a proposed list of modifications to the Division's CID. But, LSL has failed to demonstrate why the modifications are necessary or why it has imposed upon this Court to adjudicate them. The documents LSL seeks to withhold go to the heart of many of the factual issues it has asked the Court to decide. For example, document request nos. 7 and 8 will help determine the market at issue, the competitors in that market, the degree to which they presently compete, and the expected effect of Hazera entering the market. Yet, LSL asks the Court to rescind those two requests entirely.

LSL has not even attempted to demonstrate how much time or money would be saved by particular modifications. Indeed, some of the proposed modifications do not appear to limit the scope of the document search at all. For example, LSL proposes to produce documents that "explain or interpret" the agreements at issue, but not documents that "discuss" them. See Opposition at 19. LSL has failed to explain why a search for documents which "explain or interpret" the agreements would not involve the same files as documents that "discuss" them.

Moreover, the Division has offered to perform the document search itself, and LSL has refused. Regardless of any reasons LSL may have had to prevent Division personnel from searching the New York offices of Yerushalmi and Associates, LSL has provided absolutely no explanation for its refusal to allow Division personnel to inspect responsive documents at its corporate headquarters in Tucson, Arizona (a place LSL never even began searching). On-site inspection by Division personnel would alleviate much of LSL's claimed burden.[22]

LSL never approached the Division with any proposal for modification of the CIDs, until the one contained in its filing with this Court. It is inappropriate for LSL to request that the Court rule on modifications it has not even attempted to negotiate with the Division. LSL's attempts to negotiate modifications now through the Court may simply be another attempt to buy

[22] Also, the CID poses little additional burden, since much of the information the Division is seeking will likely be required through discovery in the private litigation that LSL itself instituted. Presumably LSL considered those burdens of discovery when it filed the private lawsuit last month, and determined that those burdens were not overly great. Additionally, LSL's claimed small size only means there are not as many documents to review.

more time or a last ditch attempt to withhold as many documents as possible from government review.

V. Conclusion

For the reasons stated herein, the Division requests that the court grant its previously filed Petition to Enforce Civil Investigative Demand No. 17420.

Respectfully submitted,

/s/

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Antitrust Division

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