UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE

UNITED STATES OF AMERICA, Plaintiff, vs. FEDERATION OF PHYSICIANS AND DENTISTS, INC., Defendant.	)	CA 98-475 JJF

BRIEF IN SUPPORT OF PLAINTIFF'S MOTION TO COMPEL PRODUCTION OF DOCUMENTS FROM FIRST STATE ORTHOPAEDICS

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COUNSEL FOR PLAINTIFF
UNITED STATES OF AMERICA

RICHARD G. ANDREWS
UNITED STATES ATTORNEY

Virginia Gibson-Mason (DSB # 3699)
Assistant United States Attorney
1201 Market Street, Suite 1100
Wilmington, DE 19801
Tel.: (302) 573-6277

Melvin A. Schwarz
Special Enforcement Counsel
U.S. Department of Justice
Antitrust Division
601 D Street, N.W.
Washington, D.C. 20530
Tel.: (202) 305-1210

Steven Kramer
Richard S. Martin
Denise E. Biehn
Michael D. Farber
Heather H. Howard
Jean Lin
Attorneys
U.S. Department of Justice
Antitrust Division
325 Seventh Street, N.W.
Washington, D.C. 20530
Tel.: (202) 307-0997

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I. STATEMENT OF THE NATURE AND STAGE OF THE PROCEEDING

On August 12, 1998, the United States filed its complaint (D.I. 1) against defendant, the Federation of Physicians and Dentists ("the Federation"), seeking equitable and other relief to enjoin defendant's and its orthopedic surgeon members' violation of Section 1 of the Sherman Act. The complaint alleges that defendant, in coordination with its 44 member orthopedic surgeons located in Delaware, including 10 members of the largest orthopedic group in Delaware, First State Orthopaedics ("First State"), organized and became the hub of a price-fixing conspiracy to oppose and prevent proposed reductions in payments for orthopedic services by Blue Cross and Blue Shield of Delaware ("Blue Cross").

On October 29, 1998, at the beginning of discovery in the case, the United States served a subpoena duces tecum on First State. First State has refused to produce documents in response to one request seeking documents sufficient to show First State's revenues and expenses in 1997. As explained in detail below, the United States has consulted in good faith with counsel for First State without success, and, therefore, now moves the Court for an order compelling First State's production of responsive documents.

II. SUMMARY OF ARGUMENT

Documents showing First State's 1997 revenues and expenses easily meet the liberal standard of relevance for pretrial discovery in this antitrust case. Plaintiff's Complaint explains in some detail the numerous documents demonstrating the concerted activity. Nevertheless, defendant continues to deny that it occurred. The requested information is clearly relevant to, and highly likely to lead to the discovery of, admissible evidence concerning the issue that is "clearly at the heart of th[is] litigation:"[1] whether defendant's members acted in concert or, as defendant claims, each acted independently. Specifically, the requested information is relevant to a determination of whether defendant's members' actions were against their independent self-interest and, accordingly, can be explained only by the

[1] In re ML-LEE ACQUISITION FUND II, 151 F.R.D. 37, 39 (D. Del. 1993).

fact that they were acting in concert. It also bears directly on defendant's affirmative allegations that each of its members acted independently based on concerns that Blue Cross's proposed fees were unprofitably low and threatened to erode the standard of care provided to their patients. In view of these grounds, an order compelling First State to produce information demonstrably relevant to establishing concerted action and to analysis of defendant's contrary claims is amply warranted here. Moreover, the manifest relevance of the information sought refutes First State's groundless contention that the request in dispute was propounded to harass and embarrass First State.

III. STATEMENT OF FACTS

The crucial factual issue in this case is whether defendant's challenged conduct involves concerted action with its member orthopedic surgeons in Delaware. The Complaint alleges that,

> Defendant and its co-conspirators have engaged in a combination and conspiracy . . . consist[ing] of an understanding and concert of action among Defendant and its co-conspirators that Federation members would negotiate their contractual fees with Blue Cross only through the Federation's executive director, Mr. Seddon, for the purpose of collusively resisting any reductions in fees paid by Blue Cross for their provision of medical services to its plan members.

Complaint (D.I. 1) at ¶¶ 52 and 53. The Complaint further alleges that, in effectuating this conspiracy, defendant and its members, "[t]hrough Mr. Seddon, jointly rejected Blue Cross's fee proposals and ultimately terminate their contracts with Blue Cross." Id. at ¶ 54(d).

Despite overwhelming evidence supporting these allegations, cited in the Complaint from defendant's and its orthopedic surgeon members' own documents, defendant has flatly denied that it and its members acted in concert. Amended Answer (D.I. 11) at ¶¶ 52-54. Rather, defendant claims that every one of the Federation members acted independently in resisting Blue Cross's proposed fee reductions, allegedly viewing the reductions as "so unreasonable that no individual physician or group turned out to be willing to accept them." Id. at ¶ 72. Indeed, defendant goes so far as to claim that its "members felt they were not

capable of providing and/or maintaining the standard of care necessary to their patients at the rates [Blue Cross] sought to impose" and, thus, "chose not to deal with Blue Cross." Id. at ¶ 76.

In view of defendant's denial of concerted action, the United States subpoenaed documents from First State and other orthopedic surgical groups who have been members of the Federation during the relevant period. The document requests focus, in part, on obtaining financial information that is relevant to proving the concerted nature of defendant's and its member surgeons' price fixing and boycott activities and to refuting the rationalizations that defendant has advanced to cloak those activities with its claim of independent action. Request No. 7, the one at issue here, simply seeks:

> Documents sufficient to show your practice's revenues and expenses (including all physician salaries and benefits) in 1997.

On November 12, 1998, First State filed numerous general and specific objections to the subpoena, including the following specific objections to Request No. 7:

> Request No. 7 is objectionable on the additional ground that it seeks purely private information that is not relevant and not reasonably calculated to lead to the discovery of admissible evidence, and instead is harassing and vexatious and reasonably calculated to cause needless embarrassment.

(D.I. 21). Counsel for plaintiff promptly sought to resolve First State's numerous general and specific objections to the subpoena, and, during a telephone conversation on November 19, 1998, both parties resolved all of First State's objections with the exception of its objections to Request No. 7.

Following the parties' initial productive discussion, on November 25, in a further attempt to resolve First State's objections to Request No. 7, counsel for plaintiff explained at length to counsel for First State the several grounds on which plaintiff believes the documents sought by Request No. 7 are relevant. But First State maintained its refusal to comply, and its production of subpoenaed documents, which was delivered to plaintiff on December 24, 1998, omits documents responsive to Request No. 7. Consequently, plaintiff was left with no alternative other than to file its motion to compel First State to produce documents responsive to subpoena Request No. 7.

IV. ARGUMENT

A. Rule 26(b)(1) Authorizes Broad Pretrial Discovery

Fed. R. Civ. P. 26(b)(1) provides, in part: "Parties may obtain discovery of any matter, not privileged, which is relevant to the subject matter involved in the pending action, whether it relates to the claim or defense of the party seeking discovery or to the claim or defense of any other party." "The key phrase in this definition--'relevant to the subject matter involved in the pending action'--has been construed broadly to encompass any matter that bears on, or that reasonably could lead to other matter that could bear on, any issue that is or may be in the case." Oppenheimer Fund, Inc. v. Sanders, 437 U.S. 340, 351 (1978); accord

Pennwalt Corp. v. Plough, Inc., 58 F.R.D. 257, 259 (D. Del. 1979) ("[t]his language has been given a very broad reading"); Scovill Manufacturing Co. v. Sunbeam Corp., 61 F.R.D. 598, 602 (D. Del. 1973) ("connotation of 'relevancy' is extremely liberal with respect to pre-trial discovery").

Accordingly, this Court has recognized that " 'discovery should ordinarily be allowed under the concept of relevancy unless it is clear that the information sought can have no possible bearing upon the subject matter of the action.' " In re ML-LEE ACQUISITION FUND II, 151 F.R.D. at 39 (quoting La Chemise Lacoste v. Alligator Co., Inc., 60 F.R.D. 164, 171 (D. Del. 1973)). Moreover, this Court has observed "that there is a general policy of allowing liberal discovery in antitrust cases." Kellam Energy, Inc. v. Duncan, 616 F. Supp. 215, 217 (D. Del. 1985). "Particularly where allegations of conspiracy or monopolization are involved, as in the instant case, broad discovery may be needed to uncover evidence of invidious design, pattern or intent." Id. Thus, in this antitrust conspiracy case, where defendant has alleged that its members acted independently for similar reasons, the Court should allow broad discovery of documents relevant to these alleged reasons.

. First State's Revenue and Expense Data are Relevant to this Antitrust Action on Several Grounds

The following four subsections discuss in detail the various claims and defenses to which First State's withheld revenue and expense documents are relevant under Rule 26(b)(1). Any one of these grounds warrant an order compelling production of those documents. Cumulatively, they unequivocally establish the documents' relevance and the merits of plaintiff's motion.

1. First State's Revenues and Expenses are Relevant to Assessing the Likelihood that First State's Termination of its Blue Cross Contract was Part of a Collusive Scheme by Federation Members

Defendant's claim that each of its member orthopedic groups independently terminated their respective Blue Cross agreements implies that each group was prepared to run the risk of losing its Blue Cross-insured patients to other, competing groups that might, in

the absence of collusion, continue doing business with Blue Cross. The evidence will demonstrate that defendant's members were aware, through numerous communications and meetings, that competing orthopedic groups would also be terminating their Blue Cross contracts. Consequently, Federation members were assured that they could terminate their respective Blue Cross contracts yet continue to be paid for treating Blue Cross patients at their higher billed rates because Blue Cross patients would have no good alternative for orthopedic surgery in Delaware. Despite the overwhelming evidence of this concerted behavior, defendant continues to deny such behavior. Consequently, plaintiff must seek all circumstantial, as well as direct, evidence of this concerted activity to meet its burden of proof at trial.

One circumstantial means to prove concerted action is to demonstrate that the Federation members' "parallel conduct was against the self-interest of each conspirator if they were acting alone." Bogosian v. Gulf Oil Corp., 561 F.2d 434, 446 (3d Cir. 1978). The documents responsive to Request No. 7 will enable plaintiff to determine the percentage of each member orthopedic group's revenues and costs that is attributable to Blue Cross (and the consequent extent that income would be lost). That information is relevant to determining whether, in terminating their respective Blue Cross contracts, each of defendant's member groups (including First State) acted consistently with its own financial interests. For example, it is far less likely that an orthopedic group would independently terminate its Blue Cross contract in response to the proposed fee reduction if the group, in view of its marginal costs, could profitably continue to treat Blue Cross patients at the lower fee levels. The United States, therefore, is surely entitled to the requested documents to test whether First State's revenue and cost factors are consistent with plaintiff's, or defendant's, view of what happened and why.

2. The Documents Sought are Relevant to Assessing Defendant's Claim that Each of its Members Acted Independently, Based on the Same Perception that Blue Cross's Proposed Fees were Too Low

As discussed above, the Federation's principal defense is that its members acted independently in rejecting Blue Cross's fee proposal. Defendant's contention rests on the subsidiary allegation that the fees Blue Cross proposed were too low for any orthopedic surgeon to accept. Indeed, defendant argues that Blue Cross was "exercising [its] monopsony power in the marketplace . . . to impose noncompetitive price decreases for providers." Amended Answer (D.I. 11) at ¶ 59. Ultimately, defendant is claiming that every one of its member physicians independently considered it unprofitable to serve Blue Cross patients at the proposed fee levels.

Information about First State's revenues and expenses is patently relevant to any assessment of this claim because it will allow plaintiff to evaluate First State's costs and the profitability of it providing services to Blue Cross patients at the reduced fee levels offered by Blue Cross. For example, if First State physician-salary levels demonstrate it was a highly profitable group practice and, indeed, paid salaries well above median levels for orthopedic surgeons, such information would cast doubt on a claim that First State physicians viewed the provision of their services at Blue Cross's proposed, reduced fee levels as an unprofitable endeavor. Access to First State's and other orthopedic groups' expense figures, particularly the information about physicians' salaries and benefits--the major item of expense to a physician practice--will also permit an assessment of the ability of First State and competing orthopedic practices to have tightened their cost structures to maintain their profitability, while accepting Blue Cross's reduced fees. Without revenue and cost data from First State and other major practice groups in Delaware, the United States will obviously be severely hamstrung in its efforts to refute the Federation's assertion that the proposed Blue Cross rates were a money-losing proposition for all Federation members.

3. Practice Cost Information is Relevant to Assessing Defendant's Implicit Claim that its Members Have Similar Cost Structures

In denying the existence of concerted action, defendant affirmatively asserts that its

orthopedic surgeon members' parallel actions reflect merely the independent recognition by each group practice that Blue Cross's proposed fees were unreasonable. Such an argument presupposes that defendant's member orthopedic surgeons have similar practice costs "because similar costs would necessarily require somewhat similar prices." Krehl v. Baskin-Robbins Ice Cream Co., 664 F.2d 1348, 1357 n. 22 (9th Cir. 1982). First State's costs for 1997--along with those for other Delaware orthopedic groups--are therefore directly relevant to defendant's claim. If discovery demonstrates that there were substantially different costs among defendant's Delaware orthopedic members' practices--including the physician-salary and benefits component of the practices' costs at each practice--such evidence would be consistent with plaintiff's claim that the Federation members' rejection of Blue Cross's proposed fee reductions was the result of collusion. See Weit v. Continental Illinois Nat'l Bank and Trust Co., 641 F.2d 457, 463 (7th Cir. 1981) (mere showing of parallel pricing behavior does not provide a basis for inference of price fixing conspiracy where each defendant faced "parallel costs"). Federation member orthopedic groups with lower cost structures would likely be more receptive to the proposed, reduced fees.

4. First State's Revenues and Costs in 1997 are Relevant to an Assessment of Defendant's Standard of Care Claim

First State's withheld financial documents will also help illuminate the invalidity of defendant's claim that each of its members independently rejected Blue Cross's proposal out of a concern for its alleged, perceived effects on the standard of patient care. The United States intends to expose this claim as merely a pretext for the Federation's and its members' concerted effort to avoid any lowering of physician fee income. In assessing assertions of purported motives for independent action, courts routinely evaluate whether the reason advanced is pretextual. E.g., Fragale & Sons Beverage Co. v. Dill, 760 F.2d 469, 474 (3d Cir. 1985) (evidence of pretext, if believed by a jury, would disprove likelihood of independent action); Alvord-Polk v. Schumacher & Co., 37 F.3d 996, 1012-1013 (3d Cir. 1994) (defendant's advancing of pretextual reasons for its actions "would tend to support an

inference that it acted as part of a conspiracy"); Big Apple BMW, Inc. v. BMW of North America, Inc., 974 F.2d 1358, 1363 (3d Cir. 1992) (reversing summary judgment because plaintiff set forth sufficient evidence of concerted action and further produced evidence tending to show that defendant's alleged independent reasons for actions were pretextual).

Thus, discovery of First State's 1997 revenue and cost information is clearly relevant to an evaluation of the alleged impact, if any, that Blue Cross's proposed fee reductions were likely to have on the standard of care provided by First State. A comparison of First State's costs, including physicians' salaries, with industry norms will assist in assessing defendant's standard of care argument because, if First State's physician salaries exceed industry norms, First State could have reduced its costs without causing any decrease in the standard of care it provides. The withheld information, therefore, sheds light on whether defendant's allegation that each of its members were independently concerned about erosion of their standard of care is simply a cover for their true motive and concerted opposition to Blue Cross's proposal. See, e.g., Fragale, 760 F.2d at 474; see also Kellam Energy, 616 F. Supp. at 217.

. **Contrary to First State's Objections, Request No. 7 is Neither Harassing, Vexatious, nor Calculated to Cause Embarrassment**

For the reasons explained above, the information sought in Request No. 7 is reasonably calculated to lead to the discovery of admissible evidence relevant to several issues directly related to the key issue of concerted action. The clear relevance of the material sought should, in and of itself, negate any argument that Request 7 is harassing or vexatious. Compare United States v. Howard, 360 F.2d 373, 381 (3d Cir. 1966) (upholding order that United States did not have to answer interrogatories where review showed "their lack of utility save as an harassment to the United States"). Moreover, First State has not claimed, and indeed cannot claim, that production of the requested documents would be burdensome.

This leaves only First State's argument that compliance with Request No. 7 would cause "needless embarrassment." But any concern about potential embarrassment can be appropriately accommodated by entry of plaintiff's proposed protective order (D.I. 35), filed

with the Court on December 30, 1998. That proposed order restricts pretrial disclosure of information designated confidential, such as First State's revenue and expense information.[2]

Moreover, First State's protestation that the information would cause "embarrassment" appears to prove plaintiff's point: The information could be "embarrassing" only if the practice's physician incomes significantly exceed industry norms. To the extent that First State's concern about embarrassment arises from its physicians' high income levels, they would disprove some of defendant's claims made in support of each member's purported, independent actions.

. **CONCLUSION**

The information that the United States seeks from First State is clearly relevant not only to defendant's denial of concerted action but also to defendant's affirmative allegations that each of its member groups acted independently. In view of defendant's denial and its affirmative claims, no reasonable view of the withheld information permits a conclusion " 'that the information sought can have no possible bearing upon the subject matter of the action.' " In re ML-LEE ACQUISITION FUND II, 151 F.R.D. at 39 (quoting La Chemise Lacoste v. Alligator Co., Inc., 60 F.R.D. 164, 171 (D. Del. 1973)). The Court should consequently order its prompt production.

Respectfully submitted,

COUNSEL FOR PLAINTIFF
UNITED STATES OF AMERICA

RICHARD G. ANDREWS
UNITED STATES ATTORNEY

_____/S/_____
By: Virginia Gibson-Mason (DSB # 3699)
Assistant United States Attorney

_____/S/_____
Steven Kramer
Richard S. Martin

[2] Indeed, even before the Court's entry of a protective order, First State's confidentiality concerns are protected pursuant to D. Del. LR 26.2 (restricting disclosure of confidential documents in the absence of a protective order to counsel). Therefore, upon this Court's determination of relevance, the documents sought should be produced promptly--as First State has produced other confidential, subpoenaed documents, relying on D. Del. LR 26.2.

1201 Market Street, Suite 1100
Wilmington, DE 19801
Tel.: (302)573-6277
Facsimile: (302)573-6220

_____/S/_____
Melvin A. Schwarz
Special Counsel for Enforcement
U.S. Department of Justice
Antitrust Division
601 D Street, N.W.
Washington, D.C. 20530
Tel.: (202) 305-1210
Facsimile: (202) 514-1629

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Denise E. Biehn
Michael D. Farber
Heather H. Howard
Jean Lin
Attorneys
U.S. Department of Justice
Antitrust Division
325 Seventh Street, N.W.
Washington, D.C. 20530
Tel.: (202)307-0997
Facsimile: (202)514-1517