No. 22-15634

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

DJENEBA SIDIBE ET AL.,

Plaintiffs-Appellants,

v.

SUTTER HEALTH,

Defendant-Appellee.

On Appeal from the United States District Court
for the Northern District of California

No. 12-cv-04854-LB
Honorable Laurel Beeler, Judge

BRIEF OF *AMICI CURIAE* STATES OF CALIFORNIA, ILLINOIS, NEW MEXICO, NORTH CAROLINA, OREGON, AND RHODE ISLAND AND THE DISTRICT OF COLUMBIA IN SUPPORT OF THE APPELLANTS

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INTEREST OF AMICI CURIAE AND SUMMARY OF ARGUMENT

The States of California, Illinois, New Mexico, North Carolina, Oregon, and Rhode Island and the District of Columbia respectfully submit this brief pursuant to Rule 29(a)(2) of the Federal Rules of Appellate Procedure. This case involves claims brought under a state antitrust law: California's Cartwright Act, Cal. Bus. & Prof. Code § 16720 *et seq*. When state antitrust claims are heard in federal courts, the federal courts must properly understand and apply the state law at issue—including aspects which, due to legislative choices and state common law, sometimes differ from the law that would apply to claims brought under federal statutes. An improper understanding of state law—and a failure to notice the differences between state and federal law—can lead not only to substantive errors, but also to procedural errors where the misunderstanding affects the federal court's exercise of discretion. The States, and their Attorneys General, are primary enforcers of their respective state antitrust and unfair competition laws and have vast experience in enforcing those laws. They respectfully submit this brief to offer perspective on the lower court's errors in interpreting the particular state law at issue in this case, and the broader implication of such errors more generally.

The brief will address three issues. First, the district court's jury instructions violated California law by disregarding the role of a defendant's purpose when determining whether a challenged practice violates the rule of reason in a

Cartwright Act claim. California's official pattern instructions, in keeping with the Cartwright Act's text and controlling decisions of the California Supreme Court, require consideration of the purpose behind a challenged practice as part of determining whether the practice violates the rule of reason. The district court refused to give such an instruction, however. Instead, apparently following some courts' view of how federal antitrust statutes operate, the district court excised any consideration of the role of purpose from jury instructions on the rule of reason. Federal courts adjudicating state-law claims are not permitted to override state legislative choices in that manner.

Second, that misunderstanding of the role of purpose under the State's substantive law contributed to a further error: the decision to prohibit Appellants from introducing as evidence communications in which Sutter's employees, at the time when they were initiating the conduct that Appellants later challenged, forthrightly admitted their anticompetitive motives. In the States' experience, antitrust violators frequently go to great efforts to disguise their illegal efforts as time goes on, and anticompetitive actors frequently try to invent new, false reasons when anticompetitive practices receive scrutiny. As a result, early "smoking gun" evidence of intent can be important—indeed, indispensable—to ensuring that state laws against anticompetitive conduct are properly enforced when actions are brought later in time. It can be equally important when anticompetitive conduct is

detected early—before that conduct has realized its goals of achieving price increases or other negative effects on the market.

A federal court's decision to admit or exclude evidence under Rule 403 is subject, of course, to review for abuse of discretion. But Rule 403 requires a balancing of "probative value" against the reasons for exclusion. And here the district court's misunderstanding of the substantive import of purpose under California's rule of reason—and of the indispensability of contemporaneous evidence of intent—led to such an abuse of discretion.

Finally, the district court appears to have misunderstood another important difference between California antitrust law and its federal counterparts. Federal statutes generally do not allow "indirect purchasers" to sue for the harm they suffer from a defendant's anticompetitive conduct toward direct purchasers. States such as California, however, have enacted statutes to allow indirect purchaser suits. The Cartwright Act requires a distinct mode of analysis for adjudicating such claims that equally applies to other states with indirect purchaser laws. Under that analysis, *liability* results from the defendant's anticompetitive conduct toward the relevant markets of direct purchasers; and the effect on indirect purchasers is relevant only as to subsequent determinations, such as whether the plaintiffs have made an adequately concrete demonstration of *damages*. Here, the district court refused to instruct the jury that its liability determination should be determined by

the effect Sutter's conduct had on the direct purchaser health plans. The jury instructions thus failed once again to give effect to an important feature of the state law governing the claim.

These legal errors would be of concern in any case. But they are particularly concerning to Amici in this case. This case concerns allegations that a California healthcare system engaged in conduct that violated state antitrust law by using its market power that certain of its hospitals possessed to leverage and tie in other hospitals lacking such market power in negotiations with California health insurers. The result was to coerce health insurers into paying unfair rates system-wide for healthcare services and to limit access and consumer choice. The Attorney General of California regularly investigates potential violations of antitrust and unfair competition laws to protect consumers and competition in the healthcare sector. Indeed, the Attorney General brought a successful action against Sutter in state court based on factual allegations that substantially overlapped those alleged by Appellants for injunctive relief, including for equitable disgorgement of illegal overcharges though that monetary claim tracked the claim of the direct purchaser class for damages. *See UFCW & Emp'rs Benefit Tr. v. Sutter Health*, Nos. CGC-14-538451, CGC-18-565398 (Cal. Super. Ct. S.F. Cty). In that case, the court approved a settlement in which Sutter agreed to pay $575 million to the direct purchaser class and the Attorney General to satisfy the damage claims of that

class. Sutter also agreed to 10-13 years of comprehensive injunctive relief overseen by a court-appointed compliance monitor. The vast size and complexity of the healthcare market (over $517 billion per year in California alone)[1] gives rise to numerous opportunities for anticompetitive conduct. Full enforcement of state statutes against illegal practices protects consumer health, and safeguards the financial soundness of insurers, employers, and governments. The district court's errors, which undercut those vital state policies and violated basic rules of federal procedure, should be reversed.

ARGUMENT

I. THE DISTRICT COURT ERRED IN FAILING TO INSTRUCT THE JURY TO CONSIDER WHETHER SUTTER'S CONDUCT HAD AN ANTICOMPETITIVE PURPOSE

Appellants asserted claims against Sutter for illegal tying and unreasonable restraints of trade in violation of California's Cartwright Act. 1-ER-17–21. The claims are therefore governed by California law as interpreted by the California Supreme Court. *See Paulson v. City of San Diego*, 294 F.3d 1124, 1128 (9th Cir. 2002) ("When interpreting state law, we are bound to follow the decisions of the state's highest court.").

[1] William Hsiao, Richard Scheffler, *United Financing of Health Care in California: The Road Ahead*, HEALTH AFFAIRS FOREFRONT (Aug. 11, 2022), https://www.healthaffairs.org/content/forefront/unified-financing-health-care-california-road-ahead.

A. California Law Requires Considering Purpose when Deciding Whether Conduct Is Anticompetitive Under the Cartwright Act

California's Cartwright Act was adopted in 1907. It prohibits "every trust" as "unlawful, against public policy and void." Cal. Bus. & Prof. Code § 16726. A trust, in turn, is defined to include "a combination of capital, skill or acts by two or more persons for any of the following purposes: (a) To create or carry out restrictions in trade or commerce . . . ." *Id.* § 16720. The statute correspondingly specifies that combinations are permissible where both their purpose and effect are to increase competition. *Id.* § 16725 ("It is not unlawful to enter into agreements or form associations or combinations, the purpose and effect of which is to promote, encourage or increase competition in any trade or industry[.]"). The California Supreme Court has interpreted these provisions as establishing that "[a] contract, combination, or conspiracy is an illegal restraint of trade if it constitutes a per se violation of the statute or has as its *purpose* or *effect* an unreasonable restraint of trade." *Corwin v. Los Angeles Newspaper Serv. Bur.*, 583 P.2d 777, 784 (1978) (footnote omitted). Reflecting those precedents, the Judicial Council of California's model jury instructions accordingly highlight the defendant's purpose as a necessary consideration under the rule of reason analysis.[2] The model

[2] The Judicial Council of California is a policymaking body for California state courts, whose membership is determined by California's Constitution. *See* CAL. CONST. art. 6 § 6. Although the Judicial Council's model jury instructions are

instruction for unreasonable restraints of trade includes as an element "[t]hat the purpose or effect of [*name of defendant*]'s conduct was to restrain competition[.]" *See* Judicial Council of California Advisory Committee on Civil Jury Instructions ("CACI") 3405(2). The model instruction for the rule of reason under the Cartwright Act directs the jury to decide whether defendant's "challenged restraint had an anticompetitive or beneficial purpose or effect" by considering "the results the restraint was intended to achieve . . . the reasonableness of the stated purpose for the restraint," as well as a number of other factors. CACI 3411(a)–(g).

Appellants sought such instructions. *See* Joint Proposed Jury Instructions (Disputed & Stipulated) at 75, 93, *Sidibe v. Sutter Health*, 3:12-CV-04854 (N.D. Cal. July 22, 2021), ECF No. 1133. The district court, however, denied the request and instead gave instructions that excised the need to consider Sutter's purposes for instituting the challenged restraints. 1-ER-20 (instructing that, to prevail, Appellants needed to prove "[t]hat the effect of Sutter's conduct was to restrain competition," without mentioning consideration of purpose); *id.* (instructing jury to decide "whether Sutter's challenged restraint has an anticompetitive or beneficial effect on competition" and to consider "the reasonableness of the restraint,"

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secondary, not primary, sources of law, the instructions are endorsed by the Judicial Council, which "makes every effort to ensure that they accurately state existing law." Cal. Rule of Ct. 2.1050(b). As such, use of the model jury instructions is "strongly encouraged." Cal. Rule of Ct. 2.1050(e).

without mention of considering purpose). Although the district court did not explain that decision, it appears to have credited Sutter's arguments, which relied on a line of federal precedents holding purpose irrelevant to federal claims under the Sherman Act. *See* Joint Proposed Jury Instructions (Disputed & Stipulated) at 79–80, *Sidibe v. Sutter Health*, 3:12-CV-04854 (N.D. Cal. July 22, 2021), ECF No. 1133; *see, e.g.*, *Levine v. Cent. Fla. Med. Affiliates, Inc.*, 72 F.3d 1538, 1552 (11th Cir. 1996).

Those precedents may be incorrect even as an interpretation of federal antitrust statutes.[3] But this case was brought under a state statute, under which there can be no question about the jury's duty to consider purpose in determining whether a given arrangement violates the rule of reason. As the California

[3] *See, e.g., Bd. of Trade of Chicago v. United States*, 246 U.S. 231, 238 (1918) ("[T]he purpose or end sought to be attained" is relevant under the Sherman Act's rule of reason analysis "because knowledge of intent may help the court to interpret facts and to predict consequences."); *Betaseed, Inc. v. U and I Inc.*, 681 F.2d 1203, 1228 (9th Cir. 1982) ("In determining whether a restraint is unreasonable, the court must consider whether the intent of the restraint is anticompetitive . . . ."); *New York ex rel. Schneiderman v. Actavis PLC*, 787 F.3d 638, 658 (2d Cir. 2015) (concluding that "[a]ll of Defendants' procompetitive justifications . . . are pretextual" based on evidence of antitrust defendants' anticompetitive intent); *Lewis Serv. Ctr., Inc. v. Mack Trucks, Inc*. 714 F.2d 842, 845 (8th Cir. 1983) ("Under a rule of reason analysis, the factfinder must scrutinize the intent and effect of the practice alleged . . . ."); KEVIN F. O'MALLEY ET AL., FEDERAL JURY PRACTICE AND INSTRUCTIONS, § 150:21 (6th ed. 2022) (instructing fact finder to consider "the reasons for adopting the particular practice that is alleged to be a restraint").

Supreme Court has explained, ""[i]nterpretations of federal antitrust law are at most instructive, not conclusive, when construing the Cartwright Act, given that the Cartwright Act was modeled not on federal antitrust statutes but instead on statutes enacted by California's sister states around the turn of the 20th century."[4] *In re Cipro Cases I & II*, 348 P.3d 845, 858 (Cal. 2015) (internal quotation marks omitted); *see Asahi Kasei Pharma Corp. v. CoTherix, Inc.*, 138 Cal. Rptr. 3d 620, 626 (Ct. App. 2012) ("[T]he Cartwright Act is not derived from the Sherman Act, but rather from the laws of other states, and the Cartwright Act and the Sherman Act differ in wording and scope." (internal quotation marks omitted)).

The Cartwright Act's text, as quoted above, refers to the purpose of a restraint in the two relevant provisions defining liability. *See* Cal. Bus. & Prof. Code §§ 16720, 16725. And the California Supreme Court, whose interpretation of the Cartwright Act binds federal courts in this context, has repeatedly affirmed that purpose plays a central role in a rule of reason analysis under the statute. *See Corwin*, 583 P.2d at 784 ("[a] contract, combination, or conspiracy is an illegal restraint of trade if it constitutes a per se violation of the statute or has as its

[4] This Court has similarly acknowledged the distinctions between the Cartwright Act and the Sherman Act. *See, e.g., Knevelbaard Dairies v. Kraft Foods, Inc.*, 232 F.3d 979, 985 (9th Cir. 2000) ("[F]ederal antitrust precedents are properly included in a Cartwright Act analysis, but their role is limited: they are 'often helpful' but not necessarily decisive.").

purpose or *effect* an unreasonable restraint of trade") (footnote omitted) (emphases in original); *Ixchel Pharma, LLC v. Biogen, Inc.*, 470 P.3d 571, 581 (Cal. 2020) (Cartwright Act's rule of reason standard asks "'whether an agreement harms competition more than it helps' by considering 'the facts peculiar to the business in which the restraint is applied, the nature of the restraint and its effects, and the history of the restraint and the reasons for its adoption'" (quoting *In re Cipro Cases I & II*, 348 P.3d 845, 861 (Cal. 2015))); *Marin Cty. Bd. of Realtors, Inc. v Palsson*, 549 P.2d 833, 844 (Cal. 1976) ("the rule of reason requires not only a demonstration that the anticompetitive practice relates to a legitimate purpose, but also that it is reasonably necessary to accomplish that purpose and narrowly tailored to do so").[5] The district court thus violated its duty to properly instruct the jury according to controlling state law on this state-law claim.

[5] California's Courts of Appeal—whose opinions would control if California Supreme Court opinions left any doubt—have likewise routinely considered the purpose of restraints in applying a rule of reason analysis. *See, e.g.*, *Kolling v. Dow Jones & Co.*, 187 Cal. Rptr. 797, 810 (Ct. App. 1982) (courts should consider "the purpose or end sought to be attained" in applying rule of reason analysis (internal quotation marks omitted)); *Saxer v. Philip Morris, Inc.*, 126 Cal. Rptr. 327, 336 (Ct. App. 1975) ("The court should consider . . . whether the action springs from business requirements or purpose to monopolize."); *see generally Franklin v. Cmty. Reg'l Med. Ctr.*, 998 F.3d 867, 874 (9th Cir. 2021) (when applying state law, federal courts "follow[] the decisions of intermediate state courts in the absence of convincing evidence that the highest court of the state would decide differently" (citing *Stoner v. N.Y. Life Ins. Co.*, 311 U.S. 464, 467 (1940))).

B. Consideration of a Restraint's Purpose Is Critical to Achieving the State Statute's Goals

The Cartwright Act's recognition of the importance of anticompetitive purpose is critical to achieving the statute's goal of deterring and detecting unfair and market-distorting practices. For one thing, the statute is designed to allow plaintiffs—including the Attorney General—to sue to enjoin an anticompetitive practice at its inception, before its anticompetitive effects have been achieved. *See, e.g.*, Cal. Bus. & Prof. Code § 16754.5. Consideration of purpose can be critical to the State's ability to address anticompetitive conduct in its earliest stages, when its harmful effects may only be indirect.[6] By eliminating anticompetitive purpose from consideration in a context where the effects are as yet only predicted, the district court's interpretation would deprive the statute of this important and intended aspect. Moreover, a defendant's unguarded early statements that a course of conduct is intended to reduce competition can be of great usefulness in assessing whether the defendant's later, litigation-driven avowals of the conduct's

[6] Direct anticompetitive effects include higher prices, reduced output, and reduced quality of goods in the market. By contrast, indirect anticompetitive effects may be found even early in the course of anticompetitive conduct where defendants have market power and there is "some evidence that the challenged restraint harms competition." *See Ohio v. Am. Express Co.*, 138 S. Ct. 2274, 2284 (2018). Evidence of purpose can illuminate the presence of either direct or indirect effects.

supposedly pro-competitive effect should be trusted. Indeed, the California Attorney General Office's own litigation against Sutter illustrates how. California sued Sutter in state court over the same practices Appellants attack here.[7] Like Appellants, the State was able to obtain documents in which Sutter employees, when first adopting those practices, discussed them as part of a strategy to achieve and maintain market power. 2-ER-177–79, 181–86. The documents showed that Sutter understood the pro-competitive effects of health plans' efforts to use narrow, tiered networks, steering, and other patient incentives to lower prices or otherwise provide choice. 2-ER-188–95. And the documents showed that Sutter adopted its contracting strategy in order to undermine these mechanisms of competition. 2-ER-181–86, 222, 246–47, 255. By refusing to instruct the jury on the need to consider Sutter's intent, the district court undermined the substantive goals and content of the state statute. The judgment should be reversed.

[7] The State's case filed in 2018 was consolidated with a private class action against Sutter that had been filed in 2014. Order Granting Motion to Consolidate, *UFCW & Emp'rs Benefit Tr. v. Sutter Health*, Nos. CGC-14-538451, CGC-18-565398 (Cal. Super. Ct. S.F. Cty. May 8, 2018). Although the state court matter involved factual allegations substantially overlapping with this case, the state case involved substantially similar, but not identical, theories of liability, different damages theories and different certified classes. *See* Complaint, *People of the State of California v. Sutter Health*, No. CGC-18-565398 (Cal. Super. Ct. S.F. Cty. Mar. 29, 2018); Order re Class Certification, *UFCW & Emp'rs Benefit Tr. v. Sutter Health*, No. CGC-14-538451 (Cal. Super. Ct. S.F. Cty. Aug. 22, 2017).

II. THE EXCLUSION OF CONTEMPORANEOUS EVIDENCE OF SUTTER'S INTENT TO RAISE PRICES WAS ERROR

A. Sutter's Contemporaneous Statements When It Adopted System-wide Contracting Were Key Evidence of the Elements of Liability

The district court granted Sutter's motions in limine numbers three and four, excluding all pre-2006 evidence on Sutter's intent in adopting system-wide contracting (to raise prices paid by health plans) and its other anticompetitive conduct. 1-ER-92–93, 110-11. This decision deprived the jury of key evidence showing both the purpose and history of Sutter's restraints, the exact kind of evidence that enforcers rely on to enforce state antitrust law.

Under California law pertaining to the elements of a Cartwright Act claim, this evidence was extremely relevant: The California Supreme Court has instructed that analysis of a restraint under the rule of reason test requires consideration of factors including "[t]he history of the restraint, the evil believed to exist, the reason for adopting the particular remedy, the purpose or end sought to be obtained." *Corwin*, 583 P.2d at 781. The emphasis on "history" and the "reason" for a restraint's original "adopti[on]" will often require consideration of evidence generated decades prior to the statute of limitations or class period. For example, in deciding a 2001 Cartwright Act challenge to a 1997 pay-for-delay agreement between Bayer and Barr Laboratories, Inc., the California Supreme Court considered much earlier events, including the history of Bayer's 1987 patent

for the drug at issue, Barr Laboratories' 1991 application to market a generic version of Cipro, and Bayer's monopoly of Cipro production from 1987 to 2003. *See Cipro*, 348 P.3d at 851–53. Similarly, when the California Court of Appeal considered a health insurer's 2014 policy that prohibited employers from using medical expense reimbursement plans or health expense reimbursement accounts, the court considered not only the insurer's imposition of similar restrictions beginning in 2006, but also its communications dating back to 2001. *See Ben-E-Lect v. Anthem Blue Cross Life and Health Ins. Co.*, 265 Cal. Rptr. 3d 495, 499–500, 502–06 (Ct. App. 2020).

Indeed, even federal cases applying the Sherman Act have engaged in extensive reviews of the overall history of restraints. When the U.S. Supreme Court recently decided on the permissibility of rules restricting the compensation of student-athletes under the rule of reason, its answer depended in part on the history of collegiate sports from 1852 to 2017. *See NCAA v. Alston*, 141 S.Ct. 2141, 2148–51 (2021). Failure to consider evidence relating to the adoption of the challenged conduct can be reversible error: In *Continental Ore Co. v. Union Carbide & Carbon Corp.*, the Supreme Court vacated a defense jury verdict and remanded the case for a new trial in part because of the trial court's exclusion of evidence that the conspiracy and monopolization began in the early 1930s. 370 U.S. 690, 709-10 (1962). The Supreme Court held that this evidence was "clearly

material" even though it was generated before the plaintiffs' entry into the relevant market in 1938, because it showed that upon market entry, the anticompetitive conduct alleged to have driven the plaintiffs out of business was already in existence. *Id.* These cases reflect that, because anticompetitive conduct can span decades, the most probative evidence relating to the history of a restraint may be found either at the inception of a restraint, or prior to a restraint's inception, long before statute of limitations or class period.

Here, the district court, through application of an arbitrary time bar, prevented the jury from knowing about Sutter's admitted intent to raise prices on health plans through its system-wide contracting practices. Internal Sutter memoranda explicitly stated that the reason to contract with health plans on a system-wide basis (i.e., having all Sutter hospitals collectively negotiate with health plans, rather than having Sutter hospitals individually negotiate with health plans) was to force the health plans to pay higher prices. 2-ER-178–79, 181–83. And this practice of system-wide contracting was the mechanism by which Sutter forced insurers to agree to additional anti-competitive provisions, including (1) anti-steering provisions (to prevent health plans from encouraging patients to opt for lower-cost providers), (2) anti-tiering provisions (to prevent health plans from sorting providers into tiers based on providers' cost and quality), and (3) provisions requiring the insurer to pay an unaffordable and unusual 95-percent of billed

charges for any patient that landed in a Sutter out of network hospital. 2-ER-222; 2-ER-255; 2-ER-288–89; 3-ER-577–80; 4-ER-691. Similarly, system-wide contracting is what allowed Sutter to condition the inclusion of inpatient hospital services in the tying markets on the inclusion of inpatient hospital services in the tied markets at a higher price. 3-ER-551–52, 577–80. Because system-wide contracting was the key mechanism by which Sutter could carry out its anticompetitive restraints of trade, evidence as to Sutter's intent in adopting system-wide contracting, and the history of this practice, was highly relevant to the rule of reason analysis of each of the mechanisms of restraint of trade that Appellants challenged.

B. Evidence Generated Prior to a Statute of Limitations or Class Period is Critical to Full Enforcement of the Cartwright Act

The district court's reasoning in excluding pre-2006 evidence poses significant challenges to full enforcement of the Cartwright Act going forward. The district court stated that it would limit evidence to be admitted at trial to five years before the class period, 1-ER-110–11, because a five-year cut off point "seem[ed] to be the default" for relevant discovery, 4-ER-733, and this case was "not about conduct that predates the contracting practices by more than five years." 1-ER-110–11.

In cases such as this, however, the imposition of such arbitrary and short cut-off periods effectively prevents fact finders from considering the full history and

intent of anticompetitive restraints. Because antitrust violations are difficult to detect, anticompetitive conduct often starts years before the filing of any litigation challenging that conduct. *See Rutledge v. Elec. Hose & Rubber Co.*, 327 F. Supp. 1267, 1274 (C.D. Cal. 1971), *aff'd*, 511 F.2d 668 (9th Cir. 1975) ("[S]eldom are the conspiratorial villains so devoid of cleverness as to broadcast their oral agreements or publicly circulate the written memos which describe their plan."). "Antitrust schemes generally are conceived in secrecy and live their lives in relative obscurity. It is only when they are called to face their creator that they betray their theretofore seemingly innocuous existence." *Saxer*, 126 Cal. Rptr. at 338–39.[8] Because evidence of intent is often generated early in a restraint's history, the ability to rely on evidence antedating the statute of limitations and class periods is critical to the State's enforcement efforts.

The original purpose behind a restraint—even if it antedates the limitations or class period—may thus be critical to the trier of fact's ability to understand whether a restraint has anticompetitive effects. *See Lyons v. England*, 307 F.3d 1092, 1110-1112 (9th Cir. 2002) (evidence of acts outside the limitations period

[8] Legislators' choice of remedies for antitrust violations reflects recognition of these challenges. *See* U.S. Dep't of Justice, *Antitrust Modernization Commission Report and Recommendation* (2007), 246 ("Treble damages compensate for the reality that some anticompetitive conduct is likely to evade detection and challenge."); *see, e.g.*, Cal. Bus. & Prof. Code § 16760(a)(2); 15 U.S.C. § 15(a).

"may constitute *relevant* background evidence in a proceeding in which the status of a current practice is at issue" and "may also be offered for its probative value in assessing whether the [defendant's] justifications for its present conduct lack credibility") (emphasis in original) (internal quotation marks omitted); *Reid Bros. Logging Co. v. Ketchikan Pulp Co*., 699 F.2d 1292, 1305–06 (9th Cir. 1983) (affirming admission of pre-statute of limitations evidence in Sherman Act case where "the background evidence is necessary to establish the defendants' role in the limited market . . . [and] the evidence clearly shows the continuing existence of the conspiracy"); *see generally Bd. of Trade of Chicago*, 246 U.S. at 238 ("[K]nowledge of intent may help the court to interpret facts and to predict consequences"). And as this case demonstrates, the best evidence of anticompetitive intent will often exist in admissions when the plan is first hatched, rather than afterwards when companies try to cover their tracks. The exclusion of critically probative evidence under an arbitrary cut-off date correspondingly was error and requires reversal.

III. THE JURY INSTRUCTIONS' FAILURE TO DEFINE THE RELEVANT MARKET MISINFORMED THE JURY AS TO THE CARTWRIGHT ACT'S REQUIREMENTS FOR LIABILITY IN INDIRECT PURCHASER CASES

The trial court's decision not to define in the jury instructions the identity of the relevant purchaser, left the jury in this case without the benefit of the fundamental tools that it needed to properly discharge its duty as the fact finder.

Well-crafted and detailed jury instructions are especially crucial in complex antitrust cases, including healthcare cases, where lay jurors are called upon to engage with abstract legal and economic concepts that are easily confused by even experienced antitrust practitioners. *See Los Angeles Mem'l Coliseum Comm'n v. Nat'l Football League*, 726 F.2d 1381, 1398 (9th Cir. 1984) ("Well-tailored and specific instructions may be necessary . . . in complex antitrust cases where . . . abstract legal principles are not self-explanatory to a lay jury, and the facts to which they must be applied are complex." (internal quotation marks omitted)). Instead of delivering such instructions here, the trial court left the jury uninstructed—and subject to a misimpression—about how the Cartwright Act treats indirect purchaser claims such as the one at issue here.

A. California Law Allows Indirect Purchaser Claims But Requires an Initial Determination of Liability at the Direct Purchaser Level

State and federal legislators have come to different conclusions about whether to allow antitrust claims brought by "indirect purchasers"—that is, individuals and entities that purchase a product from an intermediary. The Supreme Court long ago held that Congress's Sherman Act does not allow indirect purchasers to bring suit. *See Illinois Brick Co. v. Illinois*, 431 U.S. 720, 745–48 (1977) (holding that indirect purchasers lack standing to bring a Sherman Act claim even if higher costs from the antitrust violation are passed along to them).

That decision received criticism for leaving "most true victims of illegal cartels and other antitrust violations without a remedy to compensate them." *See* Robert H. Lande, *New Options for State Indirect Purchaser Legislation: Protecting the Real Victims of Antitrust Violations*, 61 Ala. L. Rev. 447, 448 (2010). In response, many States enacted so-called *Illinois Brick* repealer statutes, giving end consumers the ability as indirect purchasers to sue for violations of state antitrust law.[9] *Id.* at 448 n.10 (noting that 30 states have an *Illinois Brick* repealer statute).

California's endorsement of indirect-purchaser claims is codified at Cal. Bus. & Prof. Code § 16750(a). *See id.* ("This action may be brought by any person who is injured in his or her business or property by reason of anything forbidden or declared unlawful by this chapter, regardless of whether such injured person dealt directly or indirectly with the defendant."). As the California Supreme Court has recognized, the Cartwright Act, "unlike federal law . . . permits indirect purchasers as well as direct purchasers to sue." *Clayworth v. Pfizer*, 233 P.3d 1066, 1070 (Cal. 2010).

Clayworth further provides an answer to how indirect purchaser claims should be analyzed. In *Clayworth*, the court considered whether retail pharmacies

[9] North Carolina, for its part, permits indirect purchaser suits through judicial interpretation, rather than through an *Illinois Brick* repealer statute. *See Hyde v. Abbott Lab., Inc.*, 473 S.E.2d 680, 683 (N.C. Ct. App. 1996) ("The issue in this case is whether N.C.G.S. § 75–16 allows such a suit by an indirect purchaser. We hold that it does.").

could bring claims against drug manufacturers under the Cartwright Act. *Id.* at 1070-72. The manufacturers claimed that the pharmacies could not sue because they had passed along any overcharges to the end purchaser or consumer. *Id.* at 1071. The court recognized that federal antitrust law, according to *Hanover Shoe, Inc. v. United Shoe Mach. Corp.*, 392 U.S. 481 (1968), did not allow such a "pass-on" defense to defeat a claim. *Clayworth*, 233 P.3d at 1074–78. And the court determined that a similar rejection of the defense generally applies under the Cartwright Act. *See id.* at 1073 ("This rejection of using overcharge pass-ons as a defense occurs not because the law is blind to their existence, but rather because its eyes are open to their ubiquity."). At the same time, because the Cartwright Act permits suits by indirect purchasers as well as direct purchasers, consideration of pass-through effects can be necessary when it comes time to allocate damages. ("In instances where multiple levels of purchasers have sued, or where a risk remains they may sue," if "damages must be allocated among the various levels of injured purchasers, the bar on consideration of pass-on evidence must necessarily be lifted; defendants may assert a pass-on defense as needed to avoid duplication in the recovery of damages"). *Id.* at 1086.

As a result of *Clayworth*, an indirect purchaser claim under the Cartwright Act effectively requires two steps. *First*, to determine liability, the fact finder must determine whether anticompetitive conduct occurred at the *direct* purchaser level.

See id. at 1070–71 (providing overview of alleged conspiracy among defendant manufacturers to sell pharmaceutical drugs at artificially inflated prices to direct purchaser wholesalers). *Second*, there must be a determination of the *damages* suffered by indirect purchasers through the pass-on of overcharges. *See id.* at 1085-86.

As the district court recognized, this case involves a Cartwright Act claim for which "the alleged antitrust injury . . . is indirect." 4-ER-501. Specifically, Appellants alleged that Sutter raised the prices it charged health plans for inpatient hospital services and that the health plans, in turn, passed along higher costs to Appellants through higher health plan premiums. Thus, the fundamental inquiry for the jury on Sutter's liability was whether Sutter engaged in anticompetitive conduct at the direct purchaser level, causing the health plans to incur overcharges. How much of those overcharges were then passed along to the plaintiff class would be relevant only to the allocation of damages—which turns on how much of the overcharges were passed through to the consumers.

Here, Appellants requested an instruction that would have informed the jury that the relevant purchasers were the health plans that directly purchased inpatient hospital services from Sutter. 1-ER-95–96. The district court denied that request—and in so doing, allowed Sutter to seek a finding of no-liability based on their asserted lack of market power over indirect purchasers (the individual

consumer). *Id.* In so doing, the district court violated *Clayworth*'s reasoning as to the relationship between indirect and direct purchaser claims, and as to the California Legislature's goal of "maximizing deterrence." 233 P.3d at 1083. The instructions thus failed to "describe the applicable law." *Los Angeles Mem'l Coliseum Comm'n*, 726 F.2d at 1398.[10] Reversal is required.[11]

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[10] Sutter argued below, *see* Joint Proposed Jury Instructions (Disputed & Stipulated) at 62–63, *Sidibe v. Sutter Health*, 3:12-CV-04854 (N.D. Cal. July 22, 2021), ECF No. 1133, that defining the relevant purchaser or customer at the direct purchaser level would have prevented it from making arguments about a lack of market power based on the existence of Kaiser, a large closed system that generally has its own providers and provides its own insurance products with networks of those providers, *see, e.g.*, KAISER PERMANENTE, HELP ADVISOR, HOW TO FIND KAISER PERMANENTE IN-NETWORK DOCTORS, https://www.helpadvisor.com/medicare/kaiser-in-network-doctors (last visited Oct. 9, 2022). However, even in the context of an indirect purchaser suit where class members are users of non-Kaiser provider networks of non-Kaiser insurers in Northern California, Sutter could still have argued that Kaiser's presence affected whether class members in fact suffered damages. (For example, nothing in the two-step model would have prevented Sutter from attempting to show that the presence of Kaiser constrained insurers from passing Sutter's overcharges on to consumers.) Also, that Kaiser is not relevant to this indirect purchaser case, except as set out above, does not preclude analyzing the competitive effects on non-Kaiser insurers of a joint venture involving Kaiser's joint operation of a non-Kaiser provider in a Southern California local market. *See* CAL. OFFICE OF THE ATTORNEY GEN., *An Evaluation of the Proposed Change in Control of St. Mary Medical Center* (Nov. 11, 2021), https://oag.ca.gov/system/files/media/smmc-impact-report-2021-redacted.pdf; CAL. OFFICE OF THE ATTORNEY GEN., *Supplemental Report: An Evaluation of the Proposed Change in Control of St. Mary Medical Center* (Dec. 17, 2021), https://oag.ca.gov/system/files/media/smmc-supplemental-report-12172021.pdf.

[11] To the extent *Clayworth* leaves any ambiguity remaining about whether California law requires the two-step analysis, certification of the issue to the California Supreme Court could be appropriate, as Appellants have requested.

B. Proper Application of the Two-Stage Model is Also Appropriate Given Healthcare Economics

The district court's failure to instruct under the two-stage model also resulted in instructions that did not reflect the economic reality of how provider networks are assembled for inclusion in health plans provided to patients. In the modern American healthcare system, very few healthcare consumers directly purchase the care they receive from providers. Rather, "consumers purchase health insurance and the insurance companies negotiate directly with the providers." *Saint Alphonsus Med. Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd.*, 778 F.3d 775, 784 (9th Cir. 2015). Healthcare economists and courts have accordingly settled upon the two-stage model of competition as the primary analytical framework for addressing fundamental questions regarding healthcare markets, including the question of who the relevant customers are. *See, e.g.*, Gregory Vistnes, *Hospitals, Mergers, and Two–Stage Competition*, 67 Antitrust L.J. 671 (2000).

As this Court has explained in a case brought by the Federal Trade Commission and Idaho, "[the] 'two-stage model' of health care competition is 'the accepted model.'" *St. Luke's*, 778 F.3d at 784 n.10. "In the first stage, providers compete for inclusion in insurance plans. In the second stage, providers seek to

attract patients enrolled in the plans. Because patients are 'largely insensitive' to price, the second stage 'takes place primarily over non-price dimensions.' *Thus, antitrust analysis focuses on the first stage*." *Id.* (emphasis added). The two-stage model has also been applied by other courts examining healthcare cases brought by the Federal Trade Commission and various states. *See FTC v. Hackensack Meridian Health, Inc.*, 30 F.4th 160, 168 (3d Cir. 2022) (Federal Trade Commission); *FTC v. Advocate Health Care Network*, 841 F.3d 460, 470–71 (7th Cir. 2016) (Federal Trade Commission and Illinois); *FTC v. Penn State Hershey Med. Ctr.*, 838 F.3d 327, 342 (3d Cir. 2016) (Federal Trade Commission and Pennsylvania) *ProMedica Health Sys., Inc. v. FTC*, 749 F.3d 559, 562 (6th Cir. 2014) (Federal Trade Commission); *FTC v. Sanford Health*, No. 1:17-CV-133, 2017 WL 10810016, at *11 (D.N.D. Dec. 15, 2017), *aff'd*, 926 F.3d 959 (8th Cir. 2019) (Federal Trade Commission and North Dakota).

Regulators—including the Federal Trade Commission and state attorneys general as per the cases cited above—likewise have determined that the two-stage competition model is the most appropriate analytical framework in healthcare antitrust enforcement, where it is necessary to understand the respective roles of the provider, payor and the end consumer or patient. For example, the California Attorney General's Office routinely applies the two-stage competition model in its

hospital merger reviews analyzing the ability of hospital providers to raise rates on health plans post-merger.[12]

As courts and regulators have recognized, the different markets in which health insurers and end consumers interact with hospital providers mean that price-related competition occurs at the first stage or the direct purchaser stage, whereas the second (or indirect purchaser) stage involves mainly non-price factors such as reputation and referrals.

Here, the Court's failure to define the relevant customer or purchaser on key issues as being healthcare insurers, not end consumers of healthcare insurers,

[12] *See, e.g.*, CAL. OFFICE OF THE ATTORNEY GEN., *An Evaluation of the Proposed USC Health System/Methodist Hospital of Southern California Affiliation* (Apr. 22, 2022), https://oag.ca.gov/system/files/media/mhsc-usc-impact-report-04222022.pdf; CAL. OFFICE OF THE ATTORNEY GEN., *An Evaluation of the Proposed Change in Control of St. Mary Medical Center* (Nov. 11, 2021), https://oag.ca.gov/system/files/media/smmc-impact-report-2021-redacted.pdf; CAL. OFFICE OF THE ATTORNEY GEN., *The Competitive and Quality Impact of the Proposed Acquisition of Adventist Health Vallejo by Acadia Healthcare* (Sept. 25, 2021), https://oag.ca.gov/system/files/media/ahv-cqi.pdf; CAL. OFFICE OF THE ATTORNEY GEN., *Competitive Effects Analysis of the Proposed Cedars-Sinai Health System/Huntington Memorial Hospital Affiliation* (Dec. 4, 2020), https://oag.ca.gov/sites/all/files/agweb/pdfs/charities/nonprofithosp/ag-decision-huntington-121020.pdf?. Other states have done the same. *See, e.g.*, STATE OF RHODE ISLAND OFFICE OF THE ATTORNEY GEN., *Decision Re: Hospital Conversion Act Initial Application of Rhode Island Academic Health Care System Inc. et al.* at 30-37 (Feb. 17, 2022), https://riag.ri.gov/press-releases/attorney-general-denies-application-merger-lifespan-and-care-new-england-health.

meant that the instructions failed to reflect the requirements of the Cartwright Act and the economic reality of the markets in question.

CONCLUSION

This Court should reverse the judgment and remand for further proceedings under proper jury instructions and with relevant evidence.

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FOR THE NINTH CIRCUIT

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