

AGREEMENTS BETWEEN EYE DOCTORS AND MANUFACTURERS TO PROHIBIT DEALING BY NONPRESCRIBING RETAILERS

By Professor Einer Elhauge¹

Agreements between contact lens manufacturers and eye doctors to restrict retail competition from nonprescribing retailers raise two sorts of economic and legal concerns. First, they exacerbate agency costs between eye doctors and patients by giving eye doctors higher profits if they prescribe and recommend such doctor-only lenses rather than other lenses that are better and cheaper. Second, they create anticompetitive problems by restricting a form of retail competition that demonstrably lowers costs. The two problems are related given the facts that eye doctors influence purchase decisions far more than patients and that licensing restrictions mean manufacturers cannot simply create additional eye doctors to expand their distribution in the way firms in many other markets can. This gives manufacturers incentives to compete not by attracting consumers with low prices but by attracting eye doctors through offers of high retail markups that are effectively bribes designed to distort their agency decisions and by organizing participating eye doctors into a cartel that refuses to deal with nonprescribing retailers and steers prescriptions away from manufacturers who do. The evidence confirms that these agreements are in fact producing the predicted distortion of agency advice and anticompetitive effects. And the agreements have no plausible redeeming virtue.

By creating a right to get prescriptions filled by nonprescribing retailers, the Fairness to

¹ Professor of Law, Harvard University. These comments are submitted on behalf of 1-800-CONTACTS and not on behalf of Harvard University, which does not take institutional positions with respect to specific legislation, litigation, or regulatory proceedings.

Contact Lens Consumers Act was intended to address precisely these conflict-of-interest problems and these anticompetitive concerns. Unfortunately, that right is thwarted whenever eye doctors prescribe a brand of lens that is unavailable to nonprescribing retailers by virtue of such agreements. Such agreements also violate more general laws on fiduciary duties, disclosure, deception, and antitrust.

Some appropriate remedies for these problems include: (1) prohibiting eye doctors from selling the lenses that fill the prescriptions they write; (2) prohibiting prescriptions that specify a particular manufacturer rather than just the lens characteristics indicated by the eye exam; (3) prohibiting manufacturers and eye doctors from restricting competition from nonprescribing retailers; and/or (4) at a minimum, requiring manufacturers and eye doctors who do engage in such restraints to disclose to consumers: (a) that the relevant lenses cannot be sold by cheaper nonprescribing retailers; (b) that this gives eye doctors financial incentives to prescribe those lenses; (c) that there is no safety disadvantage to buying from nonprescribing retailers; and (d) any information that might suggest another brand of lenses might offer greater safety advantages.

I. BACKGROUND AND FACTS

Background. Patients cannot legally buy contact lenses without a valid prescription from an eye doctor who conducts an eye exam. Unlike medical doctors, who cannot sell the drugs that fill the prescriptions they write, eye doctors can and generally do sell the contact lenses that fill the prescriptions they write. Those prescriptions may, and in almost all cases do, specify a particular manufacturer, and when they do so, the prescription may not legally be filled with lenses by a different manufacturer even if the relevant physical parameters are the same.² This white paper concerns agreements among manufacturers and eye doctors to restrict the availability of a prescribed manufacturers' lenses to nonprescribing retailers.

The Fairness to Contact Lens Consumers Act provides that an eye doctor must provide a prescription to the patient or verify it for other sellers, and cannot require that patients buy the contact lenses from the prescribing retailer. *See* 15 U.S.C §7601. In enacting this legislation, Congress explained it was designed to address two concerns. First, because “eye doctors and optometrists (‘doctors’) are able to fill the contact lens prescriptions they write” they had “an inherent conflict of interest because third party sellers are forced to compete for the sale of lenses with the individual who is writing the prescription.” H.R. REP. 108-318. Congress was worried that this conflict of interest would be exacerbated if eye doctors could prescribe contact lenses that only they could sell. Second, Congress wanted to “increase competition in the sale of contact lenses which will bring a substantial savings to America's contact lens wearers,” with Congress finding that

² *See* 15 U.S.C §7603.

“Consumers who order prescription refills from alternative sellers can save, on average, 20 percent per order.” *Id.* Congress accordingly intended the statute to end optometrist practices that “limited the consumer's ability to shop for the best price.” *Id.* As Congress noted, “The consumer's right to a copy of their contact lens prescription means nothing unless consumers can fill that prescription at the business of their choice.” *Id.* Giving consumers that right was thus designed to “promot[e] competition, consumer choice, and lower prices . . . and allo[w] consumers to purchase contact lenses from the provider of their choice.” *Id.* Congress directed the Federal Trade Commission (FTC) to promulgate any rules necessary to carry out this act, and to impose on any violation the same penalties as for unfair or deceptive acts or practices. *See* 15 U.S.C §§ 7607-08.

The FTC Act more generally makes unlawful “[u]nfair methods of competition” and “unfair or deceptive acts or practices,” and authorizes the FTC both to penalize such conduct with enforcement actions and to promulgate rules defining such conduct. 15 U.S.C. §45. In an earlier round of competition rulemaking and litigation, the FTC used this authority to bring litigation and enact rules that ended private and public restraints that required consumers to buy their eyeglasses or contact lenses from the eye doctor who gave them a prescription and prevented eye doctors from engaging in price advertising.³ In doing so, the FTC concluded that restricting competition from nonprescribing retailers did not have procompetitive effects that outweighed its anticompetitive

³ *See* Comments of the Staff of the FTC, Intervener, *In re: Declaratory Ruling Proceeding on the Interpretation and Applicability of Various Statutes and Regulations Concerning the Sale of Contact Lenses*, Before the Connecticut Board of Examiners for Opticians (March 27, 2002) (summarizing the prior rules and litigation), *available at* <http://ftc.gov/be/v020007.htm>; 16 C.F.R. §§ 456.2(b), 456.1(c); Ophthalmic Practice Rules, Final Trade Regulation Rule, 54 Fed. Reg. 10,285 (Mar. 13, 1989); Advertising of Ophthalmic Goods and Services, Statement of Basis and Purpose and Final Trade Regulation Rule, 43 Fed. Reg. 23,992 (June 2, 1978); *American Optometric Ass’n v. FTC*, 626 F.3d 896, 899-900 (1980); *In the Matter of Massachusetts Bd. of Registration in Optometry*, 110 FTC 549 (1988); Letter from FTC Chairman Timothy J. Muris, to the Honorable Ward Crutchfield, Tennessee Senate Majority Leader n.12 (April 29, 2003), *available at* http://www.ftc.gov/be/v030009.htm#N_12_.

effects, and also reached the same conclusion about restrictions on price advertising.

Before 2001, three of the five major U.S. manufacturers of contact lenses – Johnson & Johnson, CIBA Vision, and Bausch & Lomb -- entered into agreements with distributors and eye doctors not to sell their lenses to nonprescribing retailers and to restrict competition from nonprescribing retailers for the sale of lenses to consumers. Thirty-two state attorneys general and a nationwide class of consumers brought litigation against these restraints. In 2001, the three manufacturers agreed to consent decrees requiring them to sell their lenses to nonprescribing suppliers.

The Restraints and Practices in this Case. The above litigation did not name as defendants OSI or Proclear. At the Contact Lens Association of Ophthalmologists annual meeting held in February 2001, as the above consent decrees were being finalized, OSI made a presentation to eye doctors as a group. OSI stated that eye doctors were suffering because of competition from alternative distribution channels like 1-800 Contacts, and told the group of eye doctors that the best way to protect themselves from such competition would be for them to agree to prescribe OSI brands that both OSI and eye doctors agreed would not be made available to nonprescribing retailers who tried to sell to someone other than their own patients.⁴ OSI stressed that it would prevent itself or its distributors from selling its lenses to nonprescribing retailers, but that in return doctors had to agree both (1) to refuse to resell these lenses to nonprescribing retailers and to sell them only to their patients and (2) to refrain from advertising OSI lenses outside their offices or from putting prices

⁴ See Appendix A (Notes on 2001 CLAO Annual Meeting); Appendix B (Faxes Between the Utah Attorney General and CLAO, and from CLAO to OSI).

on the advertisements put in their offices.⁵ The latter commitment prevents advertising that might bring in patients from other eye doctors. This thus made clear that the scheme was designed to prevent not only competition from retailers who had no eye doctors on premises, but also competition by one eye doctor for the business of consumers who got their eye exam at another eye doctor.

In the wake of the consent decrees, OSI also sent a letter to every eye care professional. This letter stressed that the consent decrees required its major competitors to sell to nonprescribing retailers, but that OSI was not bound by these consent decrees and would continue its longstanding policy of refusing to sell to any nonprescribing retailers and requiring that its distributors do the same.⁶ John D. Fruth, chairman and CEO of OSI, also made public statements that: “We have a policy that says no doctor, no slit lamp, no Ocular Sciences product. . . . We’re going to enforce these contracts with legal actions instead of just cutting people off. . . . When a diverter entices a customer to violate that contract, we’re going to take legal action against the diverters.”⁷

OSI also recruited eye doctors to join this anticompetitive scheme with advertisements in magazines that target eye doctors and enjoy a large circulation among them. These advertisements explicitly stated that eye doctors were suffering from lower-priced competition from nonprescribing retailers and price advertising.⁸ The ads contained statements like:

⁵ *Id.*

⁶ See Appendix C (Ocular Sciences Letter to Eye Care Professionals (Jan. 28, 2002)).

⁷ See Appendix D at 66 (Review of Optometry (April 15, 2001)).

⁸ See Appendix E (Every Tom, Dick and Harry Ad); Appendix F (Help Your Patient Catch the Latest Wave Ad).

- “Traditional eye care is being challenged. Mail order is rampant. Every Tom, Dick and Harry is offering your patients ‘low priced’ disposables.”
- “Today the basic economics of a successful practice are being altered by: . . . consumer advertising promoting price. . . Mass-market communications, including the internet. . . .Consumer branding of contact lenses is not in your best interest. The reason is—consumer branding of contact lenses leads to price advertising for the product without the necessary services for proper care. And even more problematic is the internet’s brutal efficiency in turning well-known contact lens brands into commodities – all based on price.”

The advertisements further stated that eye doctors could protect themselves from such retail competition by prescribing OSI lenses because OSI was committed to prevent nonprescribing retailers from obtaining them, required that its distributors and retailers sign agreements to sell lenses only to their own patients, electronically kept track of each box of OSI lenses to make sure it was not sold to a nonprescribing retailer, and would cut off anyone who did resell to a nonprescribing retailer.⁹ These ads stated:

- “If IT THREATENS your practice WE’LL SEE it. As the only major contact lens manufacturer that does not sell to non-professional Internet and mail-order resellers, we’re on red alert for market predators who attempt to divert our lenses. We promote patient loyalty by selling our clinically proven, patient-preferred products exclusively to you, the eye-care professional. (Over 90% of Biomedics wearers return to their prescribing professional.) Using sophisticated bar coding that allows us to trace our lenses and enforce our distribution to professionals only, we take strict and active measures to protect you, including litigation against diverters. The way we see it, keeping our eyes wide open keeps your practice well protected.”
- ““No slit lamp, no practitioner, no Biomedics lens. (Our special bar coding tracks every six pack – divert to mail order and we cut you off.)”
- “You’ve heard us say it over and over: ‘No slit lamp, no practitioner, no lenses.’ To better control lens distribution, we require Hydrogenics 60 UV dispensers to sign an agreement and pledge to sell these lenses only to their own patients. Ocular Sciences has implemented and continues to develop lens control systems such as bar-coding our packages to try and eliminate so-called ‘gray marketing.’”
- “Sorry mailorder guys, our monthly PROACTIVE 55 blister packs will be barcoded just like our disposable lenses. This unique individual blister tracing system allows us virtually total traceability to identify diverters.”

⁹ See Appendix E; Appendix G (If It Threatens Your Practice Ad); Appendix F.

– “the Hydrogenics 60 UV [is] a lens available only to authorized independent private practitioners.”

The advertisements stressed that the result of eye doctors prescribing OSI lenses would thus be to restrict competition by nonprescribing retailers.¹⁰

– “Make the system work for you with the new Hydron Biomedics 55 lens. It’s one way to help keep professional eye care where it belongs. Off the mail order roller coaster and right in your hands.”

– “We firmly believe that patients must return to their eye care professional to receive proper eye care and we’re doing everything we can to assure this result with monthly replacement.”

– “Product Coding to Help You Retain Your Patients.”

The advertisements argued that OSI’s commitment to help eye doctors retain their retail sales of contact lenses by protecting eye doctors from competition by nonprescribing retailers was an important reason for eye doctors to write prescriptions that switched patients from other brands to OSI lenses.¹¹

– “Switch me. . . . Refitting your patients with Ocular Sciences’ . . . lenses is better for your practice as well. Patients prescribed with the Biomedics 55 UV or the Hydrogenics 60 UV are more likely to return to your office for replacement lenses (and exams) than are patients fit with consumer-branded products.”

– “Over 95% of Patients Fitted with Ocular Sciences Lenses Return to Your Practice,” whereas the percentages for B&L, CIBA and J&J were 65-79% without OSI’s “professional-only” policy.

Finally, OSI advertised to eye doctors that other eye doctors understood the threat that nonprescribing retailers posed to their business. OSI advertisements quoted eye doctors as saying:¹²

– “Outside competition like 1-800 Contacts and other Internet providers are gradually siphoning our patients away. We should be more aggressive in putting up barriers against

¹⁰ See Appendix E.

¹¹ See Appendix H (Switch Me Ad); Appendix F.

¹² See Appendix I at 3-4, 10, 14 (“Using a Soft Contact Lens for Patient Retention” Ad).

that . . . “

– “originally we were fitting lenses like those from CIBA and Bausch & Lomb, and we would get calls from patients and 1-800 Contacts asking us for their contact lens prescriptions. I wanted to use another strategy to prevent that from happening. One of the strategies was private labeling. I didn’t know of any company other than Ocular Sciences that was doing it, or is doing that now effectively. Now when the patients want to order lenses, they like the particular lens that we provide. It’s a private label, so they can’t get it anywhere else. It makes it a lot easier for them to come back to us. If they go down to Wal-Mart or Costco or someplace like that and ask, ‘Do you have this lens?’ Costco or Wal-Mart or 1-800 would say, ‘Yes, we do, but it’s a different name on the box.’ That creates the problem within the patient’s mind about whether or not it’s the same lens. . . . I often don’t give the patients a choice. I don’t say this is a private label lens. I just say, ‘This is the best lens for you. It’s the one you should be wearing.’”

– “third party administrators are now requiring detailed contact lens information about the insured patients you are fitting. There can be only one reason that they want to know detailed information about the contact lens specifications—so they can send direct mailings to these patients, offering them discounted contact lenses. Obviously, if they do not have access to the Hydrogenics lens, . . . then that is definitely a determining factor in which lens I am going to reach for.”

Proclear (now owned by CooperVision) similarly advertised that its agreements restricting the availability of its lenses to nonprescribing retailers would increase the profits of eye doctors who prescribed its lenses by keeping out lower-cost retail competition. Their ads said:

– “You’ll make more money . . . since Proclear Compatibles are only available through your practice, you’ll get what you are looking for: increased patient loyalty and greater profitability.”¹³

– “There’s a better way to keep patients in your practice. . . . Introducing 1-Stop. It’s time to stop the revolving door in your practice and begin to retain patient loyalty. Patients are your most valuable asset. We can help protect your practice from eroding margins and keep contact lens patients coming back to see you instead of a website, 800 number or a discount store. . . . 1-Stop gives patients exactly what they are looking for . . . – but only through you. . . . 1-Stop, the one stop your patients need to make each year – at your office.”¹⁴

As the last ad makes clear, even the brand name was meant to indicate that patients prescribed Proclear’s “1-Stop” would have to buy their lenses from whoever gave them their eye exam and

¹³ See Appendix J (“Let’s see. You’ll make more money” Ad).

¹⁴ See Appendix K (1-Stop Ad).

prescription – precisely what Congress, the FTC and the state attorneys general hoped to stamp out.

OSI’s distribution contracts were consistent with this conspiracy to exclude competition from lower-cost nonprescribing retailers. In them, OSI promised that it would sell its brands “exclusively for use by suitably qualified eye-care professionals for resale to those professionals’ own patients.”¹⁵

OSI further promised that when it entered into any agreement with any other distributor, it would do so “on the strict understanding that the product will eventually be sold exclusively by eye-care professionals for resale to those professionals’ own patients.”¹⁶ OSI’s agreements with distributors thus covered not only the terms of their contractual relationship but also covered the terms under which OSI would deal with all other distributors. OSI’s contract further promised that it “specifically does not authorise the sale of the product, either directly or indirectly, to alternative distribution channels such as internet-based or mail order retailers.”¹⁷ But the terms of the restraint also barred distribution to any eye doctor who competed to sell OSI lenses to patients who got their eye examination from another eye doctor. OSI required its distributors to make sure that retailers understood these restrictions and to terminate any retailer who failed to abide by them.¹⁸ OSI promised to enforce these conditions by having each box of its lenses scanned before sale to retailers, making spot purchases from mail order and Internet providers, and thus identifying which distributor or retailer resold to any nonprescribing retailer.¹⁹ OSI’s Canadian distribution contracts likewise obligated them not to resell their lenses to (a) any retailer who did not have an eye doctor

¹⁵ See Appendix L (Ocular Sciences Distribution Agreement at 1 (Oct. 10, 2001)) (this agreement covered Biomedics lenses and their various private or quasi-private label equivalents).

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

on the premises or (b) any retailer who had an eye doctor on the premises but resold the lenses to retailers who did not.²⁰

OSI also admits in its comments to the FTC that “OSI lenses are only available from eye care professionals,” by which it means that “OSI does not sell contact lenses to retailers that do not also provide substantial eye care services.”²¹ OSI further acknowledges that this reflects agreements rather than just unilateral action because it says: “OSI’s agreements with its retailers prohibit these retailers from selling OSI contact lenses to anyone other than to consumers for their personal use.”²² Although OSI thus prevents all its lenses from being made available to nonprescribing retailers, it does allow some of its brands to be available to some mass merchandisers, but only if they are willing to incur the cost of hiring an eye doctor to be on the premises giving the eye exams that generate prescriptions. Further, many OSI brands are unavailable at many retail chains. OSI concedes that “its Hydrogenics 60 product is only available to independent (i.e., those not affiliated with a chain) eye care professionals with five or fewer offices.”²³ OSI not only bars sale of its Biomedics lens (and various private or quasi-private label versions of it) to all nonprescribing retailers, but also limits some prescribing mass merchandisers to only selling the private or quasi-private labels rather than the Biomedics brand.²⁴

²⁰ See Appendix M at 1.01-1.05 (OSI Canada Corporation Authorized Distributor Agreement).

²¹ See Comments submitted on behalf of OSI by James Langenfeld & Robert Maness, Competition, Consumer Awareness, and Distribution in the Contact Lens Industry at 22, 28 (June 24, 2004), available at <http://www.ftc.gov/os/comments/contactlensstudy/509969-0012.pdf>

²² *Id.* at 29.

²³ *Id.*

²⁴ OSI offers some clones of Biomedics as private or quasi-private labels to one or a limited set of mass merchandisers (like Ultraflex to Wal-Mart, Colevision, BJ’s Optical, America’s Best, Sears Optical, and For Eyes) or eye doctors (like Mediflex, Softview, and Edge III to some eye doctors). Sometimes, if an eye doctor is large enough, he can create his own licensed name (“Highland Optical 55”) as a true private label unique to his firm. These private and quasi-private labels are not even available to other firms with eye doctors on the premises and are even less available

CooperVision likewise bars sale of its Proclear lens by any nonprescribing retailer. It also makes its Proclear lens available to those mass merchandisers who specialize in eye care (like Pearle Vision or LensCrafters) but not to other mass merchandisers (like Wal-Mart or Costco). CooperVision also does not make either Encore or Cooperflex available to nonprescribing retailers, but does make a clone brand (Frequency) available to 1-800-CONTACTS.

Table 1 summarizes the doctor-only restraints used by these firms and their participating prescribing firms and eye doctors.

TABLE 1: DOCTOR-ONLY RESTRICTIONS IMPOSED BY OSI AND COOPERVISION

Manufacturer Brand	OSI		CooperVision	
	Hydrogenics	Biomedics 38, 55 & Toric	Proclear DW, Compatibles & Toric	Encore
Available to Mass Merchandisers Who Use Eye Doctors <i>as that Brand?</i>	No	Some*	Some**	Yes
Available to Mass Merchandisers Who Use Eye Doctors under a Private or Quasi-Private Label that is not available outside some limited set of retailers?	No	Yes	No	No
Available to Mass Merchandisers Who Do Not Use Eye Doctors <i>as that brand?</i>	No	No	No	No
Available to Mass Merchandisers Who Do Not Use Eye Doctors <i>as a different brand?</i>	No	No	No	Yes (as Frequency)

Notes: * Includes Wal-Mart. ** Available to optical chain like LensCrafters and Pearle Vision, but not to more general retailers like Wal-Mart or Costco.

The Increased Prices to Consumers. Since these restraints restrict competition from lower cost distributors, they predictably harm consumers by increasing prices. The available evidence

to alternative distributors like 1-800 Contacts. Reflecting this increased lack of competition, mass merchandisers and eye doctors generally charge more for these private/pseudo-private label brands even though they actually pay less for them. This also indicates price discrimination at wholesale and at retail, which further supports the conclusion that market power exists at both levels. See 1992 Horizontal Merger Guidelines, 57 Fed. Reg. 41,552 §§1.12, 1.22 (Sept. 10, 1992); PHILLIP AREEDA & LOUIS KAPLOW, ANTITRUST ANALYSIS 437 (5th ed. 1997); CARLTON & PERLOFF, MODERN INDUSTRIAL ORGANIZATION 277 (3rd ed. 2000); DON E. WALDMAN & ELIZABETH J. JENSEN, INDUSTRIAL ORGANIZATION 436 (2d ed. 2001); Richard A. Posner, *Oligopoly and the Antitrust Laws: A Suggested Approach*, 21 STAN. L. REV. 1562, 1578-79 (1969); Hal R. Varian, *Price Discrimination*, in 1 HANDBOOK OF INDUSTRIAL ORGANIZATION 599 (Richard Schmalensee & Robert D. Willig eds., 1989).

confirms this prediction. For example, 1-800-CONTACTS reports that to its knowledge OSI and Proclear's prices in the United States are twice what they charge in the EU, where they do not have agreements restricting competition from nonprescribing retailers.

Testing within the United States for price effects is difficult for OSI since it offers no lens available to nonprescribing retailers with the United States that can be used as a baseline for comparison. But we have some baseline for comparison with Coopervision since it offers not only a brand (Proclear) that is unavailable to nonprescribing retailers in any form, but a brand (Encore) that is available under a different brandname to nonprescribing retailers, and a brand (Frequency) that is freely available as that brand to nonprescribing retailers.

What the data shows is that Proclear Compatibles sell for \$20.50 at wholesale while Frequency 55 sells for \$10.00.²⁵ There appear to be no significant differences in quality or production cost that would explain this price differences. This evidence suggests that the restrictions on competition by nonprescribing retailers allows a manufacturer to inflate wholesale prices by 100% and have prescribing retailers pass that increase on downstream in higher retail prices.

Adverse effects on retail prices can clearly also be shown, as Table 2 demonstrates.²⁶

²⁵ See Appendix N (CooperVision's June 1, 2003, U.S. Distributor Price List).

²⁶ This table is based on a survey conducted by 1-800 Contacts employees of retail prices as of September 2004. 1-800 Contact's prices were obtained from the company's website. The prices for the retail chains were obtained through a series of telephone interviews. Prices reflect the price per six-pack when a six-pack is purchased with four or fewer boxes. Prices do not include any charges for shipping and handling. If those were included the price differences would be even more notable since 1-800-CONTACTS does not charge for shipping lenses ordered from its website, whereas Wal-mart and others do.

**TABLE 2: RETAIL PRICE EFFECTS OF RESTRICTING DISTRIBUTION
BY NONPRESCRIBING RETAILERS**

Make Brand	Wal-Mart	Pearle Vision	Lens Crafters	Sterling Optical	Average Price By These Chain Prescribing Retailers	1-800 Contacts	Average Savings (Percent)
CooperVision Encore	\$28.96	\$47.95	NA	\$40.00	\$38.97	\$19.95*	\$19.02 (48.8%)
CooperVision Proclear	NA	\$45.99	\$58.78	\$45.00	\$49.92	\$34.95**	\$14.97 (30.0%)

Note: * Sold as Frequency. ** Obtained on the gray market and sold as Proclear.

This pricing evidence indicates several important things. *First*, a nonprescribing retailer like 1-800-CONTACTS clearly offers a significant discount (30-48.8%) from the prices charged by prescribing retailers – including from prescribing retailers like Wal-Mart and retail chains like Pearle Vision and Lens Crafters, all of whom must incur the costs of having a prescribing eye doctor on the premises. This if anything understates the discount because the figures do not include charges for shipping and handling, for which Walmart and others charge but which is free to web customers of 1-800-CONTACTS. This rebuts the claim that the availability of such lenses to mass merchandisers or retail chains means no harm to consumers can follow from denying contact lenses to nonprescribing retailers like 1-800-CONTACTS.²⁷

Second, these prices indicate that the fact that agreements restrict the availability of a brand to nonprescribing retailers does matter even though 1-800-CONTACTS is able to get a limited supply on the gray market from those who are willing to breach the relevant agreements. In

²⁷ OSI has so claimed. See OSI Comments by Langenfeld & Maness, *supra* note 21, at 35-36.

particular, while 1-800-CONTACTS can, by getting some Proclear lenses on the gray market, sell at a 30% discount to the retail prices charged by prescribing retailers, it is able to charge a 48% discount when there are no agreements that bar it access to a lens that can be used to fill an Encore prescription. Further, even the 48% figure likely understates the consumer harm because the Encore brand is not available to nonprescribing retailers, which impedes competition by creating confusion in consumers' minds that makes many unwilling to have their prescription filled with Frequency even though it is much cheaper, physically identical, and made by the same manufacturer.

Third, the availability of lenses at discount prices from nonprescribing retailers also appears to have a constraining effect on the prices charged at prescribing retailers. The retail prices charged by prescribing retailers for Proclear lenses are 28% higher than for Encore lenses (\$49.92 compared to \$38.97), which, since the quality of the lenses does not significantly differ, would seem to be due to the fact that Proclear lenses do not face as vigorous price competition from nonprescribing retailers.

All this is consistent with earlier conclusions by Congress and the FTC. Congress concluded that “Consumers who order prescription refills from alternative sellers can save, on average, 20 percent per order.” H.R. REP. 108-318. The FTC has likewise found that: “In 1998, the average price of a six-lens multipack purchased via mail order was \$19.90, compared to an average of \$23.76 for lenses purchased from ophthalmologists, optometrists, and optical chains - a 19 percent difference.”²⁸

²⁸ See Comments of the Staff of the FTC, *supra* note 3.

Denying consumers the option of buying from nonprescribing retailers thwarts consumer retail choice at least for the 62% of consumers who say they would prefer to buy from a mail-order firm if the price difference were 15% (if we use the general 19-20% discount amount) and for the 78% who would prefer to do so if the price difference were 25% (if we use the 30-48% discount for these brands where distribution by nonprescribing retailers is restricted).²⁹ Further, this denial also results in higher prices for all consumers (even those who prefer to buy from prescribing retailers) because the prices charged by those prescribing retailers are less restrained by price competition from nonprescribing retailers.

The Lack of Any Redeeming Virtue. These significant anticompetitive effects are not offset by any redeeming virtue. None of the justifications offered for such restraints are plausible. For example, OSI tries to defend the restraints against competition from nonprescribing retailers by arguing that: “It is well accepted that when one channel (e.g. Internet outlets) can free ride off the promotional efforts of other channels, limited distribution is an important element in encouraging other channels to invest in advertising.”³⁰ But this cannot possibly be a justification for the restraints here, for those restraints *prohibit* price advertising or any advertising outside the prescribing retailer.

Indeed, it is noteworthy that, while OSI offers a long defense of their restricted distribution practices, none of their theories attempts to explain why those agreements would include provisions prohibiting approved prescribing retailers from either advertising OSI prices anywhere or having any OSI advertising outside their locations. To the contrary, as just noted, they offer as a

²⁹ *Id.*

³⁰ OSI Comments by Langenfeld & Maness, *supra* note 21, at 30, 42. *See also id.* at 33.

procompetitive justification the claim that restricted distribution will *increase* such advertising.³¹ Further, OSI itself acknowledges that “truthful and non-misleading advertising can help consumers manage their own health care” and that “advertising is an important catalyst for price and quality competition.”³² This clearly indicates that OSI’s restrictions on advertising can have no procompetitive justification, and thus must be intended to further the anticompetitive purpose of restricting retail competition *among* prescribing retailers, which does not fit any justification OSI offers nor any plausible justification one might imagine. That is, the inclusion of these provisions confirms that the real purpose of the restriction distribution was simply the anticompetitive one of reducing retail competition in general, and not really to achieve any allegedly legitimate objective by distributing only through eye doctors.

OSI and Proclear also claim that precluding competition from nonprescribing retailers encourages prescribing retailers to provide additional monitoring services that enhance patient health and that otherwise would be driven out by free riding.³³ But this argument fails on multiple scores. *First*, eye doctors in fact generally do not provide additional monitoring services to make sure replacement lenses are working well, and are not required or even encouraged by OSI to do so. To the contrary, OSI itself stresses that (1) prescribing eye doctors can provide OSI lens by mail or the Internet if they wish to do so for the convenience of customers and (2) consumers can buy a year’s supply of OSI lenses from their eye doctor so that they do not have to return until they need a new

³¹ See *id.* at 30, 33, 42.

³² *Id.* at 25 (quoting Comments of the Staff of the Bureau of Consumer Protection and the Bureau of Economics of the Federal Trade Commission, In the Matter of Direct to Consumer Promotion; Public Hearing Docket No. 95N-227, Before the Food and Drug Administration, January 11 , 1996).

³³ See *id.* at 31-32, 43; Appendix E; Appendix F; Appendix J.

prescription.³⁴ In fact, two-thirds of eye doctors utilize direct shipping from the manufacturer rather than requiring their patients to return to the office,³⁵ and even an eye doctor who prescribed OSI lenses acknowledged that 75% of those who got their lenses from his office left with a full year's supply.³⁶ Certainly there is no evidence that eye doctors provide more follow-up services for lenses that do restrict competition from nonprescribing retailers than for lenses that do not.

Second, even if such additional services were provided, there would be no way for consumers to free ride on them. Eye doctors can and do charge separate fees to cover eye exams and initial fitting. And if eye doctors did provide additional monitoring services when patients picked up replacement lenses from them, patients would not be able to get these services and then somehow carry their benefit over by instead buying from a nonprescribing retailers. Thus, the situation is not at all like the purchaser of stereos who goes to a stereo boutique to get advice from an expert salesperson about what stereo to buy and then free rides off that expertise by driving over to Costco and buying the recommended stereo. Eye doctors have already charged for the prescription that recommends the contact lens purchase, and any additional monitoring services would only be provided if the patient returns to pick up replacement lenses. Thus, if patients actually valued those follow-up services, they would be willing to pay for them without any need to restrain competition from nonprescribing retailers.³⁷

³⁴ See OSI Comments by Langenfeld & Maness, *supra* note 21, at 29; Appendix E; Appendix F; Appendix I at 5-6.

³⁵ Appendix D at 68.

³⁶ Appendix I at 5.

³⁷ If for some reason there were a real threat of free riding on some legitimate valuable service, there would be a plain, less restrictive means to barring competition from nonprescribing retailers: eye doctors could just charge for such services separately as they do for eye exams.

Third, to the extent such follow-up visits are required, they are an affirmative cost that exacerbates, not offsets, the anticompetitive effect. As the FTC found, requiring consumers to travel to a prescribing retailer (be it an eye doctor or a mass merchandiser that has an eye doctor on the premises) imposes a time cost of \$10.96-26.00, which reflects a markup of 50-130% price markup.³⁸ This reflects a pure efficiency waste because those costs are not transferred to anyone but are simply unnecessarily imposed in order to maintain the anticompetitive restraint on rival nonprescribing retailers.

Fourth, the FTC staff has already concluded that requiring patients to buy lenses from their eye doctors does not provide any meaningful additional service or safety benefit.³⁹ It noted there is “no systematic evidence that sales through alternative channels, such as Internet or mail order, pose any additional health risk as long as the retailer sells in accordance with a valid prescription.”⁴⁰ Since the Fairness to Contact Lens Consumers Act prohibits alternative channels from selling without a valid prescription, any purported safety concern is thus already precluded by law.⁴¹

Further, in fact:

“medical practitioners do not examine the fit of each replacement lens on the patient's eye after the prescription has been finalized through the fitting process. In fact, some lens manufacturers provide direct shipment of replacement lenses to consumers, and some eye care practitioners mail replacement contact lenses to patients without an office visit during the span of the patient's prescription. Thus, the practice, *even among some traditional eyecare professionals*, suggests that replacement lenses can be marketed and delivered . . . without adverse health effects.”⁴²

³⁸ See Comments of the Staff of the FTC, *supra* note 3.

³⁹ See *id.*

⁴⁰ *Id.*

⁴¹ See 15 U.S.C §7603.

⁴² See Comments of the Staff of the FTC, *supra* note 3 (emphasis in original).

The FTC also noted:

“Concerns about quality of care related to follow-up examinations can be addressed by enforcing contact lens prescriptions, rather than by inhibiting sales by non-traditional providers. Requiring customers to return to an eye care professional to purchase replacement lenses does not reduce the individual's incentive or ability to wear lenses for too long. Moreover, Connecticut law does not allow opticians to examine eyes or treat eye problems, so forcing consumers to purchase replacement lenses from an optician does not advance the health goal of more frequent eye exams.”⁴³

The state attorneys general presumably reached the same conclusion, for their consent decree with the American Optometric Association prohibits that association from “represent[ing] directly or indirectly that the incidence or likelihood of eye health problems arising from the use of replacement disposable contact lenses is affected by or causally related to the channel of trade from which the buyer obtains such lenses. Specifically, AOA shall not represent directly or indirectly that increased eye health risk is inherent in the distribution of replacement disposable contact lenses by mail order or pharmacy or drug stores.”⁴⁴ It seems safe to assume the state attorneys general would not have required a consent decree that prohibited optometrists from speaking the truth about safety issues, so one can reasonably infer the state attorneys general must have concluded those safety claims were false. Indeed, as the FTC confirmed, the consent decree provision barring such safety claims “is precisely consistent with medical evidence presented in the multidistrict litigation.”⁴⁵ This included evidence that optometrists were unable to obtain any documented reports of health problems from buying from nonprescribing retailers, that no scientific study suggested any greater health problems, and that several optometrists testified the source should not matter.⁴⁶

⁴³ *Id.*

⁴⁴ Appendix O at ¶2(h) (Preliminary Settlement Agreement with AOA, In re: Disposable Contact Lens Antitrust Litigation).

⁴⁵ See Comments of the Staff of the FTC, *supra* note 3.

⁴⁶ *Id.*

Fifth, the legitimate safety concerns run in precisely the opposite direction. The FTC concluded that the availability of lens through nonprescribing retailers may well increase lens safety because it lowered costs and thus induced consumers to reduce overwearing of lenses and to buy safer disposable lenses rather than conventional daily wear lenses.⁴⁷ By prescribing more costly lenses that are not available through nonprescribing retailers, eye doctors are thus likely causing patients to make less safe choices and overwear their lenses more. Indeed, customer complaints about health problems were actually much lower for lenses bought from nonprescribing retailers.⁴⁸

Moreover, as Congress correctly concluded, allowing eye doctors to sell contact lenses gives them a conflict of interest.⁴⁹ If some manufacturers – here OSI and CooperVision – give eye doctors a higher profit margin on their lenses by protecting them from competition from nonprescribing retailers, then eye doctors have incentives both to prescribe those lenses over others even if they are *less* safe and to make inaccurate statements to patients about their supposed safety advantages. This was highlighted in a remarkable magazine supplement paid for by OSI that, in stressing the advantages of prescribing OSI lenses because of the protection from outside competition, contained the following discussion of safety where OSI quoted several eye doctors explaining how they sold OSI lenses with inaccurate safety claims or recommendations that misleadingly omitted disclosing safety disadvantages.

The discussion first quoted one eye doctor as saying: “We’ve been using Hydrogenics 60

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *See* H.R. REP. 108-318.

lenses for a while . . . I tell my patients that it's the safest lens on the market. With . . . the inability to get this lens without a valid prescription, it ends up being a safer lens."⁵⁰ OSI's advertisement supplement went on to quote the eye doctor as saying that what he meant was that, when a lens is available from nonprescribing retailers like 1-800-CONTACTS, then patients can obtain those lens five years later after their prescription has run out, creating safety risks for the patient and a risk of legal liability for the eye doctor who prescribed such lenses.⁵¹ But this advertised statement is untrue. The law clearly prohibits nonprescribing retailers from filling orders without a valid prescription. *See* 15 U.S.C §7603. And as noted above, there is no evidence that buying contact lenses from nonprescribing retailers increases health risks. To the contrary, increased health risks result when the unavailability of low priced lenses from nonprescribing retailers causes patients to overwear their lenses to cut costs. Ironically, such overwearing is precisely what this eye doctor was affirmatively recommending to his patients in order to cut the high expense of the OSI lenses he was prescribing that were unavailable from cheaper nonprescribing retailers.⁵² The claim that eye doctors would be legally liable if others violated the prescription laws on other lenses is also manifestly untrue, and in and of itself constitutes deceptive advertising and fearmongering.

The next eye doctor then admitted he was concerned about claiming OSI lenses were safer because the data was to the contrary. He stated:

"I started to say the Hydrogenics was the safest lens, but then my associate came to me and said, 'How can you say that to a patient when the Dk is lower than the Acuvue lens?' . . . Since I've been using the Hydrogenics lens, I like it better, but then I look at the numbers and I see we've got a Dk of 24.3 vs. 28 for Acuvue. Can we make that statement that it is

⁵⁰ Appendix I at 9.

⁵¹ *Id.* at 9, 13.

⁵² *Id.* at 7.

a safer lens?”⁵³

The answer OSI’s advertisement supplement then gave was *not* that doctors should just prescribe the safer lens, nor that OSI’s disadvantage in Dk (a measure of oxygen transmissability) should be fully disclosed to patients when prescribing OSI lenses. OSI’s advertisement supplement instead quoted one eye doctor confirming the 4 point disadvantage in DK but saying the Dk’s were nonetheless “about equal,” and then quoted another eye doctor as stressing that ordering other lenses would result in “calls from patients and 1-800 Contacts asking us for their contact lens prescriptions” and that “I often don’t give the patients a choice. . . . I just say, ‘This is the best lens for you. It’s the one you should be wearing.’”⁵⁴

OSI’s advertisement supplement then quoted the next eye doctor stating:

“If you wanted to be safest, you would probably put your patients in the new Focus Night & Day (CIBA Vision)lens, which provides high oxygen permeability. . . But for daily wear, I think there’s excellent safety with every contact lens that’s out there. I think two or three points on the Dk really does not make a difference in terms of safety, so when I say it’s the safest lens, that’s assuming that a patient is taking it off every night.”⁵⁵

Finally, it quoted another eye doctor as saying:

“Generally, we position the UV lens, the Hydrogenics, as our lens of choice. I simply present it to patients who are successful contact lens wearers, by saying ‘Would you like to try the newest lens technology?’ Almost without exception, they all want to try the newest lens technology. I do not present it as the safest lens available, but simply as the newest technology . . .”⁵⁶

That same eye doctor then candidly admitted that the inability of third parties to offer discounted

⁵³ *Id.* at 9-10.

⁵⁴ *Id.* at 10.

⁵⁵ *Id.* at 12.

⁵⁶ *Id.*

OSI lenses to his patients “is definitely a determining factor in which lens I am going to reach for.”⁵⁷

In short, even OSI’s paid advertisement supplement inadvertently reveals that doctor-only agreements distort the sort of statements eye doctors make to their patients. They cause eye doctors to prescribe lenses that do not have highest safety measures, to make false claims that OSI lenses are the safest, or to simply present OSI lenses as the best choice without disclosing contrary evidence on safety. And OSI advertisements coach eye doctors to make these sorts of statements. If this is what even OSI’s own advertisements indicate, the reality of the distorting effect on eye doctor prescriptions and statements to patients is likely far greater.

* * *

In short, the agreements restricting competition from nonprescribing retailers raise not only the sort of anticompetitive concerns that guide FTC and other regulators in enforcing antitrust laws, but consumer deception concerns that should motivate FTC and other regulators to enforce consumer protection laws.

Indeed, along with the participating eye doctors, OSI and Proclear are basically seeking through their agreements to install precisely the sort of undesirable and uncompetitive regime that Congress, the FTC, and the state attorneys general had sought to end: a regime where consumers must buy their prescribed lenses from the eye doctor who gave them a prescription, where eye doctors engage in no price advertising about lenses, and where eye doctors are paid higher retail

⁵⁷ *Id.* at 14.

markups in exchange for distorting the prescriptions and advice they give. The costs to consumers and supposed benefits of such a regime have already been assessed by all those government actors, which correctly concluded that the costs are significant and the supposed benefits nonexistent.

EXACERBATING AGENCY AND INFORMATION PROBLEMS: FIDUCIARY DUTIES, DISCLOURE AND DECEPTION

The facts described above indicate the following. OSI and Proclear are wooing eye doctors by offering them higher profit margins on their contact lenses in exchange for eye doctors prescribing OSI and Proclear lenses. This market strategy appears to be successful in getting eye doctors to steer new patients toward OSI and Proclear lenses: according to OSI's own analysis, the market share of OSI and CooperVision are both higher for new patients, with their combined share for all patients at 25.5% and their share for new patients at 31.2%.⁵⁸ OSI and Proclear are also making deceptive safety claims in their advertisements about the relative risks of lenses bought from nonprescribing retailers. Eye doctors who prescribe OSI lenses are, according to OSI's own advertisements, likewise making deceptive safety claims to their patients or are recommending OSI lenses without disclosing contrary safety information. And OSI advertisements are coaching eye doctors to engage in this sort of behavior. Eye doctors are also prescribing OSI lenses without revealing the eye doctor's financial interest in doing so, and the evidence suggests that these financial incentives do distort eye doctor prescriptions. This raises several economic and legal

⁵⁸ See OSI Comments by Langenfeld & Maness, *supra* note 21, at 5.

concerns.

Agency Problems and Special Fiduciary Duties. For consumer choice to function well, consumers must be able to ascertain the value of the product they are buying compared to other products. For contact lenses, however, consumers do not make such judgments themselves. Rather, they rely on eye doctors to prescribe contact lenses for them as their agent, and that creates agency problems whenever the interests of the doctor/agent diverge from the interests of his patient/principal.

This partly reflects the fact that consumers lack sufficient information. Even though consumers may know the value of corrected vision to themselves, they cannot be expected to keep track of complicated technical issues about which type of contact lens would offer them the best and most comfortable corrected vision with the least risk. OSI acknowledges that this problem is real and significant for medical care in general, but argues that contact lens consumers are so well-informed that they can second-guess the judgment of their eye doctors.⁵⁹

Part of OSI's argument is that consumers are so well-informed about contact lenses that they have no serious informational disadvantage compared to their eye doctors. This claim seems clearly over-stated: one doubts that many consumers, for example, know about the Dk disadvantage of OSI lenses compared to Acuvue. Further, this argument misses the deeper point that the problem is not just that patients lack information. The deeper problem is that the *knowledge* necessary to evaluate

⁵⁹ *See id.* at 26-28.

the information may require exactly the set of skills that patients are purchasing from their eye doctor.⁶⁰ For example, a patient may know the Dks of various lenses. But without the same training and experience as an eye doctor, the patient will not fully understand what that means or how much of a health benefit it might provide. Unless patients have the equivalent of eye doctor training, patients will always be less able to determine the value of various characteristics of lenses than their eye doctor. Obviously, the costs of such patient training would be prohibitive. More fundamentally, such patient training would undermine the main reason for seeing eye doctors at all -- that the eye doctor knows something the patient does not. In short, the inability of eye care patients to fully evaluate their contact lens purchase is inherent in the fact that what they are purchasing from eye doctors *is* knowledge about what purchase decision to make.

Second, OSI argues that even if consumers have some informational disadvantage the first time they buy contact lenses, that disappears over time because contact lenses patients are repeat players who must get their contact lens prescriptions renewed and refilled in upcoming years.⁶¹ Thus, if a consumer has a bad experience with the contact lenses he buys, he won't return to the same eye doctor the next time. But the problem with this argument is threefold. First, of all, even if a consumer does have a bad experience with the contact lenses he receives, he will have no basis for determining whether the fault lies with the lenses his eye doctor prescribed or because the patient has dry eyes or is otherwise a poor candidate for contact lenses. Second, the most prevalent problem is that consumers will have a pretty good experience with their contact lenses, but will never know

⁶⁰ See Kenneth Arrow, *Uncertainty and the Welfare Economics of Medical Care*, 53 AMER. ECON. REV. 941 (1963).

⁶¹ See OSI Comments by Langenfeld & Maness, *supra* note 21, at 27-28.

that their experience could have been better (or just as good and less expensive) if they had bought other contact lenses. Third, for many consumers, the inflated retail prices for contact lenses will induce them to instead buy eyeglasses, and thus these consumers will not have any experience with the contact lenses in question.

In any event, even if consumers were well-informed, the fact remains that they legally cannot obtain whatever contact lens they want without an eye doctor, and thus are dependent on an eye doctor for access to their desired product.

For all these reasons, the key purchase decision – that is, which contact lens is named in the prescription – is made by the eye doctor who writes that prescription, not by the patient. And thus patients must rely on eye doctors, as the patients' agents, for purposes of deciding what contact lens to prescribe. Such an agency relationship predictably produces divergency costs when, because the agent and principal have diverging interests, the agent takes action contrary to the principal's interests.⁶² Here, as OSI acknowledges, such divergency costs can result if eye doctors exercise their discretion to prescribe contact lenses that are more profitable to the physician, even though they are more costly or less beneficial to the patient.⁶³ Principals (here patients) can try to reduce divergency costs through increased monitoring of the agent (such as gathering more information themselves). But as long as eye doctors have some informational advantage that makes them worth hiring at all, monitoring will never be perfect and thus some divergency cost will always remain.

⁶² See Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. FIN. ECON. 305, 330 (1976).

⁶³ See OSI Comments by Langenfeld & Maness, *supra* note 21, at 26-27.

We can thus minimize, but not eliminate, agency costs that reflect the sum of monitoring and divergency costs.⁶⁴ Although unavoidable, those agency costs will still be worth bearing if they are offset by the benefits of having an agency relationship (here the benefits of hiring eye doctors at all). But society still has an interest in adopting market rules that minimize agency costs to reduce any avoidable inefficiency drag such costs would otherwise create.

This is not a new problem for the law, which governs the agency relationship with many standard fiduciary duties that reflect the law's view about how best to minimize total agency costs. These fiduciary duties extend far beyond the duty to avoid deceptive statements that applies to ordinary businesses. Every agent has a fiduciary duty not to make secret profits from third parties when acting as an agent.⁶⁵ Thus, eye doctors are in breach of their fiduciary duties if they fail to disclose *all* material facts regarding any increased profits they make from prescribing OSI and Proclear lenses over lenses that are more available from nonprescribing retailers. This duty to disclose any such financial interest applies even if the eye doctors are dealing fairly and in good faith with their patients.⁶⁶ This is also true even if patients already know that eye doctors are making

⁶⁴ See Jensen & Meckling, *supra* note 62, at 308.

⁶⁵ See Restatement (Second) of Agency §388 (“Unless otherwise agreed, an agent who makes a profit in connection with transactions conducted by him on behalf of the principal is under a duty to give such profit to the principal.”); Restatement (Second) of Agency §389 (“Unless otherwise agreed, an agent is subject to a duty not to deal with his principal as an adverse party in a transaction connected with his agency without the principal's knowledge.”); *Henderson v. Hassur*, 225 Kan. 678, 688 (1979) (“An agent who makes a secret profit in connection with transactions conducted by him on behalf of the principal is under a duty to give such profit to the principal.”).

⁶⁶ See Restatement (Second) of Agency §388 Comments (“Thus, an agent who, without the knowledge of the principal, receives something in connection with, or because of, a transaction conducted for the principal, has a duty to pay this to the principal even though otherwise he has acted with perfect fairness to the principal and violates no duty of loyalty in receiving the amount.”); Restatement (Second) of Agency §389 Comments (“The agent's failure to reveal that he has an interest in the transaction is sometimes spoken of as fraudulent. . . . But, irrespective of the words used to characterize the agent's conduct, such a transaction can be rescinded by the principal although the agent acts in good faith and without consciousness of wrong doing. . . . The rule stated in this Section is not based upon the existence of harm to the principal in the particular case. It exists to prevent a conflict of opposing interests in the minds of agents whose duty it is to act solely for the benefit of their principals. The rule applies, therefore, even though the transaction

some profit on contact lenses and thus understand that eye doctors have at least some degree of conflict of interest – patients are entitled to all material facts regarding the financial incentives that might cause eye doctors to prescribe one contact lens over another.⁶⁷ The reason is simple: patients are not in an arms-length business relationship with eye doctors. Rather, patients are relying on eye doctors for professional advice about which lens to buy, and thus need to have disclosed to them any information that might possibly compromise the neutrality of that advice.

Indeed, as medical professionals, eye doctors not only have ordinary fiduciary duties, but also have heightened duties to disclose under the doctrine of informed consent. These informed consent duties apply to optometrists and other eye care providers who make prescriptions for contact lenses even though they are not physicians.⁶⁸ This informed consent duty requires full and accurate disclosure not only about the medical risks of the recommended treatment but about alternatives and their relative risks.⁶⁹ Eye doctors thus violate this informed consent doctrine if they prescribe OSI or Proclear lenses without revealing any safety information that might suggest benefits to using other lenses, such as the Dk difference that is acknowledged in OSI's own paid advertising. Further, informed consent also requires a health care giver to “disclose personal interests unrelated to the

between the principal and the agent is beneficial to the principal.”).

⁶⁷ See Restatement (Second) of Agency §389 Comment (“Unless the terms of such an agreement provide otherwise, an agent acting as an adverse party, even though with the knowledge of the principal that he is so doing, is subject to the duty stated in Section 390 to reveal to the principal all the material facts which he knows or which he should know, and to deal fairly with the principal.”); Restatement (Second) of Agency §390 Comment (“One employed as agent violates no duty to the principal by acting for his own benefit if he makes a full disclosure of the facts to an acquiescent principal and takes no unfair advantage of him. Before dealing with the principal on his own account, however, an agent has a duty, not only to make no misstatements of fact, but also to disclose to the principal all relevant facts fully and completely.”); *Desfosses v. Notis*, 333 A.2d 83, 87 (Me. 1975) (“An agent is a fiduciary with respect to matters within the scope of his agency. No principle of law is better settled than that which requires the agent in all his dealings concerning the matter of his agency to act with utmost faith and loyalty and disclose all facts within his knowledge which bear materially upon his principal's interest.”).

⁶⁸ See *Laskowitz v. CIBA Vision Corp.*, 632 N.Y.S.2d 845 (2d Dep't 1995).

⁶⁹ 70 C.J.S. Physicians and Surgeons § 93.

patient's health, whether research or economic, that may effect his medical judgment.”⁷⁰ Thus, the informed consent doctrine is violated when an eye doctor prescribes OSI or Proclear lenses while failing to disclose the eye doctor’s economic interest in prescribing a lens for which retail competition from nonprescribing retailers is prohibited.

If an eye doctor uses interstate mail or phone or wire lines, then making prescriptions for contact lenses from which the eye doctors makes additional profits that are not disclosed to patients would appear to also constitute mail or wire fraud. The United States Supreme Court has held that it constituted mail and wire fraud for a reporter to trade on the stock advice he was giving in a news column because the reporter was profiting by using confidential business information he had a duty to safeguard while giving the pretense that he was loyal to his principal, the newspaper.⁷¹ It would likewise seem that using the mail or wires to profit from an agency relation without disclosing those profits would constitute mail or wire fraud. And a pattern of such activity would constitute a RICO violation.

OSI and Proclear are not themselves in a fiduciary relationship with patients and thus would not have the same duties. But to the extent their advertisements encourage doctors to commit such breaches of fiduciary duty, provide financial gain for doing so, and coach them about what statements to make to patients, they would be guilty of aiding and abetting the violations of the eye

⁷⁰ *Id.*

⁷¹ *Carpenter v. United States*, 484 U.S. 19, 27 (1987).

doctors.⁷²

General Problems of Asymmetric Information and Laws Against Deceptive Advertising.

Asymmetric information also plagues many markets even when buyers deal with businesses who are not their agents.⁷³ It is in part to deal with those problems that we have laws that prohibit all businesses from engaging in deceptive advertising. Otherwise, the inability of buyers to distinguish the truth-telling businesses from the deceptive ones would make them discount all their statements equivalently, and make it profitable for businesses to make deceptive statements to get business.

Under the FTC Act and similar consumer protection statutes, such deceptive advertising is defined broadly to go beyond merely making intentionally false statements. An advertisement is deceptive within the meaning of the FTC Act even if the words and sentences it contains are literally and technically true if the overall impression it creates is misleading.⁷⁴ In particular, telling less than the whole truth in an advertisement is a well known method of deception, and he who deceives by resorting to such methods cannot excuse the deception by relying upon the truthfulness of the partial truth by which the deception has been accomplished.⁷⁵ Further, advertisements are deemed illegally

⁷² “Aiding-abetting includes the following elements: (1) the party whom the defendant aids must perform a wrongful act that causes an injury; (2) the defendant must be generally aware of his role as part of an overall illegal or tortious activity at the time that he provides the assistance; (3) the defendant must knowingly and substantially assist the principal violation.” *Halberstam v. Welch*, 705 F.2d 472, 477 (D.C.Cir.1983); see also *In re Temporomandibular Joint (TMJ) Implants Prods. Liab. Litig.*, 113 F.3d 1484, 1495 (8th Cir.1997); *Hurley v. Atlantic City Police Dept.*, 174 F.3d 95, 127 (3d Cir.1999); CJS TORTS § 37; REST 2d TORTS § 876.

⁷³ See George Akerloff, *The Market for Lemons*, 84 Q. J. ECON. 588 (1970).

⁷⁴ *Koch v. Federal Trade Commission*, C.A.6 1953, 206 F.2d 311; *Kalwajtys v. Federal Trade Commission*, C.A.7 1956, 237 F.2d 654; *Bennett v. Federal Trade Commission*, C.A.D.C.1952, 200 F.2d 362; *Bockensteete v. Federal Trade Commission*, C.C.A.10 1943, 134 F.2d 369; *National Bakers Services, Inc. v. F.T.C.*, C.A.7(Ill.) 1964, 329 F.2d 365; *Sebrone Co. v. Federal Trade Commission*, C.C.A.7 1943, 135 F.2d 676.

⁷⁵ *P. Lorillard Co. v. Federal Trade Commission*, C.A.4 1950, 186 F.2d 52.

deceptive if they have a tendency to convey a misleading impression, even if an alternative nonmisleading impression might also be conveyed.⁷⁶ It is not necessary to show an intent to deceive, and the good faith of the advertiser is legally irrelevant.⁷⁷ Advertising is condemned if it has a tendency to deceive any appreciable or measurable segment of public,⁷⁸ and even if actual deception is unproven.⁷⁹

The advertisements by OSI and Proclear make safety claims, and encourage eye doctors to make safety claims, that are false and certainly deceptive within the meaning of the FTC Act. They repeatedly either state or insinuate that OSI and Proclear lenses are safer than rival lenses because their lenses are not available to nonprescribing retailers even though that proposition is inaccurate and unsupported by any evidence. Such false disparagement of rival products violates the FTC Act,⁸⁰ and deceives consumers into taking at face value prescriptions by eye doctors that are based on bogus safety claims.

Remedies for Agency and Informational Problems. The FTC has the general authority, and indeed the responsibility, to protect consumers from being misled by regulating how goods and

⁷⁶ Country Tweeds, Inc. v. F. T. C., C.A.2 (N.Y.) 1964, 326 F.2d 144; F.T.C. v. Pharmtech Research, Inc., D.C.D.C.1983, 576 F.Supp. 294.

⁷⁷ Warner-Lambert Co. v. F. T. C., C.A.D.C.1977, 562 F.2d 749; Chrysler Corp. v. F.T.C., C.A.D.C.1977, 561 F.2d 357; Beneficial Corp. v. F.T.C., C.A.3 1976, 542 F.2d 611; Montgomery Ward & Co. v. F. T. C., C.A.7 (Ill.) 1967, 379 F.2d 666; F. T. C. v. Sterling Drug, Inc., C.A.2 (N.Y.) 1963, 317 F.2d 669; Feil v. F.T.C., C.A.9 1960, 285 F.2d 879; Koch v. Federal Trade Commission, C.A.6 1953, 206 F.2d 311; Ford Motor Co. v. Federal Trade Commission, C.C.A. 6 1941, 120 F.2d 175; L & C Mayers Co v. F T C., C.C.A. 2 1938, 97 F.2d 365.

⁷⁸ Feil v. F.T.C., C.A.9 1960, 285 F.2d 879.

⁷⁹ Trans World Accounts, Inc. v. F. T. C., C.A.9 (Cal.) 1979, 594 F.2d 212; . Montgomery Ward & Co. v. F. T. C., C.A.7 (Ill.) 1967, 379 F.2d 666.

⁸⁰ E B Muller & Co v. F T C, C.C.A. 6 1944, 142 F.2d 511.

services are advertised and sold to individual purchasers.⁸¹ It can bring actions against such deceptive conduct, or issue rules to prophylactically prevent such conduct from occurring. Further, the Fairness to Contact Lens Consumers Act gives the FTC specific authority to bring such actions and issue such rules as are necessary to protect the right of patients to get their contact lens prescriptions filled by nonprescribing retailers. *See* 15 U.S.C §§ 7607-08. This right is clearly undermined when deceptive conduct, nondisclosure and breaches of fiduciary duty are used to distort which lenses are prescribed in favor of lenses that are not available through nonprescribing retailers without fully informing consumers about all the material facts. Enforcement by litigation or rules is particularly merited given that, when Congress enacted this legislation, it stressed its concern that eye doctors have “an inherent conflict of interest” when they “fill the contact lens prescriptions they write.” H.R. REP. 108-318. State attorneys general or other agencies likewise have similar authority to prevent deceptive advertising and breaches of fiduciary duties in their states. And Congress can of course legislate to clarify or add new provisions to the Fairness to Contact Lens Consumers Act.

Four sorts of remedies seem appropriate, whether adopted in adjudication, as new agency rules for future cases, or included in new statutory provisions.

1. *Prohibit Conflict-of-Interest Sales By Prescribing Eye Doctors.* One possibility for remedying these problems would be to prohibit eye doctors from selling the contact lenses that fill their own prescriptions, just as medical doctors are forbidden from selling drugs to fill their own

⁸¹ National Petroleum Refiners Ass'n v. F. T. C., C.A.D.C.1973, 482 F.2d 672.

drug prescriptions. *See* H.R. REP. 108-318. This would make sure that eye doctor prescriptions are not biased by the profits they make on the prescribed lenses.

2. *Prohibit Prescriptions from Specifying Manufacturers.* Another possibility would be to prohibit prescriptions that specify a particular manufacturer rather than just the lens characteristics indicated by the eye exam. While it may be that sometimes some patients do better with some lenses than others even though they have the same corrective characteristics, there is no particular reason why a prescription should limit a patient to one option. Alternatively, even if a prescription does mention a specific manufacturer, 15 U.S.C §7603 could be clarified or amended to make clear that prescriptions can be filled with contact lenses by different manufacturers that meet the same vision correction parameters indicated by the eye exam.

3. *Prohibit Restrictions Against Competition from Nonprescribing Retailers.* Another possibility would be to at least eliminate the most severe financial biases by issuing a rule that prohibits any restrictions on sales to and by nonprescribing retailers. This would be justifiable because of the inherent tendency of such restrictions to (a) distort prescriptions in favor of lenses having such restrictions and (b) bias the statements and disclosures that eye doctors make to their patients. Further, such a categorical rule would be much more administrable than case-by-case adjudication of whether prescription choices were distorted and of whether the statements that eye doctors made to each particular patient were accurate and fully disclosing.

At a minimum, the government could bar contact lens manufacturers that restrict sales to

nonprescribing retailers (like OSI and Proclear) from using advertisements that suggest to eye doctors that they should prescribe their lenses to stave off competition from nonprescribing retailers because of the inherent tendency of such advertisements to distort eye doctor prescriptions and statements. Such a rule would not ban the restrictions themselves, but would at least ban advertisements that seek to take advantage of such restrictions to distort eye doctor prescriptions.

4. Requiring Disclosure and Banning Certain Deceptions to Help Offset Informational Asymmetries. If the FTC and other government regulators do not implement such a categorical ban, then at a minimum they should bring litigation to penalize the nondisclosures and deceptive statements outlined above and should issue affirmative rules that would:

(a) bar any contact lens manufacturer, distributor, or eye doctor from stating or implying that lenses purchased from nonprescribing retailers are less safe;

(b) require every eye doctor who prescribes any lens that the manufacturer makes unavailable to nonprescribing retailers (such as OSI and Proclear) to disclose to patients: (a) the fact that these lenses, unlike other lenses, are not available from nonprescribing retailers, and any price disadvantage that might thus result; (b) the fact that this protection from retail competition gives the eye doctor financial incentives to prescribe that lens over lenses that are available from nonprescribing retailers; (c) any safety information that would cut in favor of another lens, such as any advantage in Dk that another lens might have; and (d) the fact that there is no increased safety risk to buying lenses from nonprescribing retailers. To minimize administrative problems and difficulties of proof in making sure disclosure is adequately made, this disclosure should take the form of a brief document written by the

FTC or other government agency that eye doctors are required to hand to their patients and explain. An eye doctor who prefers to prescribe lenses that are unavailable from nonprescribing retailers should be required to make this disclosure *before* the patient pays for his eye exam so that the patient is not locked in by the fact that he has already paid for a prescription for such a lens. Or, if the doctor makes the disclosure afterward, the eye doctor should be required to refund the eye exam fee if the patient decides to get another prescription after the disclosure. The disclosure statement required should advise patients of these rights; and

(c) require any contact lens manufacturer (such as OSI and Proclear) that restrains sales to nonprescribing retailers to make the same disclosures as set forth above for eye doctors both in their advertisements and on any packaging of contact lenses sold to consumers.

The disclosure option would be particularly attractive if the FTC and government regulator believed (contrary to the evidence) that doctor-only distribution might have some efficiency advantage because it makes sure patients receive desired services. Even if such an efficiency advantage did exist, full disclosure would further, rather than hinder, it because (by hypothesis) consumers would be willing to pay extra for the extra services they get.

Indeed, it is hard to see what legitimate objection manufacturers and eye doctors could possibly have to disclosing accurate information to patients. As OSI itself stressed in its submission to the FTC, “One of the best ways to protect consumers is to arm them with the knowledge to protect

themselves.”⁸² OSI also emphasizes the desirability of the disclosures it does make to consumers in their brochures about their doctor-only distribution policy.⁸³ Unfortunately, those brochures themselves are deceptive because (a) they falsely suggest that there is some additional health benefit to restricting purchases from prescribing retailers, and (b) they misleadingly omit the extra costs to consumers, the financial incentives this gives eye doctors to distort prescriptions, and information suggesting other lenses are safer. Further, the brochures come too late because, by the time the patient receives them, their eye doctor has already conducted the eye exam and prescribed the OSI lens. But OSI is correct on the general principle that it should be making full and accurate disclosure to patients, as should any eye doctor who prescribes its lenses.

COMPETITION PROBLEMS WITH THE AGREEMENTS PROHIBITING DISTRIBUTION BY NONPRESCRIBING RETAILERS

Traditional antitrust concerns are also raised by the restrictions on competition from nonprescribing retailers and by the advertising restrictions on competition among prescribing retailers too. Although OSI has claimed in some public statements that its distribution restraints are legal because they are unilateral, it is plain that these restraints reflect agreements among OSI, Proclear, their distributors, and eye doctors. Indeed, although the written contracts are vertical in form, the overall agreement is a horizontal one under standard antitrust doctrine.

⁸² OSI Comments by Langenfeld & Maness, *supra* note 21, at 17 (quoting former FTC Chairman Tim Muris, The Federal Trade Commission and the Future of U.S. Consumer Protection Policy," George Mason University School of Law, Law and Economics Working Paper Series, p. 2).

⁸³ *Id.* at 22-23.

Why the Restraint Can Properly Be Called Horizontal. The classic case is *Interstate Circuit*, which held that a horizontal agreement in restraint of trade could be inferred where the exhibitor entered into a series of vertical contracts with distributors that disadvantaged the exhibitor's rivals. The U.S. Supreme Court in that case reasoned:

“While the District Court's finding of an agreement of the distributors among themselves is supported by the evidence, we think that in the circumstances of this case such agreement for the imposition of the restrictions upon subsequent-run exhibitors was not a prerequisite to an unlawful conspiracy. It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it. Each distributor was advised that the others were asked to participate; each knew that cooperation was essential to successful operation of the plan. They knew that the plan, if carried out, would result in a restraint of commerce, which, we will presently point out, was unreasonable within the meaning of the Sherman Act, and knowing it, all participated in the plan. The evidence is persuasive that each distributor early became aware that the others had joined. With that knowledge they renewed the arrangement and carried it into effect for the two successive years.

“It is elementary that an unlawful conspiracy may be and often is formed without simultaneous action or agreement on the part of the conspirators. Acceptance by competitors, without previous agreement, of an invitation to participate in a plan, the necessary consequence of which, if carried out, is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the Sherman Act.”

Interstate Circuit, Inc. v. United States, 306 U.S. 208, 226-27 (1939).

The *Interstate Circuit* test of a horizontal agreement thus has four elements: (1) an invitation to common action; (2) the knowledge that rivals were likewise invited; (3) parallel acceptance of the invitation; and (4) the fact that joint action is necessary for the success of the plan, that is that the individual invitees would not want to accept the invitation alone. Where those four elements exist, a horizontal agreement can be inferred from a series of vertical contracts.

In this case, all these four elements are met and support the inference of a horizontal

agreement among participating eye doctors (a) to steer prescriptions away from contact lens sold by manufacturers that allow nonprescribing retailers to sell to consumers and (b) to refrain from advertising that competes for the contact lens business of consumers who got their eye exam at another eye doctor.

(1) There was an invitation to common action. As described in the facts above, OSI and Proclear have invited eye doctors to collectively steer prescriptions away from lenses that are available to nonprescribing retailers. They have done so through advertisements and public statements that explicitly state that eye doctors are collectively suffering from competition from nonprescribing retailers who sell by mail order and the internet, and that this retail competition can be defeated if eye doctors will prescribe OSI and Proclear lenses that those manufacturers commit to make unavailable to those nonprescribing retailers. OSI also made such an invitation at the 2001 CLAO annual meeting, where OSI stressed to eye doctors as a group that they were suffering because of competition from alternative distribution channels like 1-800 Contacts and told the group of eye doctors that the best way to protect themselves from such competition would be for them to agree to prescribe OSI brands that both OSI and eye doctors agreed would not be made available to nonprescribing retailers who tried to sell to someone other than their own patients, and not to advertise OSI lenses outside their offices nor to put prices on the advertisements put in their offices. OSI also made such an invitation in the letter it sent to every eye care professional indicating that, while the consent decrees prevented eye doctors from continuing their agreements with other manufacturers to preclude competition from nonprescribing retailers, eye doctors could achieve the same result by entering into the same agreement with OSI.

(2) Eye Doctors Knew Others Were Invited. It is also clear that eye doctors knew others were invited. OSI and Proclear's advertisements were made in magazines that targeted eye doctors and enjoy wide circulation among them. OSI even specifically made clear in its advertisement supplements that other eye doctors understood the threat that nonprescribing retailers posed to their business. The CLAO meeting was obviously conducted with each eye doctor knowing other eye doctors were present at the same time. And the mass mailing by OSI specifically indicated that it had been sent to every eye care professional.

(3) Parallel Acceptance of the Invitation. Clearly, many rival eye doctors have accepted this invitation by steering prescriptions to OSI and Proclear lenses in order to get the benefit of precluding competition from nonprescribing retailers, and by agreeing to refuse to resell to nonprescribing retailers and to restrain their advertising.

(4) Joint Action Was Necessary for Success. Joint action is also necessary for the success of this plan. If only a few eye doctors joined the scheme to steer prescriptions to lens that are unavailable from nonprescribing retailers and to refrain from advertising against other prescribing retailers, then they would risk losing business to other eye doctors who do not impose the same anticompetitive constraints on consumer choice by colluding with contacts makers. Further, if some of the eye doctors who do join the scheme resell the lenses to nonprescribing retailers, then the entire scheme will unravel. Instead, the success of the scheme depends (a) on participating eye doctors collectively deciding not to resell the lenses to nonprescribing retailers and (b) on enough eye doctors collectively deciding to steer prescriptions to OSI and Proclear lenses that impose such

restrictions. It is only through such collective action that they can prevent retail competition in contacts sales to their customers. This element is also confirmed by the fact that the agreements here were explicitly designed to replace a prior horizontal agreement among eye doctors that was the target of the prior consent decrees, a horizontal agreement which presumably was made because of this motive for common action.

Factually, the cases are quite similar too. In *Interstate Circuit*, a horizontal agreement was inferred where the exhibitor entered into a series of contracts with distributors that disadvantaged the exhibitor's rivals at retail. Likewise, here OSI and Proclear have entered into a series of contracts with the eye doctors that disadvantage the eye doctors' rivals at retail. This case also resembles *Klor's*, where a horizontal boycott of suppliers organized by a retailer was inferred from series of vertical contracts that the retailer entered into with those suppliers. See *Klor's v. Broadway-Hale Stores*, 359 U.S. 207 (1959). Indeed, here the case is stronger because those cases did not have the plus factor that the agreements at issue were designed to replace a prior horizontal agreement among eye doctors that had been ended by a consent decree.

Classifying the agreements here as horizontal rather than vertical is also justified by underlying economic theory. The reasons for generally treating vertical restraints more leniently than horizontal restraints are (1) that manufacturers generally have a financial interest to minimize (rather than increase) the retail markup and (2) that vertical restraints on distribution are more likely to have procompetitive justifications. Neither reason applies here.

The first reason does not apply where, as here, the manufacturer operates as a cartel ringmaster, who through a series of vertical contracts organizes a horizontal cartel among downstream firms in exchange for a share of their supracompetitive profits.⁸⁴ Here, eye doctors can enjoy supracompetitive profits in the sale of contact lenses if they collectively prevent nonprescribing retailers from getting access to those lenses by agreeing to refuse to resell lenses to such nonprescribing retailers and to steer prescriptions away from lenses whose manufacturers sell to nonprescribing retailers. But if eye doctors directly entered into such an agreement amongst themselves, it would be a blatant horizontal agreement easily and quickly condemned by severe antitrust sanctions. An enterprising contact lens manufacturer can thus gain the business of such doctors by agreeing to organize a cartel for them with a series of vertical agreements that impose the same terms, reaping a share of their supracompetitive profits with some combination of higher wholesale prices and/or increased prescriptions that its product would not otherwise merit. Indeed, the ability to be able to strike an agreement between sellers and buyers that enhances the other's market power in exchange for a share of the resulting supracompetitive profits is just one special application of the general Coase Theorem.⁸⁵

In short, the first reason does not apply because it is in the financial interest of OSI and Proclear to help eye doctors create supracompetitive profits that can then be shared among them. OSI and Proclear are effectively agreeing to help the eye doctors exact supracompetitive profits in

⁸⁴ See generally Thomas G. Krattenmaker & Stephen C. Salop, *Anticompetitive Exclusion: Raising Rivals' Costs to Achieve Power Over Price*, 96 YALE L.J. 209, 238-40 (1986); Elizabeth Granitz & Benjamin Klein, *Monopolization by Raising Rivals' Costs: The Standard Oil Case*, 39 J.L. & ECON. 1 (1996); Hovenkamp, *Mergers & Buyers*, 77 VA. L. REV. 1369 (1991); IV AREEDA, HOVENKAMP & SOLOW, ANTITRUST LAW ¶943b, 204-06 & n.4 (1998).

⁸⁵ See IV AREEDA, HOVENKAMP & SOLOW, ANTITRUST LAW ¶943b, at 204-06 & n.4 (1998).; XI HOVENKAMP, ANTITRUST LAW 95 & n.27, 100 & n.44 (1998).

the market for retailing contacts in return for the eye doctors agreeing to increase their market share. OSI and Proclear do not benefit from the increased retail markup this arrangement produces, which standing alone would either reduce its wholesale price or reduces overall market output and sales. But OSI and Proclear do benefit from the fact that, in exchange for this anticompetitive boon, the eye doctors give them a competitive advantage over their rivals by preferring OSI and Proclear in prescriptions that their rivals now cannot fill.

One might wonder why rival manufacturers would not try to undermine such a scheme by selling at a lower retail markup that they advertise to consumers and thus attract consumers away from firms that do use restricted distribution through eye doctors. The reason they do not, as the evidence in the consent decree litigation indicated, is that all the contact lens manufacturers are too dependent on eye doctors for business because it is the eye doctors who really make the purchase decisions for their patients.⁸⁶ Thus, no contact lens manufacturer can afford to anger eye doctors by undercutting them, for the way to gain business is to compete for the eye doctors who really make the consumption decisions by offering eye doctors the highest profits, not by offering patients the lowest prices. Nor, unlike in other industries, can manufacturers sidestep uncompetitive retailers by simply creating their own new retailers, for licensing laws prohibit anyone other than eye doctors from prescribing contact lenses. Accordingly, before the consent decrees prohibited the three leading manufacturers from restricting sales to nonprescribing retailers, every manufacturer was driven to adopt the same sorts of restrictions because it was individually profitable to do so, even though the total effect may well have been to reduce industry output. Even now, manufacturers

⁸⁶ See Douglas Greer, *Liability Report of on Behalf of The Thirty-One Plaintiff States*, at 51-55, In re Disposable Contact Lens Antitrust Litigation, 94 MDL 1030-J-20A (February 13, 1999).

subject to the consent decrees are reluctant to promote distribution through nonprescribing retailers for fear of upsetting the eye doctors on whom they depend for prescriptions. And, if OSI and Proclear are permitted to engage in these sorts of agreements, the other manufacturers will likely try to reinstate such agreements when their consent decrees expire.

The second reason does not apply where, as here, the ordinary procompetitive justifications offered for such distributional restraints do not apply. Normally, such restraints are justified on the ground that increasing the retailer's profit margin allows them to provide additional advertising or services that otherwise could not be sustained because of free rider problems. But those justifications are plainly inapplicable here for reasons that have already been addressed at length before but can be summarized here. The restraints cannot be justified by a desire to increase advertising because in fact the restraints specifically restrict such advertising. Nor can the restraints be justified as needed to get doctors to provide other services, for in fact eye doctors already charge a separate fee for their eye exams, and provide no additional services when they sell lenses that restrict sales by nonprescribing retailers, let alone services on which consumers can somehow free ride by buying the lenses elsewhere.⁸⁷ Instead, the plain articulated purpose of the restraint was the anticompetitive one of preventing nonprescribing retailers from driving down the prices consumers paid. This has also been the plain effect given the evidence that nonprescribing retailers charge substantially lower prices, that OSI and Proclear charge much lower prices in Europe where such restrictions are not allowed, and Proclear and prescribing retailers charge much less for brands that

⁸⁷ For example, if (contrary to the evidence) eye doctors did provide additional services on OSI and Proclear lenses like refitting each new set of replacement lenses that would not be a service consumers could get by shopping at the eye doctor and then buying from nonprescribing retailers and thus would not be subject to free riding problems.

face competition from nonprescribing retailers. The only “service” that OSI and Proclear could be purchasing was the anticompetitive one of getting eye doctors to distort prescriptions to favor their lenses.

Why the Restraints Violate Antitrust Law Even If Vertical. Even if the agreements here were classified as vertical, these same sort of considerations should lead the agreements to be condemned under the rule of reason. Plainly, here there are, at a minimum, vertical agreements between OSI and eye doctors that, if the eye doctors will prescribe OSI and Proclear contact lens, OSI and Proclear will not compete with the eye doctors at retail by supplying nonprescribing retailers with those lenses, and will secure agreements from each prescribing eye doctor that they will neither resell their lenses to nonprescribing retailers nor engage in price advertising or any advertising outside their office of such lenses. Such agreements are judged under the rule of reason. And the rule of reason condemns any restraint that lacks any procompetitive justification as a naked restraint without requiring any proof of market power or actual anticompetitive effects.⁸⁸ Further, this line of authority excludes from consideration any claimed justification that suppressing

⁸⁸ See *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 459 (1986) (“Absent some countervailing procompetitive virtue--such as, for example, the creation of efficiencies in the operation of a market or the provision of goods and services ... an agreement limiting consumer choice by impeding the ‘ordinary give and take of the market place,’ cannot be sustained under the Rule of Reason.”); *NCAA v. Bd. of Regents*, 468 U.S. 85, 109-110 (1984); *National Society of Professional Engineers v. United States*, 435 U.S. 679, 693-95 (1978). This line of authority was not overruled in *California Dental Association v. FTC*, 119 S. Ct. 1604 (1999), which instead simply held that the naked restraint doctrine could not be applied where the defendant *had* articulated a plausible procompetitive justification. See *id.* at 1613-16. See also *id.* at 1617-18 (“The point is not that the CDA’s restrictions necessarily have the procompetitive effect claimed . . . The point, rather, is that the plausibility of competing claims about the effects of the professional advertising restrictions rules out the indulgently abbreviated review to which the Commission’s order was treated.”) Nor is *NYNEX v. Discon*, 525 U.S. 128 (1998), to the contrary. That case held that a vertical agreement to deal with one firm did not fall within the *per se* rule against boycotts just because it had no procompetitive justification. *Id.* at 130, 135-37. But it did not purport to overturn the traditional doctrine under the rule of reason that some procompetitive justification must be articulated, nor to address agreements other than a refusal to deal with a single firm, but to the contrary stressed that its holding was limited to such cases and justified by the special concerns a *per se* rule would raise in such cases. *Id.*

competition is desirable because it increases safety.⁸⁹ And even if such a justification were admissible it would be contrary to fact because the restraints actually increase health risks and distort medical advice.

Even if one did conclude that a sufficiently plausible procompetitive justification had been demonstrated to require some proof of anticompetitive effects, those effects can be found here. Direct proof of such anticompetitive effects exist because the scheme has in fact restricted the availability of OSI and Proclear lenses to nonprescribing retailers, notwithstanding some gray market sales created by marginal cheating on the anticompetitive agreement. Further, the evidence noted above indicates an increase in prices for these lenses because of this agreement. Where such direct proof of anticompetitive effects exist, market power need not be proven.⁹⁰

Even if one thought that proof of market power were required, such market power should not be equated with the market shares that OSI and Proclear have in the contact lens market in general. For in reality the relevant market, if one views the restraints as vertical, is the market for retailing contact lenses to patients who have already received a prescription for a particular manufacturer's lens. Once an eye doctor has prescribed lenses from that manufacturer, the patient

⁸⁹ See *Professional Eng'rs*, 435 U.S. at 681 (professional association liable for ethical canon even though its "purpose" was to protect "public safety"); *Indiana Dentists*, 476 U.S. at 462-63 (professional association liable even though their purpose was "legal, moral, and ethical policy of quality dental care"); see also *NCAA*, 468 U.S. at 101 n.23 ("good motives will not validate an otherwise anticompetitive practice"); *FTC v. Superior Court Trial Lawyers Ass'n*, 493 U.S. 411, 421-24, 427 & n.11 (1990) (Sherman Act provides no "immunity from prosecution on the basis of their good intent").

⁹⁰ "Since the purpose of the inquiries into market definition and market power is to determine whether an arrangement has the potential for genuine adverse effects on competition, 'proof of actual detrimental effects, such as a reduction of output,' can obviate the need for an inquiry into market power, which is but a 'surrogate for detrimental effects.'" *Indiana Dentists*, 476 U.S. at 460-61 (quoting VII AREEDA, ANTITRUST LAW ¶ 1511, at 429 (1986)).

cannot get that prescription filled with a lens by any other manufacturer. True, the patient could get a new eye exam, but that is expensive both because of the financial outlay and because the time costs of scheduling and going to another appointment are high. As a practical matter, the barrier to switching to another lens is accordingly too high after a prescription has been written. Thus, the foreclosure of the market for filling the prescriptions that have actually been made is effectively 100% both at wholesale and retail. The eye doctors in effect give OSI and Proclear a legal monopoly over wholesale supply by prescribing their lenses in exchange for OSI and Proclear agreeing to give the eye doctor an effective monopoly over retail sales of the only lenses allowed to fill that prescription.

One might expect that OSI and Proclear would argue that eye doctors cannot enjoy any such local market power because they must compete with other eye doctors to get new patients. But the more one believes that, the more it confirms that there is a motive for common action that suggests a horizontal conspiracy. Moreover, the Supreme Court decision in *Kodak* indicates that eye doctors can have market power in a market for filling their own prescriptions even if eye doctors have no market power in market for making prescriptions.⁹¹ Once the patient gets the prescription, they are locked-in by the financial and time costs of having to get another eye exam at another eye doctor. And the information costs of selecting only eye doctors who do not engage in this practice are too high. Thus, the same sort of lock-in effects and information cost barriers that *Kodak* held could suffice to prove market power also can be shown here.

⁹¹ See *Eastman Kodak Co. v. Image Technical Services, Inc.*, 504 U.S. 451 (1992).

Further, the existence of this sort of localized market power is consistent with evidence that eye doctors do price discriminate against their patients.⁹² For example, when customers respond to high eye doctor prices by putting in orders at 1-800-CONTACTS, eye doctors routinely cut their prices to match 1-800-CONTACTS prices.⁹³ This indicates lower pricing to the most price sensitive customers, and thus higher prices to other customers, which shows that eye doctors are not pricing at marginal costs, which would be the same for both sets of customers. Market power is further indicated by evidence that eye doctors have expended resources lobbying for legal restrictions on nonprescribing retailers, and have been willing to distort the prescriptions they make and statements they utter to patients in order to more fully exploit that power. One might think that the supracompetitive profits eye doctors can earn from this local market power would simply cause them to cut eye exam fees to attract these patients and in the long run offset the supracompetitive profits earned from lenses. But in fact this does not occur, most likely because 70% of optical patients have insurance coverage for their eye exams, and because licensing laws restrict the number of eye doctors in every state and give them a legal monopoly on making prescriptions.

Alternatively, if one did think the agreements were only vertical, one might wonder why some enterprising eye care provider does not try to gain market share by advertising that it is willing to prescribe lenses that are cheaply available from nonprescribing retailers. One reason is probably that the capacity to conduct eye exams is limited by the number of eye doctors the eye care provider has. An eye care firm cannot simply create more eye doctors because the number of licensed eye

⁹² For authorities stating that price discrimination indicates market power, see sources cited *supra* note 24.

⁹³ See Appendix P (Responses to Prescription Verification Requests); Appendix Q (For Eyes Memo to All Technicians, Drs, and Managers (March 24, 2003)); Appendix D at 68.

doctors is limited by licensing laws. Nor can an eye care firm attract more eye doctors by offering to pay them less than the supracompetitive profits they already earn by restricting rival competition in contact lens sales. The opportunities for expansion by avoiding such anticompetitive behavior are thus limited.

Another reason is that where some consumers are informed and others are not, then economic models show that supracompetitive prices will often be charged to the uninformed consumers even in markets with many retailers. (1) Some economic models show that, where retailers can price discriminate, it can be profit maximizing for each retailer to charge supracompetitive prices to the uninformed buyers and low prices to the informed ones.⁹⁴ (2) Other economic models show that, where retailers cannot price discriminate, and uninformed buyers choose retail stores at random but informed buyers do not, it can be a profit-maximizing for some retailers to charge supracompetitive prices and others to charge low prices.⁹⁵ Both may be going on here, with some eye doctors price discriminating among their patients, as noted above, and others choosing to be high-priced OSI or Proclear retailers to get a random proportion of uninformed buyers. Indeed, part of the motive for the restraints at issue here may be precisely to protect the ability of prescribing retailers to price discriminate and thus maximize their ability to profit from local market power and share those benefits with OSI and Proclear.

⁹⁴ See Aaron S. Edlin, *Do Guaranteed-Low-Price Policies Guarantee High Prices, and Can Antitrust Rise to the Challenge?*, 111 HARV. L. REV. 528, 529-31, 536-52, 573-75 (1997).

⁹⁵ See Steven Salop & Joseph Stiglitz, *Bargains and Ripoffs: A Model of Monopolistically Competitive Price Dispersion*, 44 REV. ECON. STUD. 493, 494, 502-07 (1977).

Finally, problems of asymmetric information may create a market for lemons.⁹⁶ Suppose that some eye doctors do loyally prescribe the best and cheapest contact lenses for their patients, but that other eye doctors instead prescribe the lenses that only they can sell and that thus make them the most money. Suppose further that patients are not sufficiently informed about which are the best and cheapest lenses, and thus have a hard time distinguishing one type of eye doctor from the other. If so, then patients will simply discount the value of all eye doctors by the average agency cost associated with using them, and thus will lower the prices they are willing to pay all eye doctors for their services. The eye doctor who is more loyal to their patients than average will make less money than the one who diverges from his patients' interests, and so the former will shrink or drop out of the market, and the latter will grow or gain converts from the former, until in the end the market is completely occupied by the latter sort of eye doctors. True, the more loyal eye doctors might try to overcome this informational asymmetry by advertising their greater loyalty to patients. But patients will have a hard time knowing whether to believe their advertisements over the advertisements of other eye doctors who claim that restricting sales by nonprescribing retailers is better for patients. The information costs of sorting out such a complicated issue well enough to know which advertisements to believe may not be worth the benefits of doing so, in which case patients will never incur those information costs, and the informational asymmetry will persist.

* * *

However we characterize the restraint, for the set of customers who receive prescriptions for OSI and Proclear lenses, the agreements at issue here create precisely the sort of regime that was

⁹⁶ See George Akerloff, *The Market for Lemons*, 84 Q. J. ECON. 588 (1970).

meant to be eradicated by the Fairness to Contact Lens Consumers Act, prior FTC litigation and rulemaking, and the consent decrees obtained by the State Attorneys General. In enacting that statute, Congress already considered and rejected the very same claims that there were justifications for restricting sales by nonprescribing retailers that offset their adverse effects. In its prior litigation and rulemaking, the FTC likewise considered and rejected the very same sort of claims that the justifications for such restrictions offset their anticompetitive effects. And in the prior contact lens litigation, the State Attorneys General likewise considered the very same arguments and found no reason to think there were procompetitive justifications that offset the anticompetitive effects. The alleged justifications and adverse effects are precisely the same here, and there is no reason to draw a different conclusion about them just because the restrictions were implemented through different means.

Thus, the FTC (or similarly situated state agencies) should either bring litigation against the agreements restricting distribution by nonprescribing retailers and advertising among prescribing retailers, or simply adopt a rule that bans such agreements. Such action would be justified by traditional antitrust principles for the reasons detailed above. Indeed, under the FTC Act such action would be justified even if the conduct were considered unilateral because FTC Act §5 does not require proof of an agreement.

Alternatively, the FTC could simply rely on the fact that the right to obtain lenses from nonprescribing retailers, which the Fairness to Contact Lens Consumers Act meant to give consumers, is rendered completely ineffective if eye doctors can prescribe a manufacturer brand that

nonprescribing retailers are barred from obtaining. After all, the Congress that promulgated that Act specifically stressed that: “The consumer's right to a copy of their contact lens prescription means nothing unless consumers can fill that prescription at the business of their choice.” H.R. REP. 108-318. That is precisely what the agreements at issue prevent consumers from doing. And Congress wanted the statute to end practices that “limited the consumer's ability to shop for the best price,” *id.*, which is again precisely what the practices here do. The statute and legislative history thus justify FTC litigation or rulemaking under that Act to carry out its purposes by penalizing or prohibiting such restrictions on distribution to nonprescribing retailers. *See* 15 U.S.C §§ 7607-08.

