05-7010-cv

IN THE

United States Court of Appeals

FOR THE SECOND CIRCUIT

BRUCE CHAPMAN and HANDLE WITH CARE BEHAVIOR MANAGEMENT SYSTEM, INC.,

Plaintiffs-Appellants,

- against -

NEW YORK STATE DIVISION FOR YOUTH, NEW YORK STATE OFFICE OF CHILDREN & FAMILY SERVICES, NEW YORK STATE DEPARTMENT OF SOCIAL SERVICES, JOHN JOHNSON, Commissioner of New York State Office of Children and Family Services and former Commissioner of the New York State Division for Youth, in his official and individual capacity, MARGARET DAVIS, former Director of Training for the New York State Division for Youth, and former Director of Training for New York State Office of Children and Family Services, in her official and individual capacity, PATSY MURRAY, former Associate Training Technician for the New York State Division for Youth,

(Caption Continued on Inside Cover)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF NEW YORK

PETITION FOR PANEL REHEARING
PETITION FOR REHEARING *EN BANC*

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and current position as Trainer for New York State Office of Children and Family Services, in her official and individual capacity, CORNELL UNIVERSITY, JEFFREY LEHMAN, President of Cornell University, in his official and individual capacity, DOCTOR HUNTER RAWLINGS, III, former President of Cornell University, in his official and individual capacity, NEW YORK STATE COLLEGE OF HUMAN ECOLOGY, FAMILY LIFE DEVELOPMENT CENTER, RESIDENTIAL CHILD CARE PROJECT, THERAPEUTIC CRISIS INTERVENTION, MARTHA HOLDEN, Project Director of the Residential Child Care Project and Therapeutic Crisis Intervention Trainer and Coordinator, in her official and individual capacity, MICHAEL NUNNO, Project Director of the Residential Child Care Project and Therapeutic Crisis Intervention Trainer and Coordinator, in his official and individual capacity, HILLSIDE CHILDREN'S CENTER, DENNIS RICHARDSON, President and CEO of Hillside Children's Center, in his official and individual capacity, DOUGLAS BIDLEMAN, employee of Hillside Children's Center and Therapeutic Crisis Intervention Trainer, in his official and individual capacity,

Defendants-Appellees.

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

BRUCE CHAPMAN, *et al.*,

Plaintiffs-Appellants

-against-

NEW YORK STATE DIVISION FOR YOUTH, *et al.*,

Defendants-Appellees

Docket No.: 05-7010

CORPORATE DISCLOSURE STATEMENT UNDER RULE 26.1

Pursuant to Fed. R. App. P. Rule 26.1, the undersigned counsel of record for Plaintiff-Appellant Handle With Care Behavior Management System, Inc. submits this statement identifying all of its parent corporations and listing any publicly held company that owns 10% or more of its stock.

Parent Companies: None

Publicly Held Companies Owning 10% or More of Handle With Care Behavior Management System, Inc.'s Stock: None

Dated: New York, NY
December 2, 2008

Respectfully Submitted,
GUY L. HEINEMANN, P.C.

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STATEMENT PURSUANT TO FED. R. APP. PRO. 35(b)(1)(A)

The Panel Decision (sometimes "Decision") conflicts with decisions of the Supreme Court and this Court, and consideration by the full Court is therefore necessary to secure and maintain uniformity of its decisions.

In particular, the Decision conflicts with *FTC v. Indiana Federation of Dentists*, 476 U.S. 447 (1986); *National Society of Professional Engineers v. United States*, 435 U.S. 679 (1978); *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377 (1956); *Freedom Holdings, Inc. v Spitzer*, 357 F.3d 205 (2d Cir. 2004); *PepsiCo, Inc. v. Coca-Cola Co.*, 315 F.3d 101 (2d Cir. 2002); *Todd v. Exxon Corp.*, 275 F.3d 191 (2d Cir. 2001), in that when a plaintiff pleads direct evidence of anticompetitive effects, a flawless relevant market is not crucial to pleading Sherman Act claims.

The Decision also conflicts with *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207 (1959) and *Freedom Holdings*, *supra*, in its rejection of *per se* liability for the collective refusal to deal imposed on the horizontal array of over 80 private entities.

The Decisions' affirmance of a dismissal with prejudice of a *first* Complaint, without granting leave to amend, also conflicts with *Discon, Inc. v. Nynex Corp.*, 93 F.3d 1055 (2d Cir. 1996), *rev'd on other grounds*, *Nynex Corp. v. Discon, Inc.*, 525

U.S. 128 (1998) and *Freedom Holdings*, *supra*.

PRELIMINARY STATEMENT

Plaintiff-Appellant Handle With Care Behavior Management System, Inc. ("HWC") petitions for Panel Rehearing and Rehearing En Banc so this Court may review the Decision that affirmed the dismissal with prejudice of antitrust claims in HWC's *only* Complaint, notwithstanding HWC's factually specific allegations of collective conduct constituting, *inter alia*, "monopoly control" and "systematic[ ] refus[al]" to allow other competition (C ¶¶ 34, 86, 88-90).[1] The Complaint even recited direct evidence of anticompetitive effects from Defendants' conduct on the numerous private foster care agencies in New York, including prices *more than four times* charged other customers (C ¶¶ 40, 91-92, 97). The Decision's affirming the dismissal without leave to amend also conflicts with precedents of this Court that command liberality in granting leave to amend -- *especially* in complex antitrust cases. Finally, the Panel also misapprehended the relevant market asserted by HWC.

BACKGROUND

HWC is a provider of restraint training to public and private agencies in New York State and elsewhere. HWC alleged collective conduct by Defendants Cornell

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[1] The Complaint ("C") is located at A-25 through A-45 of the Appendix. The District Court's opinion is reported at 2005 WL 2407548 and is reproduced at A-296 - A-315 of the Appendix. The Panel Decision (annexed hereto) is also reported at 2008 WL 4558047.

University ("Cornell"), The New York State College of Human Ecology ("CHE") and a state agency now known as the New York State Office of Children and Family Services ("OCFS"). Defendants' collective conduct, persisting over twelve years, consisted of an agreement under which OCFS refused regulatory approval of the restraint policies of the more than 80 privately-owned and autonomous foster care agencies ("PFAs")[2] throughout New York State -- *unless* the PFAs contracted with Cornell and CHE to use their "Therapeutic Crisis Intervention" ("TCI") program to provide restraint training to PFA staff (C ¶¶ 35, 87, 90; A-48, A-95-A-102, A-124-A-136). This coercive policy was inconsistent with OCFS regulations governing the PFAs, which are responsible for their own management, including restraint training.[3]

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[2] This number is estimated from "New York State Office of Children and Family Services Standards of Payment System for Foster Care of Children," available at http://www.ocfs.state.ny.us/main/rates/fostercare/rates/fc-voluntary07-07.pdf. PFAs are the principal institutions in New York State that take in foster children, with thousands of New York children in their care. The Complaint used various terms to describe the PFAs, such as "child care providers" (¶ 23) and "private child care providers" (¶ 31), but they are defined as "voluntary authorized agencies." N.Y. Soc. Serv. Law §§ 371(10)(a) and (c). For simplicity, as in HWC's briefs, they are hereinafter referred to as "PFAs."

[3] This autonomy is manifest from N.Y. Soc. Serv. Law § 460-a and 18 N.Y.C.R.R. §§ 441.3, 482.3. The "board of directors" of a PFA "shall manage the affairs of such agency (18 N.Y.C.R.R. § 441.3(a)(l)), "assur[ing] the proper care of children for whom such agency is responsible." 18 N.Y.C.R.R. § 441.3(a)(4)(iii). The PFAs' "chief executive officer" ("CEO") is responsible to the board for the administration of the PFA, 18 N.Y.C.R.R. § 441.3(a)(4)(i), including the responsibility to "direct, evaluate and coordinate all aspects of [a PFA's restraint training] program," including "staff development *and training*." 18 N.Y.C.R.R. § 441.3(c)(l) (emphasis added). PFAs must submit their restraint policies to OCFS for approval (C ¶¶ 82-84). 18 N.Y.C.R.R. § 441.17. *See also* HWC's Principal Brief ("PrBr") at 10-12.

Defendants have not presented the slightest *pretense* of some putative goal of efficiency, quality or any *legitimate* interest in imposing the expensive TCI program on the PFAs.[4] Various tactics employed to enforce this exclusion included threats of adverse regulatory and licensing actions (C ¶¶ 70-74, 88-90).[5] Defendants did not deny that this was manifestly anticompetitive behavior, conceding below that the Complaint "may be broadly and liberally construed to alleged [sic] anticompetitive conduct," and acknowledging that a dismissal without leave to amend is appropriate only "in *extraordinary* circumstances" (Docket No. 51 at 10, 15; emphasis added). HWC alleged both injury to competition[6] and its own antitrust injury.

This exclusion also allowed Cornell and CHE to charge more than *four times* the price charged other (*i.e.*, non-OCFS-regulated) customers.[7] OCFS, Cornell and

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[4] In addition to price competition, quality competition was also suppressed. *E.g.*, portions of the record indicate that HWC's program is preferred over TCI (A-174 - A-176, A-227 - A-230, A-252 - A-257; PrBr at 35 n.3).

[5] OCFS also approves PFA corporate charters. N.Y. Soc. Serv. Law § 460-a; 18 N.Y.C.R.R. §§ 441.17(c), 477.1, 477.4. *See also* C ¶¶ 82, 89; PrBr at 10-15; HWC's Reply Brief ("RepBr") at 5-6, 51-54.

[6] HWC asserted that other vendors have also been excluded (C ¶¶ 38, 70, 73, 89; PrBr at 13-15, 19-20). *See also* District Court opinion at A-302 - A-303, A-306.

[7] Defendants did not put forward any justification for this supracompetitive pricing. PrBr at 13, 15, 34. Defendants did submit a 1994 "Memorandum of Agreement" ("MOA") between Cornell and OCFS, of which the most explicit goal was to help *maximize* federal funding for the Defendants' sale of TCI (C ¶¶ 91-91; A-141; RepBr at 7-10, 19). Defendants contented that the MOA cloaked their behavior in state action immunity from antitrust laws, but the MOA was null and void because it was not approved by the State Comptroller pursuant to N.Y. Fin. Law § 112. This was determined by the State Attorney General on September 14, 2005 (shortly before the

CHE all benefitted financially from these supracompetitive prices because federal reimbursement covers 75% of the (legitimate) cost of this training (C ¶¶ 92, 96-97; PrBr at 15 n.9, 31; RepBr at 15 n.15, 29, 37 n.32). Hence, instead of seeking competitive prices, OCFS had a strong incentive to *favor* the high prices for TCI and the exclusion of other vendors because OCFS is repaid most of the "cost" of Cornell's overpriced TCI training under Title IV-E of the Social Security Act (C ¶¶ 14, 35; PrBr at 30-32; Rep.Br. at 15, 29, 37 n.32).[8]

HWC had only one chance to plead its antitrust claims, as the District Court dismissed them with prejudice and the Panel affirmed.[9] The Panel Decision did not review HWC's allegations of *per se* liability nor, *per se* liability aside, HWC's allegation that the supracompetitive pricing and exclusion of competition had an "actual anticompetitive effect" (PrBr at 36). The Decision simply held that HWC had failed to allege a "properly defined" relevant market, which it found fatal *to all* of HWC's antitrust claims.

District Court's dismissal, but without any Defense counsel bringing it to the District Court's attention). Formal Opinion 2005-F2, 2005 WL 2332807 (N.Y.A.G.). *See* RepBr at 7-10.

[8] Cornell and CHE have also benefitted financially from this arrangement, but illegally so (C ¶¶ 14, 35; PrBr at 30-32). *I.e.*, OCFS has fraudulently overbilled the federal government for these "costs." *See* Amended Complaint in *United States of America ex rel. Chapman v. Cornell University, et al.*, 1:04-CV-1505 (N.D.N.Y. 2005), brought under the *qui tam* provisions of the False Claims Act, 31 U.S.C.A. §§ 3729 *et seq.* at ¶¶ 98-102, 122.

[9] The Panel consisted of Circuit Judges Straub, Walker and Pooler.

ARGUMENT

The Panel Decision places beyond the reach of the Sherman Act collective conduct by three entities that forced the selection of Cornell and CHE as the vendor of restraint training for the over 80 PFAs, each independently responsible for the safety of children in their care. The Decision conflicts with decisions of the Supreme Court and this Court in that the Complaint demonstrated direct evidence of anticompetitive effects sufficient to sustain violations of *both* Sections One and Two -- even without a relevant market analysis.

Moreover, the dismissal with prejudice of HWC's first -- and only -- Complaint conflicts with decisions of this Court requiring liberality in granting leave to amend under Fed. R. Civ. Pro. 15(a)(2). If adhered to, the decision would essentially transform 12(b)(6) reviews of antitrust complaints into summary judgments.

POINT I

THE PANEL DECISION WRONGLY CONCLUDED THAT HWC'S ANTITRUST CLAIMS WERE DEPENDENT ON FLAWLESSLY PLEADING A RELEVANT MARKET

HWC's Complaint clearly described the anticompetitive nature of the Defendants' misconduct, including that Defendants had "monopoly control," had "systematically refus[ed]" to allow PFAs to hire vendors other than Cornell and CHE (C ¶¶ 34, 86, 88-90), and had actually caused supracompetitive pricing (C ¶¶ 40, 90-

92, 97). These kinds of factual allegations at the pleading stage obviate any exposition of the effect on a relevant market. As a leading scholar has explained, "Market definition is *not a jurisdictional prerequisite*, or an issue having its own significance under the statute; it is *merely an aid* for determining whether power exists." L. Sullivan, *Handbook of Antitrust Law* 41 (1977) (emphasis added).

A. Section One Liability

As this Court held in *Todd v. Exxon Corp.*, 275 F.3d 191, 206 (2d Cir. 2001), "[i]n this Circuit, a threshold showing of market share is not a prerequisite for bringing a § 1 claim . . .." Quoting *K.M.B. Warehouse Distributors, Inc. v. Walker Mfg. Co.*, 61 F.3d 123, 129 (2d Cir. 1995), *Todd* further explained, "[i]f a plaintiff can show an *actual adverse effect on competition* . . . we do not require a further showing of market power." 275 F.3d at 206-07 (emphasis added). Relying on *Capital Imaging Assocs. v. Mohawk Valley Med. Assocs.*, 996 F.2d 537, 546 (2d Cir. 1993), *Todd* also held that an antitrust plaintiff "may *avoid* a 'detailed market analysis' by offering 'proof of actual detrimental effects . . ..'" 275 F.3d at 207 (quoting *FTC v. Indiana Federation of Dentists*, 476 U.S. 447, 460-61 (1986); emphasis added).

Within the four corners of HWC's Complaint, very specific -- and "actual" -- adverse effects on competition were pleaded: supracompetitive prices and the horizontal exclusion of vendors competing to provide restraint training to the over 80

PFAs in New York State. *Either* sustains the Section One claims under the Rule of Reason. *See, e.g., FTC v. Indiana Federation of Dentists, supra* (horizontal agreement to withhold particular services from customers); *National Society of Professional Engineers v. United States*, 435 U.S. 679, 692 (1978) (horizontal agreement to refuse to negotiate prices).

Moreover, the fact that OCFS, with Cornell and CHE, *imposed* the horizontal exclusion of all other vendors is of no importance. *324 Liquor Corp. v. Duffy*, 479 U.S. 335, 345-46 n.8 (1987) (holding Section One claims made out by state action compelling private parties to engage in anticompetitive behavior, calling this a "hybrid" restraint). *Accord Freedom Holdings, Inc. v. Spitzer*, 357 F.3d 205, 223-24 (2d Cir. 2004).[10]

B. Section Two Liability

Pleading a relevant market is likewise not always necessary for a Section Two claim. *PepsiCo, Inc. v. Coca-Cola Co.*, 315 F.3d 101, 107 (2d Cir. 2002). *PepsiCo* cited *United States v. E.I. du Pont de Nemours & Co.*, 351 U.S. 377, 391(1956) and

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[10] *Freedom Holdings* rejected a claim of state action immunity where, as here, there was "no mechanism . . . whereby New York may review the reasonableness of the pricing decisions of [the parties]." 357 F.3d at 231 (internal quotation marks and citation omitted). Accordingly, the exhortation of two antitrust scholars is appropriate here: "Private parties who restrain trade pursuant to government directives do so at their peril." J. Lopatka & W. Page, *State Action and the Meaning of Agreement Under the Sherman Act: An Approach to Hybrid Restraints*, 20 Yale J. Reg. 269, 292 (2003).

Tops Markets, Inc. v. Quality Markets, Inc., 142 F.3d 90, 98 (2d Cir. 1998), "noting that monopoly power 'may be proven directly by evidence of the control of prices or the exclusion of competition . . .'" 315 F.3d at 107.[11]

C. *Per Se* Liability

The above analysis also places the antitrust misconduct alleged squarely in the *per se* category of a group boycott under *Klor's, Inc. v. Broadway-Hale Stores, Inc.*, 359 U.S. 207, 212 (1959).[12] *See also NYNEX Corp. v. Discon, Inc.*, 525 U.S. 128, 136 (1998). Although the group boycott by all PFAs was *imposed* upon them, that is no matter. *See* discussion of *324 Liquor* and *Freedom Holdings*, *supra*. A vertically imposed group boycott is thus as actionable *per se* as one voluntarily organized by a horizontal group of sellers or buyers.

POINT II

THE DISTRICT COURT'S DISMISSAL WITH PREJUDICE WAS AN ABUSE OF DISCRETION AND WRONGLY HELD THAT LEAVE TO AMEND WOULD BE "FUTILE"

The Panel Decision was simply wrong to let stand the District Court's dismissal with prejudice. This Court has a long history of recognizing the

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[11] *See also* 2A Phillip E. Areeda, *et al.*, Areeda & Hovenkamp's *Antitrust Law*, ¶ 531a at 156 (2002) (stating that a relevant market definition simply serves as a "surrogate" for market power).

[12] HWC alleged *per se* liability in the alternative, as the District Court recognized. District Court opinion at A-311 - A-312. *See also* PrBr at 36; RepBr at 44.

vicissitudes of parties' attempts to plead antitrust violations. Indeed, the decision below resembles the dismissal reversed by this Court in *Discon, Inc. v. Nynex Corp.*, 93 F.3d 1055 (2d Cir. 1996), *rev'd on other grounds*, *Nynex Corp. v. Discon, Inc.*, 525 U.S. 128 (1998). In *Discon*, this Court held, "In this case, we believe that the District Court may have been misled by a poorly drafted complaint into categorizing the arrangement as one that is presumptively legal."[13] 93 F.3d at 1059 (C.J. Newman). This Court even found that the *Discon* complaint "states a cause of action under Section One of the Sherman Act, though under a *different legal theory* than the one articulated by Discon." *Id.* (emphasis added). Although the Supreme Court reversed on the merits, it did not question this Court's duty to review antitrust complaints such that they may "properly be understood to allege arrangements that *might be shown* to be unlawful . . .." *Id.* (emphasis added).

As Judge Winter more recently wrote in another case involving antitrust claims:

> It is too late in the day and entirely contrary to the spirit of the Federal Rules of Civil Procedure for decisions on the merits to be avoided on the basis of [ ] mere technicalities. 'The Federal Rules reject the approach that pleading is a game of skill in which one misstep by counsel may be decisive to the outcome and accept the principle that the purpose of

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[13] Appellate Counsel for HWC has conceded that, as to the precise theories of liability, the Complaint was not a model of clarity -- although the *factual* allegations were certainly clear enough to put Defendants on notice of the alleged misconduct (PrBr at 23).

pleading is to facilitate a proper decision on the merits.'

Freedom Holdings, Inc. v. Spitzer, supra, 357 F.3d at 235 (internal citations omitted).

HWC well appreciates that after the briefs in this appeal were filed, the Supreme Court decided *Bell Atlantic Corp. v. Twombly*, 550 U.S. 544, 127 S. Ct. 1955 (2007). *See* Panel Decision at 5340. However -- and here the Panel Decision grievously misses this point -- even though *Twombly* may have added to the pleading standard of Fed. R. Civ. Pro. 8(a)(2) the patina of "above the speculative level," *Twombly* left *untouched* Rule 15(a)(2)'s command to "freely give leave [to amend]."[14]

As noted, the *factual* details in HWC's Complaint sufficed to describe antitrust misconduct, while the specific antitrust *legal* theories were not precise. Accordingly, the language of then-Chief Judge Newman in *Discon* continues as a beacon:

> This appeal typifies one of the primary difficulties in the judicial application of antitrust law. Under Section One of the Sherman Act, courts are asked to categorize various complex commercial arrangements into a rigid legal taxonomy, *e.g.*, horizontal restraint, vertical restraint, price-fixing, market division, concerted refusal to deal, and so on. This initial categorization is often outcome-determinative. Under one category, the arrangement may be *per se* illegal, while under another, it may be found permissible under the rule of reason. Due to the complexity of modern business transactions, however, courts often find that commercial arrangements can be classified theoretically under a number of different categories. ("[Elasy labels do not always supply

[14] Notably, in *Twombly* and *Discon*, this Court's review of the sufficiency of the complaint was of an already *amended* complaint. HWC is entitled to no fewer opportunities to articulate more precisely the theories of antitrust liability that the *facts* in the original Complaint would support.

ready answers.").

93 F.3d at 1058-59 (emphasis added; internal citation omitted).

The Decision's sole reliance on *Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430 (3d Cir. 1997) is inapposite, and its citation is somewhat surprising. Unlike here, *Queen City* did not deal with a regulated market (*see* Point III, *infra*), but with a retail franchise arrangement, with which courts have had extensive experience. Nor, unlike here, did the *Queen City* complaint allege *facts* demonstrating direct evidence of anticompetitive effect. *See* Argument, Point I, *supra*.[15]

Even after *Twombly*, then, this antitrust case warrants an opportunity to replead. To hold otherwise would undermine the notice pleading basis of federal civil practice. *See* R. Epstein, *Bell Atlantic v. Twombly: How Motions to Dismiss Become (Disguised) Summary Judgments*, 25 Wash. U. J.L. & Policy 61 (2007).

POINT III

THE PANEL DECISION MISAPPREHENDED HWC'S ASSERTION OF THE RELEVANT MARKET

In its Complaint, as construed by the District Court, HWC maintained that the

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[15] Notably, the Third Circuit panel decision in *Queen City* was not unanimous. 124 F.3d at 444 (dissenting opinion of Circuit Judge Lay). Nor did the dispute end there, as Circuit Judge Becker wrote a spirited dissent from the order denying *en banc* consideration. 129 F.3d 724 (3d Cir. 1997) ("[E]ven if the majority's legal position is correct, it can only be sustained if it were an affirmance of a summary judgment on a full record," rather than a 12(b)(6) motion to dismiss.).

relevant market was the New York State PFAs, as *buyers* of restraint training services. This discrete market is clearly demarcated by the OCFS regulatory regime. As noted, OCFS had not only licensing and regulatory authority over the PFAs, but also the authority -- which it abused -- to approve their restraint training vendors. No PFA can operate in New York without this approval.

In its cursory relevant market analysis, the Decision misapprehended the significance of this regulatory structure. Although it cited *Todd*, the Panel did not afford HWC the deliberation it gave the complaint in *Todd*. At the pleading stage, the Panel could not determine that HWC's market definition was not "plausible." *See* PrBr at 24-30, 31 n.18, 37; RepBr at 32-45. *See also Chicago Bridge & Iron Co. N.V. v. F.T.C.*, 534 F.3d 410, 438 (5th Cir. 2008), *quoting United States v. Syufy Enters.*, 903 F.2d 659, 673 (9th Cir.1990) ("[S]some of the most insuperable barriers in the great race of competition are the result of government regulation."); *Rebel Oil Co., Inc. v. Atlantic Richfield Co.*, 51 F.3d 1421, 1439 (9th Cir.1995) (noting one "main source[ ] of entry barriers" is "legal license requirements.").

Defendants' TCI program should face competition in New York State from other vendors. The fact that Cornell and CHE do not face competition, despite charging four times what they charge in a competitive market, clearly manifests that the New York PFAs, as a buyers' market for training, is distinct from the larger

market that the District Court, and this Court, erroneously selected (RepBr at 42).

The Panel Decision failed to consider that the market asserted by HWC is, as mandated by *Todd*, "comprised of buyers *who are seen by sellers as being reasonably good substitutes*." 275 F.3d at 202 (emphasis added; internal citation omitted). The regulatory strictures on the PFAs controlled by OCFS render them utterly outside the larger market selected by the Panel (Decision at 5344-45).

Finally, in cases where normal competition is confined and restricted by law and regulation, there is less reason to focus on theoretical concepts of interchangeability of use or cross-elasticity of demand, simply because the regulatory environment keeps normally broad market forces at bay.[16]

CONCLUSION

> Antitrust laws in general, and the Sherman Act in particular, are the Magna Carta of free enterprise. They are as important to the preservation of economic freedom and our free-enterprise system as the Bill of Rights is to the protection of our fundamental personal freedoms. And the freedom guaranteed each and every business, *no matter how small*, is the freedom to compete -- to assert with vigor, imagination, devotion, and ingenuity whatever economic muscle it can muster.

United States v. Topco Associates, Inc., 405 U.S. 596, 610 (1972) (emphasis added).

For the foregoing reasons, Plaintiff-Appellant HWC respectfully requests

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[16] Moreover, the Panel's reliance on the opinion of a divided Third Circuit panel in *Queen City*, *supra* -- dealing with suppliers of pizza dough, which is *not* a regulated market -- was both factually inapposite and reflects an inadequate analysis of the PFAs' regulatory environment abused by Defendants.

rehearing *en banc* (and, alternatively, by the Panel) and that the Panel Decision be vacated, that a new decision issue reversing the decision of the District Court and vacating its judgment, and, further, that the case be remanded with leave to HWC to replead its antitrust claims in an amended complaint.

Dated: New York, NY
December 3, 2008

Respectfully submitted,

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UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

August Term, 2007

(Argued: October 25, 2007 Decided: October 14, 2008)

Docket No. 05-7010-cv

BRUCE CHAPMAN AND HANDLE WITH CARE BEHAVIOR MANAGEMENT SYSTEM, INC.,

Plaintiffs-Appellants,

—v.—

NEW YORK STATE DIVISION FOR YOUTH, NEW YORK STATE OFFICE OF CHILDREN & FAMILY SERVICE, NEW YORK STATE DEPARTMENT OF SOCIAL SERVICES, JOHN JOHNSON, Commissioner of New York State Office of Children and Family Services, and former Commissioner of the New York State Division for Youth, in his official and individual capacity, MARGARET DAVIS, former Director of Training for the New York State Division for Youth, and former Director of Training for New York State Office of Children and Family Services, in her official and individual capacity, PATSY MURRAY, former Associate Training Technician for the New York State Division for Youth, and current position as Trainer for New York State Office of Children and Family Services, in her official and individual capacity, CORNELL UNIVERSITY, JEFFREY LEHMAN, President of Cornell University, in his official and individual capacity, DOCTOR HUNTER RAWLINGS, III, former President of Cornell University, in his official and individual capacity, NEW YORK STATE COLLEGE OF HUMAN ECOLOGY, FAMILY LIFE DEVELOPMENT

CENTER, RESIDENTIAL CHILD CARE PROJECT, THERAPEUTIC CRISIS INTERVENTION, MARTHA HOLDEN, Project Director of the Residential Child Care Project and Therapeutic Crisis Intervention Trainer and Coordinator, in her official and individual capacity, MICHAEL NUNNO, Project Director of the Residential Child Care Project and Therapeutic Crisis Intervention Trainer and Coordinator, in his official and individual capacity, HILLSIDE CHILDREN'S CENTER, DENNIS RICHARDSON, President and CEO of Hillside Children's Center, in his official and individual capacity, DOUGLAS BIDLEMAN, Employee of Hillside Children's Center and Therapeutic Crisis Intervention Trainer, in his official and individual capacity,

Defendants-Cross-Defendants-Appellees.

B e f o r e :

WALKER, STRAUB, and POOLER, *Circuit Judges.*

Plaintiffs-appellants seek review of an order of the United States District Court for the Northern District of New York (David N. Hurd, *Judge*) dismissing their copyright and antitrust claims pursuant to Fed. R. Civ. P. 12(b) and (c) and declining to exercise supplemental jurisdiction over their state law claims. The district court dismissed plaintiffs' copyright claims on the basis that a contract unambiguously granted the defendants a perpetual license to copy plaintiffs' materials. We conclude that the contract is ambiguous, and remand the case for further fact-finding on this issue. With regard to plaintiffs' antitrust claims, we agree with the district court that plaintiffs have failed to allege a plausible antitrust market. We therefore affirm the district court's order dismissing plaintiffs' antitrust claims with prejudice.

AFFIRMED in part; VACATED and REMANDED in part.

GUY L. HEINEMANN, Guy L. Heinemann, P.C. (Irene M. Vavulitsky, Guy L. Heinemann, P.C., and Hilary Adler, Law Offices of Hilary Adler, Gardiner, N.Y., *on the brief*), New York, N.Y., *for Plaintiffs-Appellants*.

ANDREA OSER, Assistant Solicitor General (Daniel Smirlock, Deputy Solicitor General, *on the brief*), for Eliot Spitzer, Attorney General of the State of New York, Albany, N.Y., *for Defendants-Appellees, New York State Division for Youth, New York State Department of Social Services; New York State Office of Children & Family Services, John Johnson; Margaret Davis, and Patsy Murray.*

NELSON E. ROTH (Valerie L. Cross and Norma W. Schwab, *on the brief*) Office of the University Counsel, Ithaca, N.Y., *for Defendants-Appellees, Cornell University, Jeffrey Lehman, Hunter Rawlings, III, New York State College of Human Ecology, Family Life Development Center, Residential Child Care Project, Therapeutic Crisis Intervention, Martha Holden, and Michael Nunno.*

DAVID H. WALSH, Petrone & Petrone, P.C., Syracuse, N.Y., *for Defendants-Appellees, Hillside Children's Center, Dennis Richardson, and Douglas Bidleman.*

JOHN M. WALKER, JR., *Circuit Judge*:

Plaintiffs-appellants Bruce Chapman and Handle With Care Behavior Management System, Inc., (collectively "HWC") market a training program ("Handle With Care") that teaches individuals a safe technique for physically restraining others. HWC sued three

groups of defendants alleging generally that they had infringed HWC's copyright and adversely affected the market for such restraint services in violation of the antitrust laws.

Specifically, HWC sued various New York state agencies and their officers and agents (collectively "the state defendants"). The state defendants include: the New York State Office of Children and Family Services ("OCFS"), which in 1998 succeeded the New York State Division for Youth ("DFY") and the New York State Department of Social Services ("DSS") also named as defendants; John Johnson, the former Commissioner of DFY and the current Commissioner of OCFS; Margaret Davis, the former Director of Training for DFY and the current Director of Training for OCFS; and Patsy Murray, a former Associate Training Technician for DFY and current Trainer for OCFS.

HWC also sued Cornell University and the New York State College of Human Ecology (the "College") and related persons and entities (collectively "the Cornell defendants"). The Cornell defendants include: Cornell University; Jeffrey Lehman, Cornell's then-current president; Hunter Rawlings III, Cornell's former president; the College and subsidiaries the Family Life Development Center, the Residential Child Care Project, and Therapeutic Crisis Intervention ("TCI"); and Project Directors of the Residential Child Care Project and TCI Trainers and Coordinators, Martha Holden and Michael Nunno.

Finally, HWC sued Hillside Children's Center ("HCC"), a private childcare provider and residential treatment center, and two of its officers, Dennis Richardson, HCC's president, and Douglas Bidleman, HCC's Coordinator for Sociotherapy (collectively "the Hillside defendants").

The state and Cornell defendants moved to dismiss the complaint pursuant to Fed. R. Civ. P. 12(b)(6), and the Hillside defendants moved to dismiss the complaint pursuant to Fed. R. Civ. P. 12(c). The district court granted both motions as to all of plaintiffs' federal claims and declined to exercise supplemental jurisdiction

over the remaining state law claims. The federal claims dismissed were: (1) copyright infringement against the state defendants; and (2) conspiracy to monopolize and restrain trade, together with monopoly, restraint of trade, and unfair competition, against all defendants.

The district court dismissed plaintiffs' copyright claim on the basis that the contract at issue unambiguously granted the state defendants the right to copy plaintiffs' materials indefinitely. We disagree with that conclusion, find the contract ambiguous, and remand the case to the district court to determine the duration of the license to copy plaintiffs' materials granted under the contract.

With regard to the antitrust claims, the district court held that the plaintiffs failed to offer a plausible relevant market in which the defendants monopolized the trade for restraint services or engaged in restraint of trade or unfair competition with respect thereto. We agree that the plaintiffs have failed to define a plausible market and conclude that the plaintiffs cannot establish that the defendants have substantial market power in the market for restraint services properly defined. Accordingly, we affirm the district court's dismissal of plaintiffs' antitrust claims and vacate the district court's dismissal of the copyright claim against the state defendants.

BACKGROUND

For purposes of reviewing a motion to dismiss, we assume the accuracy of the plaintiffs' allegations in their complaint. *Patane v. Clark*, 508 F.3d 106, 111 (2d Cir. 2007) (per curiam). "[O]ur review is limited to undisputed documents, such as a written contract attached to, or incorporated by reference in, the complaint." *Official Comm. Of Unsecured Creditors of Color Tile, Inc. v. Coopers & Lybrand, L.L.P.*, 322 F.3d 147, 160 n.7 (2d Cir. 2003) (citing *Cortec Indus., Inc. v. Sum Holding, L.P.*, 949 F.2d 42, 47 (2d Cir. 1991)).

OCFS (previously DFY and DSS) operates juvenile facilities and monitors child care providers in the state of New York. The New York legislature mandated that OCFS:

> promulgate regulations concerning standards for the protection of children in residential facilities and programs operated or certified by the division, from abuse and maltreatment . . . Such standards shall . . . establish as a priority that: . . . administrators, employees, volunteers and consultants receive training in . . . : the characteristics of children in care and techniques of group and child management including crisis intervention.

N. Y. Exec. Law § 501(12); *see also* N.Y. Soc. Serv. Law § 462(1)(c). To that end, state regulations require that each supervised child care facility "submit[ ] its restraint policy to [OCFS]" and prohibit the use of "any method of restraint unless it has . . . been approved in writing by [OCFS]." 18 N.Y. Comp. Codes R. & Regs. § 441.17(c).

In 1987, New York State purchased HWC's method for use in its own facilities. That year, DFY contracted with HWC to provide training in HWC's methods to its staff (the "1987 contract"). The 1987 contract provided that HWC would train 120 DFY staff members over fifteen days in HWC's methods. It further provided that HWC would furnish DFY with one "copy of Handle With Care (copyrighted) which [DFY] may reproduce in whole or in part as required by [DFY]" and "a videomaster of the restraint program to be used by [DFY's] master trainers in conducting training programs for facility staff." Finally, the contract stated that "[t]his agreement shall commence January 1, 1988 and end March 31, 1988." There is no dispute that HWC fulfilled its obligations under the 1987 contract and trained 120 DFY staff, some of whom were master trainers, during the relevant three-month term. In 1997, however, after two incidents at DFY facilities in which children were harmed by the use of improper restraint techniques, DFY requested that HWC provide retraining to its staff.

The resulting contract (the "1997 contract") provided that HWC would "update and recertify existing [DFY] Crisis Management/Physical Restraint trainers in the techniques encompassed in the *Handle With Care* program;" that it would "deliver twelve (12)

days of training to approximately one hundred twenty (120) existing [DFY] trainers;" and that DFY had "the right to reproduce all training materials."[1] The contract provided that the "agreement shall commence May 1, 1997 and end August 31, 1997." Additionally, HWC required DFY staff members to sign individual contracts acknowledging that their certification to train in HWC's methods terminated after one year.

HWC furnished the training and materials in conformity with the 1997 contract. Thereafter, there is no dispute that DFY master trainers, using HWC's materials, trained the rest of DFY's staff in the HWC method. A year later, DFY merged into OCFS and the latter continued to use HWC's materials to train its staff.

HWC faced competition in the restraint method and training business. Cornell, in partnership with the State of New York, developed and marketed its own restraint method and training services called Therapeutic Crisis Intervention ("TCI"). HWC and TCI competed in providing restraint training services to various agencies, organizations, and businesses.

Sometime after DFY merged with OCFS in 1998, OCFS began to withhold its approval of each facility's restraint method unless the TCI method was used. After learning of the alleged policy change at OCFS, HWC filed the instant action challenging the policy, claiming that OCFS, Cornell, and HCC conspired to monopolize the market for restraint services in violation of the antitrust laws. HWC also claimed that OCFS infringed HWC's copyright by reproducing HWC's materials in 1998 and by continuing to use them and made various state law claims. After the district court dismissed these claims, HWC appealed.

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[1] We note that, as defendants acknowledge on appeal, the district court was mistaken in its view that the contract was "drafted by Chapman."

DISCUSSION

I. Legal Standard

We review *de novo* the dismissal of a complaint for failure to state a claim, and accept all well-pleaded facts as true and consider those facts in the light most favorable to the plaintiff. *Patane v. Clark*, 508 F.3d 106, 111 (2d Cir. 2007) (per curiam).

> To survive dismissal, the plaintiff must provide the grounds upon which his claim rests through factual allegations sufficient 'to raise a right to relief above the speculative level.' Once a claim has been adequately stated, it may be supported by showing any set of facts consistent with the allegations in the complaint.

ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 493 F.3d 87, 98 (2d Cir. 2007) (quoting *Bell Atl. Corp. v. Twombly*, 127 S. Ct. 1955, 1965 (2007)).

II. The Copyright Claim

HWC's copyright claim against the state defendants is dependent upon the terms of the 1997 contract. There is no dispute that DFY copied HWC's materials; the only question is whether DFY had the right to do so. *See Graham v. James*, 144 F.3d 229, 236 (2d Cir. 1998) ("A copyright owner who grants a nonexclusive license to use his copyrighted material waives his right to sue the licensee for copyright infringement."). "In interpreting a contract, the intent of the parties governs. A contract should be construed so as to give full meaning and effect to all of its provisions." *Am. Express Bank Ltd. v. Uniroyal, Inc.*, 562 N.Y.S.2d 613, 614 (N.Y. App. Div. 1990) (citations omitted). The question of whether a provision in an agreement is ambiguous is a question of law. *Collins v. Harrison-Bode*, 303 F.3d 429, 433 (2d Cir. 2002). Under New York law, the presence or absence of ambiguity is determined by looking within the four corners of the document, without reference to extrinsic evidence. *Kass v. Kass*, 696 N.E.2d 174, 180

(N.Y. 1998). "[A]n ambiguity exists where a contract term could suggest more than one meaning when viewed objectively by a reasonably intelligent person who has examined the context of the entire integrated agreement and who is cognizant of the customs, practices, usages and terminology as generally understood in the particular trade or business." *World Trade Ctr. Props., L.L.C. v. Hartford Fire Ins. Co.*, 345 F.3d 154, 184 (2d Cir. 2003) (internal quotation marks and citation omitted).

We must decide whether the 1997 contract is ambiguous as to the duration of the license granted to copy HWC's materials. Although both parties contend that the 1997 agreement is unambiguous on its face, they draw different conclusions as to the duration of the license. HWC claims that, according to the 1997 contract's "Term of Agreement" provision, DFY's right to copy its materials ended on August 31, 1997 (120 days after the agreement commenced). The state defendants, however, contend that the 1997 contract unambiguously grants DFY a perpetual right to copy HWC's materials. The district court agreed with the state defendants. We disagree and conclude that the contract on its face is ambiguous.

The purpose of the 1997 contract is not disputed: HWC agreed to "update and recertify existing [DFY] Crisis Management/Physical Restraint trainers in the techniques encompassed in the *Handle With Care* program." To that end, the agreement provided that HWC would perform twelve days of training to DFY trainers. The DFY trainers would then train the rest of DFY's staff in HWC's methods. Contemplating that the DFY trainers would need to utilize HWC's materials in training the rest of the Division staff, the 1997 contract acknowledged that "[DFY] has the right to reproduce all training materials."

HWC's argument that the license to copy its materials expired after 120 days conflicts with the agreement's purpose. While the 1997 contract states that the "agreement shall commence May 1, 1997 and end August 31, 1997," there is nothing in the contract that expressly indicates that this provision governs the duration of

the license to copy HWC's materials. Indeed, from the four corners of the agreement, it is not at all certain that the parties intended that DFY's rights to copy HWC's materials terminate so quickly. HWC plainly knew that it was training trainers who, if they were to train the rest of DFY's staff, would need to copy HWC's materials. The provision allowing use of HWC's materials is unclear on its face as to whether it was meant to end with the agreement, or whether it was meant to continue for a reasonable period of time after the agreement ended to allow for further training of DFY staff.

We are equally unpersuaded that the 1997 contract granted a perpetual license. There is no indication from the contract that the license to copy HWC's materials was meant to be perpetual. And under New York law, "[c]ontracts which are vague as to their duration generally will not be construed to provide for perpetual performance." *Ketcham v. Hall Syndicate, Inc.*, 236 N.Y.S.2d 206, 214 (N.Y. Sup. Ct. 1962). In the absence of a clear provision, courts are reluctant to declare a perpetual license as a matter of law. *See Warner-Lambert Pharm. Co. v. John J. Reynolds, Inc.*, 178 F. Supp. 655, 661 (S.D.N.Y. 1959), *aff'd*, 280 F.2d 197 (2d Cir. 1960) (per curiam). Because the contract here does not explicitly grant a perpetual license, we do not find that it did so.

After rejecting both parties' arguments and finding no plausible alternative within the four corners of the document, we conclude that the 1997 contract is ambiguous as to the duration of the license. This leaves us two choices. "We may resolve [the] ambiguity . . . if there is no extrinsic evidence to support one party's interpretation of the ambiguous language or if the extrinsic evidence is so one-sided that no reasonable factfinder could decide contrary to one party's interpretation. Or, we may remand for the trial court to consider and weigh extrinsic evidence to determine what the parties intended." *Collins*, 303 F.3d at 433 (internal quotation marks and citation omitted). We choose the latter.

The extrinsic evidence presently in the record does not answer the question. HWC points out that when it provided retraining in 1997, it required each Division trainer to sign a contract acknowl-

edging that his/her certification expired after one year. This evidence would support a finding that the license granted under the 1997 contract was of a more limited duration. The evidentiary record, however, is incomplete. Because further fact-finding is necessary, we remand the copyright claim to the district court for further proceedings consistent with this opinion.[2]

III. Plaintiffs Have Failed to Define the Proper Market for Antitrust Purposes

HWC claims that OCFS, in cooperation with Cornell, has conspired to create a monopoly in the market for "training services to private child care providers located within the State of New York" by withholding approval of supervised facilities that do not use the TCI method. HWC alleges that HCC was complicit in this arrangement because, after HWC trained HCC's staff in 2001, HWC discovered that one of HCC's training coordinators "appeared in TCI's training manual and video illustrating" HWC's proprietary methods.

For a monopoly claim "[t]o survive a Rule 12(b)(6) motion to dismiss, an alleged product market must bear a rational relation to the methodology courts prescribe to define a market for antitrust purposes — analysis of the interchangeability of use or the cross-elasticity of demand, and it must be plausible." *Todd v. Exxon Corp.*, 275 F.3d 191, 200 (2d Cir. 2001) (internal quotation marks and citation omitted). "[T]he reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it" determine "[t]he outer boundaries of a product market." *Brown Shoe Co. v. United States*, 370 U.S. 294, 325 (1962). Though "market definition is a deeply fact-intensive inquiry [and] courts [therefore] hesitate to grant motions to dismiss

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[2] Because the district court did not have occasion to reach the state defendants' Eleventh Amendment immunity defenses, and because the Eleventh Amendment would not, in any event, bar suit against OCFS officials and employees sued in their official capacity for injunctive relief, *Henriettta D. v. Bloomberg*, 331 F.3d 261, 287 (2d Cir. 2003), we do not need to reach this issue.

for failure to plead a relevant product market," *Todd*, 275 F.3d at 199-200, "[w]here the plaintiff fails to define its proposed relevant market with reference to the rule of reasonable interchangeability and cross-elasticity of demand, or alleges a proposed relevant market that clearly does not encompass all interchangeable substitute products even when all factual inferences are granted in plaintiff's favor, the relevant market is legally insufficient and a motion to dismiss may be granted," *Queen City Pizza, Inc. v. Domino's Pizza, Inc.*, 124 F.3d 430, 436 (3d Cir. 1997). Here we find that plaintiffs' proposed relevant market does not encompass all interchangeable substitute products. We therefore affirm the district court's dismissal of the antitrust claims.

HWC contends that the relevant market for our analysis here is the market for "restraint training services to private child care providers located within the State of New York." This definition is too narrow. HWC has failed to show how the market for restraint training services *to child care providers* is any different from the larger market for restraint training services to other businesses, agencies, and organizations. "Interchangeability implies that one product is roughly equivalent to another for the use to which it is put. . . ." *Queen City*, 124 F.3d at 437 (internal quotation marks and citation omitted). Plaintiffs do not contest that Handle With Care is marketed to and utilized by various organizations, institutions, and agencies that are not child care providers. Indeed, plaintiffs readily admit in their complaint that they compete for such contracts on a "national and international" basis. The unifying characteristic of this market is that each purchaser needs to restrain individuals, not just children.

Because "the reasonable interchangeability of use . . . between the product itself and substitutes for it" determines "[t]he outer boundaries of a product market," it is apparent that the proper market here is the larger market for restraint training services to businesses, agencies, and organizations with the need to safely restrain individuals of all ages, not the more limited market for child restraint services. *Brown Shoe*, 370 U.S. at 325. As the district

court noted, the larger market includes social service agencies, law enforcement agencies, correctional facilities, educational facilities, and even airlines.

Furthermore, we reject HWC's argument that because private child care providers in New York must have OCFS approval in order to operate, and thus that the market is specialized, it stated a plausible discrete relevant market. The relevant inquiry is not whether a private child care provider may reasonably use both approved and non-approved OCFS methods interchangeably, but whether private child care providers in general might use such products interchangeably. *See Queen City*, 124 F.3d at 438. HWC's proposed relevant market "clearly does not encompass all interchangeable substitute products even when all factual inferences are granted in plaintiff 's favor." *Id.* at 436. We thus agree with the district court that the "Plaintiffs have not offered any theoretically reasonable explanation for restricting the product market to child care providers that require OCFS approval, or provided a sufficient factual predicate to support an inference that OCFS enjoys any substantial market power in the broader market for restraint services." Plaintiffs' proposed market is therefore legally insufficient and dismissal of the antitrust claims was appropriate.[3]

CONCLUSION

For the foregoing reasons, the judgment below is AFFIRMED as to the antitrust claims and VACATED as to the copyright claim and the case is REMANDED to the district court for further proceedings consistent with this opinion.

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[3] HWC argues that the district court exceeded its allowable discretion in dismissing their antitrust claims with prejudice, as opposed to allowing HWC to amend their complaint. Given the nature of the claims; repleading would be futile; HWC offers no plausible argument as to how the failure to plead a relevant market could be rectified through an amended complaint. *See Patane v. Clark*, 508 F.3d 106, 113 n.6 (2d Cir. 2007) (per curiam).

ANTI-VIRUS CERTIFICATION FORM

See Second Circuit Interim Local Rule 25(a)6.

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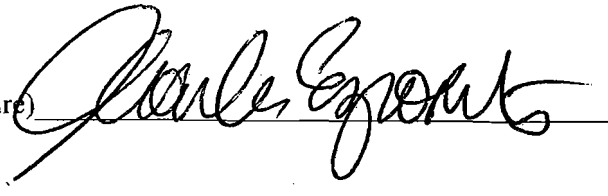
(Your Signature) 

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EDWIN RIOS, being duly sworn, deposes and says that he is over the age of 18 years, is not a party to this action, and resides at 2828 West 15th Street, Brooklyn, New York 11224.

That on December 4, 2008, he served 2 copies of Petition for Panel Rehearing Petition for Rehearing *En Banc* (Chapman, et al. v. New York State Division for Youth, et al.) on:

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December 4, 2008

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COMMISSION EXPIRES OCTOBER 31, 2009