

LITIGATION

MEMOREX: SPENDING CONTINUES

Memorex will seek another trial, but a directed verdict for IBM also is a possibility.

As recently as mid-May of this year, Memorex Corp. chairman Robert C. Wilson was saying that one thing seemed certain in his company's billion-dollar antitrust suit against IBM. In the latter half of this year, it then appeared, the case would be resolved and the company would be able to reduce drastically its spending on the litigation. Wilson would not say how much the company was spending, but it has been estimated at somewhere between \$1 million and \$1.5 million a year. The spending could continue.

After 20 days of deliberation, the 11-member jury in the Memorex case remained deadlocked and a mistrial was declared last month by U.S. District Judge Samuel Conti. At that time, Memorex said it would file for a retrial, again by jury. And IBM filed motions for a directed verdict in its favor, much as was done successfully in the CalComp case

against IBM, which CalComp is appealing.

As this was being written, therefore, it was still possible that a directed verdict in favor of IBM would settle the entire case, before a retrial could even be considered.

The hung jury in the Memorex case raises again the question of whether any jury can adequately understand and unanimously agree on the issues in one of these IBM cases. Immediately after the mistrial was declared, IBM chairman Frank Cary said, "We are not surprised that the jury could not reach agreement in a case of this complexity . . ."

But securities analyst Calvert D. Crary of Bache Halsey Stuart Shields Inc., a trained lawyer who follows corporate cases, disagrees. "I've never seen one that was too complex for a jury," he remarks.

Crary views the mistrial as a blessing in disguise for Memorex. He says some passages in the court's instructions to the jury are questionable and could be cause for a reversal on appeal. If, for example, the decision had been in Memorex's favor and IBM had appealed, only to have the verdict overturned, both parties would have to go through the entire procedure of a trial again, just as Memorex was preparing to do. Only it would now be two years and several million dollars later.

What Crary is especially critical of are the instructions regarding predatory pricing. He says anyone who obeyed those

instructions would have had to decide the case for Memorex. "I think Memorex the next time around will make sure that that instruction is radically changed."

Assuming that there is a next time around for Memorex, one can see that the company joins six other private parties whose antitrust suits against IBM remain in the balance (see chart). That's not to mention the large federal trial still underway in New York City. And anyone who had the misfortune of having to sit through all of those and earlier proceedings would find that many of the issues are the same, as are many of the witnesses.

The Memorex trial, which many thought would require 10 months or more, came in in less than six months. It produced a trial transcript of more than 18,000 pages and saw the introduction as evidence of thousands of exhibits and more than 80 witnesses. In it, Memorex charged IBM with monopolizing four markets—specifically the markets for general purpose systems or mainframes, for IBM-compatible disc drives, for compatible disc drive controllers, and for compatible communications controllers or front-ends. Of course, each is a market that Memorex is active in or one that it tried to get into.

The one market where it no longer is

was further alleged, IBM took measures to discredit the viability of the plug-compatible peripherals business.

In his final arguments to the jury, Memorex's lead attorney John Endicott drew from a reservoir of months of testimony. He flashed graphs and numbers on a large screen, showed a page out of the trial transcript and read a line or paragraph from someone's testimony, and repeatedly said, "if you recall" and "you may remember."

In an effort to show that IBM possessed monopoly power in the relevant market, he displayed a bar chart that contrasted IBM's and Memorex's gross incomes in billions of dollars from 1966 through 1973. One could hardly find the bar that represented Memorex. He also had one that showed the two companies' shares of the IBM plug-compatible disc drive market—in megabytes and as of December '73. It indicated that IBM had almost 80%, Memorex less than 10%.

Finally, there was one showing the installed value in the general purpose computer systems market, IBM being shown having 70% of this market, followed by Univac with less than 10%, and the other dwarfs dutifully following behind.

The Los Angeles attorney also drew upon some documents recovered from

IBM's San Jose, Calif., lab, one that recommended a development contract with the Atomic Energy Commission. "It should be deliberately done as a competition stopper," Kolsky wrote. "It should get our machines back into our customers' future plans. It should be a deliberate prestige winner. That is, a project to get IBM back into the position of being the real leader of the computing community. It should be deliberately done as a money loser (or, more tactfully, a shared cost development for the benefit of the government)."

"I submit that this document alone conclusively shows that IBM's purpose was to exclude competition," Endicott said.

The attorney reviewed testimony and exhibits that he said showed IBM tried to eliminate competition not only among mainframe manufacturers, such as RCA and GE, but also to eliminate third-party leasing companies.

The Memorex attorney was especially critical of the IBM 2319A, the disc drive developed for use with the 370/145 and the 135. Endicott charged that IBM chose not to use the existing 2314 drives with those two mainframes because the 2314 interfaces would allow plug-compatible peripherals suppliers to supplant IBM drives. In its place, he alleged, IBM developed the 2319A, code-named Mallard, which had part of the interface buried in



DEADLOCK—The vote was 9-2 for Memorex

active, that for systems or mainframes, was the long-term goal that the company's founders were working toward, it was said. The company diversified from the manufacture of media (mag tape) to hardware, from disc drives and controllers to front-end processors, all with the idea of eventually developing the capability to make and market its own mainframes. And, it was charged, IBM kept maneuvering to head off any progress toward this objective. What's more, it

IBM's internal files, trying to show how IBM willfully acquired or maintained its alleged monopoly power. He referred to a memo written by IBM's T.J. Watson Jr., dated August 1963, that showed the executive's displeasure at Control Data Corp. taking a leadership position in super-scale computers with its announcement of the 6600. IBM's response was said to have been the 360/90.

Memorex's Endicott also referred to an internal memo from a Mr. Kolsky of

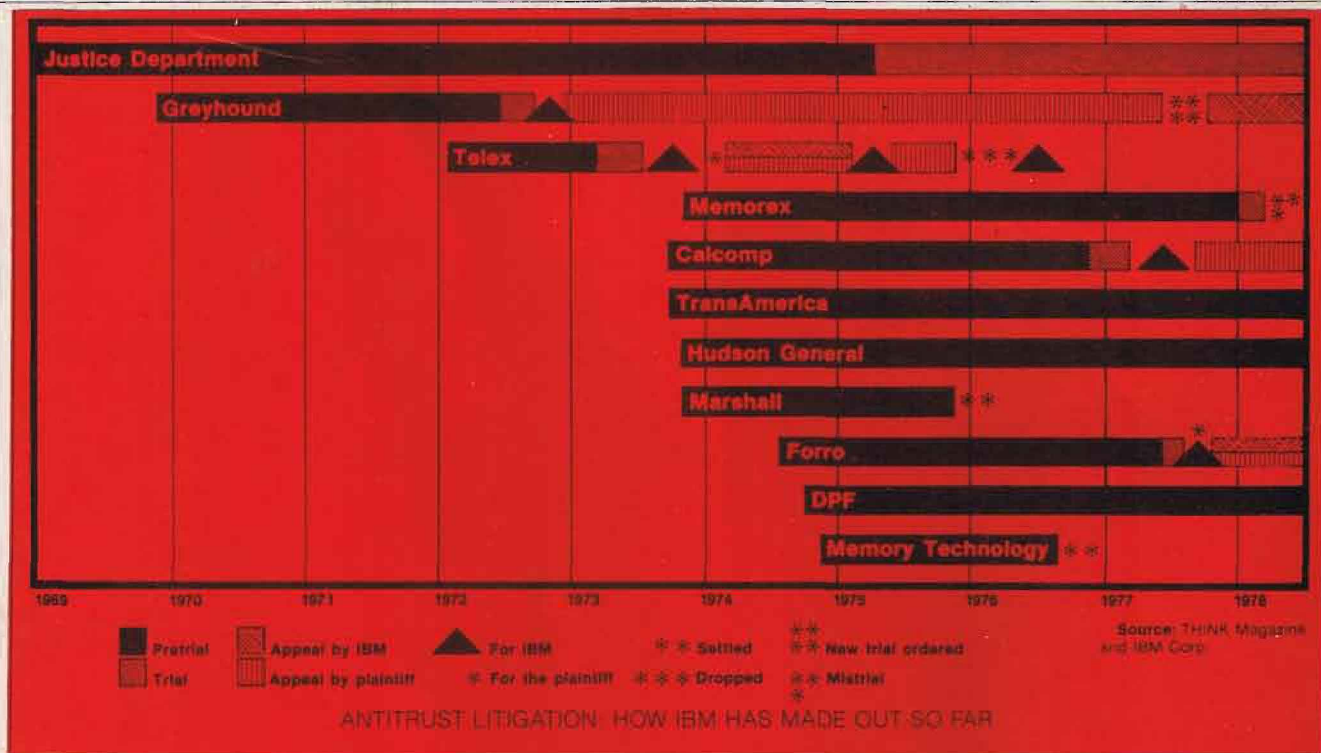
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the mainframe, the remainder in the drives. "The effect of that was to exclude competition," he charged, adding that "from the evidence in this case, no PCM ever did attach at that interface."

Further, he said, IBM lowered the spindle price on the 2319As and raised the prices of the 135 and 145s. He termed these moves as examples of selective and discriminatory price cutting, of price balancing, and of predatory pricing.

"It was really the first message by IBM to the financial community that the PCM's might be a dangerous investment," he said. "that it might not be wise to either lend money or invest money in the PCM's because IBM was willing to give up short-term profits in order to get rid of some competition."

Endicott also referenced testimony by the president of Marshall Industries, who said the price cuts on the 2319A "made it impossible for us to get any kind of private or public financing on any reasonable terms." Memorex cofounder and past president Laurence L. Spitters testified to the same effect. And a Wall Street securities analyst was also quoted as having recommended that Memorex share-



holders sell their stock because of the newly announced 370/145 and the 2319 "that will complicate life for the independents." The analyst, in his sale recommendation, also cited IBM's price cuts as having serious effects on the PCM's.

The industry giant in the fall of 1970 was said to have made a thorough study of the impact on Memorex's profitability if IBM were to make specific price cuts and introduce certain products. The attorney reviewed testimony that purported to show the preoccupation by IBM'ers with how IBM's product strategies might strain Memorex's relations with institutional lenders.

Said Endicott on a number of occasions during his summation: "Now, I submit you should ask yourself these questions: Are studies of the impact on the cash flow and profitability of a competitor the acts of a company which seeks to compete on the merits of its products and its services and its price? . . . The answer is no."

IBM's attorney Patrick Lynch, in his summation, had an answer for that. He referred to an internal Memorex memorandum that expressed the need to study competitors and to assess their "investment thrust and financial viability" ("Does that lead you to the conclusion that Memorex is a monopolist?" Lynch asked) and competitive strategy, both product and financial ("Does that lead you to conclude that Memorex is a monopolist because Memorex thought it worthwhile to understand the financial strategy of its competitors?").

For his part, Lynch denied any wrongdoing by IBM, attempted to ascribe Mem-

orex's problems to its mismanagement, and asserted that IBM was guilty only of being aggressive in the marketplace—as any company must. "The point is that the law encourages every company to do its best to win if it can," he said. ". . . Basically when you get down to the hard facts, we have two strong companies, two able companies, two aggressive companies competing for the business. Memorex wants some of that business, IBM wants some of that business."

He told the jurors they are in the position to legislate how business is to be conducted in the computer industry. "If

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you grant Memorex \$4 of damages," he said, "you are legislating that IBM was wrong to cut prices. You are legislating that IBM was wrong to meet competition. You are legislating that IBM cannot design new and better products for fear that some competitor may think it shouldn't have been done. You are legislating that IBM cannot announce new products" without first informing competitors of its intentions and asking for their comments.

In defending IBM's new attachment strategy, Lynch said that "what Memorex is attacking is progress. What Memorex is attacking is product improvement. What Memorex is attacking is giving users alternatives."

The damages that Memorex was asking for, before trebling, was \$306-

\$80,000. That was comprised of \$94.5 million in losses having to do with the Memorex 660 and 3670 disc drive. An additional \$27.2 million was tacked on for disc controllers. Then there was \$50.7 million for the communications front-end processors. Finally, for the amount written off for the ill-fated systems activity and the profits lost in that endeavor that never quite came off, Memorex asked for damages of \$97.8 million.

Endicott, trying to play down the enormity of \$306 million, put that amount into perspective in this way. He observed that IBM during fiscal 1977 made \$29,000 a minute, or \$1.7 million per hour, or almost \$14 million per 8-hour day. "At that rate," he said, "it takes something like 22 days—three weeks and a day—to come up with the \$306 million. You were selected as jurors on Jan. 16, 1978, as I recall. By Feb. 6th, IBM would have made the \$306 million we are asking. Since the trial has started, IBM has made something like \$1.8 billion, or six times more than our claim."

But all things said and done, does Memorex have a better chance of winning on any second go-around with IBM? After all, the jury in San Francisco was voting 9 to 2 in Memorex's favor when it became deadlocked. Analyst Crary doesn't believe so. "I don't think you can say that, one way or the other, even though I'm sure some people will," he says. Indeed, he thinks IBM was lucky this time because two of the jurors refused to be swayed by the other nine. And if a retrial were held, the jury next time might have more people like those two.

—Edward K. Yasaki