

Dearly Beloved

THE MARKER, July 2001

Breaking news: internal correspondence of Boston Scientific on its relations with Medinol : "*Guys, I think we should false sign these prints*"

By: Amir Helmar

On April 28th, 2000, one day before the eve of Passover, Kobi and Judith Richter, owners of Medinol Ltd., arrived at the office of the new General Manager of Boston Scientific, James (Jim) Tobin. The two directors could never have imagined what news the General Manager of their five-year partnership was about to break to them. Tobin spoke little in introduction. He pulled a three-paged document out of the drawer, placed it on the desk, and gave it to the Richters to read. One can only imagine how the couple felt when their eyes began running rapidly over the lines.

Later they said that Tobin had muttered, "*They are crooks*", meaning Boston Scientific's former management, which was responsible for the acts described in the document. Later on Boston claimed that these statements were taken out of context.

However, even without the words of description which were or were not stated by Tobin, the document is self-explanatory. Its title was: "*Project Independence: Timetable*". Thereafter, there is a description of the "milestones" for the project, which commenced in 1997 and continued to 2000.

It took the Richters no more than two minutes to understand the exact nature of the "project". The words "straw company", "ghost office" or "cover name", and particularly the repetition of the word "confidential" with its various inflections well clarified its nature.

The first paragraph of the document described it appropriately: "*Project Independence was initiated by Jim Corbett (Boston Scientific's former President) as a contingency plan due to the single sourcing nature of BSC-Medinol relationship. The goal of Project Independence was to create in-house manufacturing capacity of sufficient quantities of NIR stents (Medinol's product) in the event that the Medinol supply chain becomes interrupted, and to also establish an alternative etching vendor.*"

"The project was/is intended to be on a need to know basis only and not disclosed or discussed without the program directors approval."

And if the astounded Richters had still not completely understood, the June 1997 "milestone" made it very clear: Richard Gahan, an external consultant, was requested to set up a straw company to prevent the possibility of any link between Irish Boston Scientific and the operations of the special project. The company's name was FORWICH, but was given the cover name BBD.

BBD, three letters which told in fact the whole story of the project - Bringing a Better Deal.

For whom was the deal? Boston Scientific - the Richters' partner in the medical equipment company, Medinol. What deal? A better deal than the American company had had for the last five years with Medinol, under which it had been purchasing "stents" (springs used in catheterization surgeries) from Medinol, subject to significant payment of royalties amounting to hundreds of millions of dollars.

The Richters had no more doubts: their partner had attempted, right under their noses, to "duplicate" Medinol's plant, including the special patents and its unique production methods - so that in the future it would be able to become "independent" of the partnership with them and "obtain a better deal for itself".

The occurrence of this dramatic meeting at Boston Scientific's offices was revealed only a year later, as part of a lawsuit filed by Medinol against Boston Scientific. The lawsuit revealing this document as well as a long line of other documents, shed light on an affair which had occupied the press for a year, while the latter was unaware of what was really going on between Medinol and its American partner.

Until the filing of Medinol's claim, the whole story had looked different. Since April 2000 news coming from various directions has been published, according to which Boston Scientific and Kobi and Judith Richter had decided to split up and Boston was conducting negotiations to purchase their shares. The papers knew to tell that the Richters were demanding huge sums for their shares and that Boston was unwilling to pay this. This huge amount was attributed not only to Medinol's immense profitability, which according to estimates yielded the Richters an income of hundreds of millions of dollars throughout the years of the partnership, but also to the stubbornness and unrestrained aggression of the couple in business.

No one knew that by this time the Richters had good reason to be aggressive in the negotiations: they sat at the negotiating table after the documents had already been given to them and exposed what at least *prima facie* appeared as a plan to deceive them.

Once the Richters found about Project "Independence" that had been set up right under their noses, they understood two things: the first, that they no longer wanted a partnership with Boston Scientific at their plant. The other, that there was probably an opportunity to extract from it a very high price for their shares in Medinol - as Boston would have a significant interest to "put an end to the affair".

It is appropriate to mention in short who are the Richters, what is Medinol and what is its partnership with Boston Scientific. Medinol is an Israeli company incorporated nine years ago by the Richters together with the Russian scientist Gregory Pinchasik and the urologist Dr. Benad Goldwasser. The company developed a stent, which is a kind of a spring used to expand the arteries of the heart in catheterization surgery. The stents market is a huge market, with a turnover of over 2 billion dollars per annum (in 1998 this market yielded 1.75 billion dollars and is growing by approximately 15% annually).

In 1995 Boston Scientific joined the company as a minority partner, purchasing 11% of the company at a huge sum for those days - 350 million dollars (thereafter it increased its holdings at Goldwasser's expense to 22%). Under the Agreement Medinol was to be the exclusive supplier of stents to Boston, and Boston was to be the exclusive distributor of Medinol's stents - all up to 2005.

The partnership operated excellently, at least in the beginning: in 1998, the best year, Medinol's product, named "NIR" brought Boston a 39% market segment in the American stents market - namely sales of nearly one billion dollars. Medinol's share of the loot was very large - royalties of approximately 23%. Its revenues for this year were valued at ca. \$ 250 M and its profits at ca. \$ 100 M. Big money.

Medinol's profitability, according to estimates, is very high; the company employs only 150 workers and the management is limited. Thanks to its unique production technology, developed by Richter, it succeeded in reducing production costs by a significant percentage in comparison with its competitors. Richter apparently brought this technology from the first company he established - Orbotec, engaged in testing equipment for the printed circuits market.

However, in the course of the last year a rapid deterioration took place in the relationship of both companies, and Boston's market segment in the stents market dropped to only 17%. Media reports stated that the reason was the failure to introduce new stents produced by Medinol into the market. Medinol accused Boston of not developing delivery systems for the new stents and thus withholding their introduction into the market. This brings us to April 2000 and to the brutal negotiations for the full purchase of Medinol by Boston.

The amounts mentioned during the negotiations ranged from 1 billion dollars to the inconceivable amount of 8 billion. Nonetheless, the parties failed to conclude the transaction successfully. The bad feeling between them, the embarrassing situation, and primarily the uncompromising insistence on the part of the Richters, all led eventually to the blowing up of the negotiations, both parties going to court, exposing all their dirty laundry and a tremendous legal struggle, in which the best and most expensive attorneys in New York took part.

This turn took place at the beginning of April this year, when Medinol filed a lawsuit in the Federal Court of the Southern County of New York claiming that already in 1997 Boston had commenced operations with a view to plundering its intellectual property.

Review of the Complaint shows that pursuant to the distribution agreement between Medinol and Boston Scientific, Medinol was required to supply to its partner an alternative production line, for operation where the Jerusalem production line was unable to supply the required quantity. At the same time, the agreement prohibited Boston from producing more than 500 stents monthly using this line, with a view to maintaining production capacity.

In 1997 Medinol transferred the alternative production line to Boston Scientific in Ireland. Medinol contends in its claim that Boston copied the machines in order to create for itself its own production line and thus to cut itself off from its dependency on Medinol. As stated above, the company set up by Boston was given the picturesque name BBD. Later on the project name was changed to Independence and at times was referred as Project "Harmony".

Medinol further contends in its claim that in order for the plot to be successful, Boston attempted to deceive the authorities and present Medinol as the supplier of a certain "component". Correspondingly, it submitted documents evidencing that BBD

was also a supplier of the same component, thereby in fact wishing to swap the two "suppliers".

Why in fact did Tobin give Richter the ammunition used by him against Boston Scientific? The answer to this remains unclear. It may be that he had no choice: the whole affair was about to be discovered in view of the demand of Medinol's firm of auditors, Earnest & Young, to expose BBD's true face. And maybe this move stemmed from the belief that by doing so he would be able to put back in track the relationship between the two interdependent companies. If that's what he thought, he, as aforesaid, was wrong.

The Marker obtained some of the central documents to the claim. Several of these are printed here below:

1.

From: Scovil, Brian

To: (partial list) Brown, Brian; Miller, Matt;, Schabel, Bill; Mullins Bob.

Sent: October 29, 1998

Subject: RE: Oct 27th Project Prioritization.

Gang, when discussing the new stent project priority list with others, please cross off part of priority #1 project name "BSIL Stent Capacity", this is a very sensitive subject and should not be discussed openly...

2.

From: Paidosh, Stephen

To: Flanagan, Aiden; Heeghan, Denise; Stenzel, Eric

Sent: 9 February 1998 17:43

Subject: BBD Prints

Importance: High

Guys, I think we should false sign these prints. Eric you should sign your name but we should use alias for the rest of us. Can you send new copies and everyone pick a new name to sign them with.

3.

From: Stenzel, Eric

To: (partial list) Heneghan, Denise; Redmond, Paul; David, Toohey; Champaud, Phillippe.

Denise Heneghan arranged for a meeting with Peter Cohen, a consultant working for Jim Tobin, to discuss project harmony and Scimed's (the department responsible for stents in Boston Scientific in the United States) laser objectives.

This meeting started off with a presentation by Denise of the project history to date and our concerns that all pertinent information was not being properly channeled through Scimed to senior management.

Peter was then taken through the BSC NIR line and shown the manufacturing process used by Medinol. This was followed by a visit to BBD where the secret capacity was demonstrated. In particular, the more efficient manual welding method....

Peter was very impressed with what he saw, both the actual company having contingency plans in place for supply disruption and with the processing ability and speed of manufacturing operations.

In summary, things looked very positive for BSIL and he (Cohen) was very impressed. He did seem taken back that the laser cut NIR® products in Scimed was not disclosed to him as the NIR® stent is a critical item to the corporation and said that "this seemed to complete the picture for him".

He was asking if Jim Taylor was informed about this project as he would like to discuss this issue with him during his visit this week. I am not aware of this and could not confirm.

To follow up on this, I would like to propose that Jim Taylor is given a tour of project Harmony if appropriate. As Paul La Violette he was very supportive of the laser cut stent during his last visit, it may be beneficial to show our process capabilities to senior management to ensure that we are included in future planning (and funding).

4.

From: Toohey, David

To: Champaud, Phillippe; Lydon, Emmet; Heneghan, Denise; Redmond, Paul; Stenzel, Eric.

Date: 19 October 1999, 9:36

Subject: RE: Meeting with Peter Cohen

Sensitivity: Confidential.

Eric,

(...)

Given that this project has always been on a "need to know" basis and has a potentially catastrophic impact on our relationship with Medinol it is absolutely essential that we treat it as such. To my knowledge there are several members of the EC who are unaware of this initiative. It is not our job to share this stuff with anyone without express approval from a senior VP.

I will ask Bernard whether it is appropriate to share this project with Jim Taylor or not...I imagine that we will be doing so, but I do not want to jump to any conclusions.

5.

From Heneghan, Denise

To: (same as above)

Sent: 29 October 1999 09:53

Subject: RE: Meeting with Peter Cohen

Sensitivity: Confidential

Folks, I have to say this was entirely my fault, not Eric's, or indeed, anyone else's.

At an initial meeting with Peter, we were being very circumspect in what we were telling him, being unsure of our brief. I subsequently attempted to check whether or not it was appropriate to be completely frank with Peter Colen as a vehicle for communications, and understood that it was. In retrospect I should have double checked and treble checked specifically on the Harmony issue. Sincere apologies here, not that an apology is much use, but it was my initiative, and I enlisted Eric, having told him I had o.k'd it.

6.

From: Champeud, Phillippe
Sent: Wednesday, October 20, 1000 07:10
Subject: RE: Meeting with Peter Cohen
Sensitivity: Confidential

Thanks Denise for your position. I appreciate it. I also sincerely hope what you've done will in the end serve our cause (BSIL's), sometimes you have to go beyond the limits to get results! We should make sure that Peter only feedbacks what he learned about Harmony to Jim Tobin only until we get more info re: Jim Talyor.
Daniel Rosing [drosing@netvision.net.il]

7.

From: Paidosh, Stephen
Sent: 25 February 1999
Subject: Stent Manufacturing

Many people in BSIL are not aware of project Independence but are receiving e-mails from folks in SciMed on this topic. Eric and I spent an increasing amount of time telling white lies about this activity to our people to keep them in the dark. The problem is they will buy it once but they continue to get e-mails that reference BBD or alternative panels, etc. Pete Nicholas (President of Boston Scientific) hasn't decided how far he wants to take this so it would be a shame for Medinol to learn of the initiative. The people copied on this e-mail know about this and have a responsibility to maintain control. Please talk to anybody you have told other than on this lists and stop the flow of info.

(...)

8.

From: Stenzel, Eric
Sent: 12 April 1999 13:31
Subject: BBD Quality

Denise & Helen,

As discussed previously, we are adding BBD to the BSIL approved vendor list. I received a request from BSIL purchasing to complete a supplier survey.

To make everything look legitimate (as much as possible) I began drafting a quality manual based on the ISO 9001 standard- I did not want it to be highly visible to an auditor (internal or external) that we started buying key items from a “cowboy” vendor. The inclusion of official quality procedures with the survey should assist in this.

I hope to have this completed by tomorrow and would appreciate a quick review as I have to send return the supplier survey ASAP.

As a note, these procedures will be followed and records maintained should we come alive and officially start supplying BSIL.