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FTC Continues Active Enforcement with Decision to Block Hospital Merger in Toledo, Ohio

Although the challenging and dynamic environment facing many hospitals and the requirements of the Affordable Care Act might suggest that the Federal Trade Commission ("FTC") will displace or rethink traditional antitrust analysis for hospital mergers, the FTC recently made clear that any hospital merger resulting in high market shares faces a steep uphill climb to win FTC approval.

During the same week that the constitutionality of the Affordable Care Act was being argued before the Supreme Court, the FTC, on March 28, 2012, announced its decision to block ProMedica Health System acquisition of St. Luke's Hospital ("ProMedica" and "St. Luke's"). To view the decision, please **click here**.

The ProMedica decision continues the agency's active enforcement in the hospital area. In March 2012, the Solicitor General, at the request of the FTC, filed a petition for certiorari in the *Phoebe Putney* case, seeking to have the Supreme Court consider whether the State Action Defense protects, from antitrust scrutiny, an otherwise anti-competitive acquisition by a government-owned hospital, where the hospital is leased to and operated by a private entity. To view *Phoebe Putney*, please **click here**. In addition, the agency obtained a preliminary injunction blocking a hospital acquisition in Rockford, Illinois pending an administrative trial. To view an FTC statement on this ruling, please **click here**.

Background

In May 2010, ProMedica and St. Luke's entered into an agreement whereby St. Luke's became part of the ProMedica System. Internal St. Luke's documents made clear that one of the reasons for the affiliation was to improve the rates that St. Luke's was able to negotiate with Managed Care Organizations ("MCOs").

In July 2010, the FTC began an investigation of the transaction. In August 2010, the parties entered into a "hold separate" agreement that allowed the deal to close but prevented ProMedica from renegotiating health-plan contracts or raising the rates it charged to health plans. In January 2011, the FTC issued an administrative complaint against ProMedica challenging the acquisition, and the FTC also filed suit in the U.S. District Court for Northern District of Ohio seeking a temporary restraining order and preliminary injunction to maintain the parties hold separate agreement, which was set to expire. In March 2011, the court entered a preliminary injunction ordering the parties to maintain the hold separate agreement pending the outcome of the FTC's administrative litigation.

In its Complaint, the FTC alleged that the acquisition would result in ProMedica controlling 60 percent of a market for general acute care inpatient hospital services and 80 percent of a market for inpatient OB/GYN services in the Lucas County, Ohio area. The FTC alleged that these high market shares rendered the acquisition presumptively illegal under Section 7 of the Clayton Act and that the acquisition was likely to substantially reduce price and quality competition between St. Luke's and ProMedica.

The FTC conducted the administrative litigation under its revised Part 3 rules, which were updated in 2009 to expedite the resolution of merger challenges. This was the first case litigated to a conclusion under those revised rules. The FTC's Administrative Law Judge ("ALJ") held an evidentiary hearing beginning in May 2011, and issued his Initial Decision concluding that the deal violated Section 7 of the Clayton Act in December 2011.

The Litigation and the FTC's Decision

Although the FTC and ProMedica quibbled on the edges regarding proper market definition, ProMedica's principal defenses focused on rebutting the presumption of competitive harm that allegedly flows from its high post-deal market share. The FTC ultimately rejected those arguments. At the evidentiary hearing, ProMedica argued that the efficiencies and pro-competitive benefits resulting from the transaction outweighed any anti-competitive harm. The ALJ found the efficiencies evidence insufficient, and ProMedica did not raise that issue on appeal. ProMedica also argued that St. Luke's was a financially weak and limited competitor so that the deal did not cause significant harm to competition. Both the ALJ and the Commission rejected this argument.

The weakened competitor or "flailing firm" defense is raised frequently in the current economic climate, and so it is important to understand the FTC's view of it. In assessing this evidence, the FTC noted that ProMedica needed to meet "an extremely heavy burden" to show that St. Luke's was so weak that its combining with ProMedica was not of concern. The FTC held that ProMedica would have to show that: (1) St. Luke's was so weak that its market share would likely soon reduce to a level that combining with ProMedica would not be a concern; and (2) the weakness could not be resolved by other means. In its decision, the FTC acknowledged that due to declining reimbursements from government payers and relatively poor rates with commercial payers, St. Luke's combined reimbursements did not cover its costs for providing care. Nevertheless, the FTC found that the evidence showed that St. Luke's condition had been improving with new management and that its market share was improving. In addition, the FTC found that ProMedica had not shown that it was the only option available to improving St. Luke's, and the FTC pointed to the possibility of St. Luke's improving its rate structure without joining ProMedica or an out-of-area entity affiliating with St. Luke's.

The FTC also rejected ProMedica's argument that testimony from MCOs that the acquisition would lead to higher prices was unreliable. Citing *Oracle* and *Arch Coal*, ProMedica argued that this testimony was not supported by any market studies or other objective support. The FTC disagreed, and distinguished the testimony before it from that criticized in *Oracle* and *Arch Coal*, finding the testimony was not speculative but rather based on real world examples of prior competition and pricing behavior by St. Luke's and ProMedica. To view *Oracle*, please **click here**. To view *Arch Coal*, please see 329 F. Supp. 2d 109 (D.D.C. 2004), appeal dismissed per curiam, No. 04-5291, 2004 WL 2066879 (D.C. Cir. Sept. 15, 2004).

The FTC and ProMedica also differed on the ability of MCOs to constrain ProMedica's pricing post-affiliation. While noting that MCOs do have some leverage in their negotiations with hospitals, the FTC found that MCOs would not be able to build a commercially viable network of hospitals without ProMedica after the acquisition, giving ProMedica the leverage to raise prices. Similarly, the FTC noted that ProMedica's arguments that MCOs could steer patients away from ProMedica to discipline any effort by ProMedica to raise prices was undercut by evidence that steering was ineffective and that ProMedica's contracts prohibited MCOs from such steering.

Remedy

To remedy the violation, the FTC ordered ProMedica to divest St. Luke's either to a new purchaser or to a newly constituted St. Luke's. In doing so, the FTC rejected ProMedica's argument that the proper remedy, if a violation was found, was to require St. Luke's to create a separate and discrete negotiating team for reimbursement negotiations with MCOs, but to otherwise let ProMedica and St. Luke's affiliate and integrate. The Commission previously adopted this type of conduct remedy in its challenge to Evanston Northwestern Healthcare Corporation's acquisition of Highland Park Hospital. To view materials related to *Evanston*, please **click here**. In urging this remedy, ProMedica argued that, absent an affiliation, St. Luke's would be unable to meet the requirements of the Affordable Care Act and the dynamic healthcare marketplace. The FTC, however, found that prior to the affiliation St. Luke's had enjoyed a reputation as a high-quality, low-cost provider, which put St. Luke's in the right position to prosper under the Affordable Care Act.

What Does it Mean

Despite the Affordable Care Act's influence upon an uptick in hospital mergers, the FTC is not signaling any leeway regarding traditional merger requirements. Hospitals seeking to engage in mergers and acquisitions, particularly those between close competitors, should continue to retain experienced counsel.

If you have any other questions regarding this or other antitrust concerns, please contact one of the attorneys in our Antitrust Practice Group at **www.Venable.com/Antitrust-practices**.