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Administrative Law Judge Upholds FTC
Complaint Ordering Evanston
NorthwesternHealthcare Corporation to
Unwind Five-Year-Old Acquisition

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Administrative Law Judge Upholds FTC Complaint Ordering Evanston NorthwesternHealthcare Corporation to Unwind Five-Year-Old Acquisition

James Lowe and Alexander Krulic

Abstract

On October 21, 2005, the Federal Trade Commission (FTC) announced that Administrative Law Judge Stephen J. McGuire had ordered Evanston Northwestern Healthcare Corporation (ENH) to divest Highland Park Hospital, located in a Chicago suburb. (The decision can be found at <http://www.ftc.gov/os/adjpro/d9315/051021idtextversi.pdf>.) ENH had acquired Highland Park five years ago for \$200 million. In an administrative complaint issued in February 2004, the FTC alleged that the acquisition had resulted in “substantially lessened competition” and higher prices for insurers and healthcare consumers for general acute care inpatient services sold to managed care organizations. In upholding part of the complaint, Judge McGuire evaluated post-acquisition evidence that “ENH exercised its enhanced post-merger market power to obtain price increases significantly above its premerger prices and substantially larger than price increases obtained by other comparison hospitals.” (ENH has filed notice that it will appeal the judge’s initial decision to the full Commission.)



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Administrative Law Judge Upholds FTC Complaint Ordering Evanston Northwestern Healthcare Corporation to Unwind Five-Year-Old Acquisition

On October 21, 2005, the Federal Trade Commission (FTC) announced that Administrative Law Judge Stephen J. McGuire had ordered Evanston Northwestern Healthcare Corporation (ENH) to divest Highland Park Hospital, located in a Chicago suburb.¹ (The decision can be found at <http://www.ftc.gov/os/adjpro/d9315/051021idtextversion.pdf>.) ENH had acquired Highland Park five years ago for \$200 million. In an administrative complaint issued in February 2004, the FTC alleged that the acquisition had resulted in “substantially lessened competition” and higher prices for insurers and healthcare consumers

for general acute care inpatient services sold to managed care organizations.² In upholding part of the complaint, Judge McGuire evaluated post-acquisition evidence that “ENH exercised its enhanced post-merger market power to obtain price increases significantly above its premerger prices and substantially larger than price increases obtained by other comparison hospitals.”³ (ENH has filed notice that it will appeal the judge’s initial decision to the full Commission.)

Judge McGuire’s decision is notable for two reasons. First, it reverses a “string of government losses in hospital

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1. In the Matter of Evanston Northwestern Healthcare Corporation and ENH Medical Group, Inc., Initial Decision, Oct. 20, 2005, Docket No. 9315, *available at* <http://www.ftc.gov/os/adjpro/d9315/051020initialdecision.pdf>. See *also*, FTC Press Release, Administrative Law Judge Orders Evanston Northwestern Healthcare Corporation to Sell Highland Park Hospital, Oct. 21, 2005, *available at* <http://www.ftc.gov/opa/2005/10/evanston.htm>.

2. In the Matter of Evanston Northwestern Healthcare Corporation and ENH Medical Group, Inc., Complaint, Feb. 10, 2004, Docket No. 9315, *available at* <http://www.ftc.gov/os/caselist/0110234/040210emhcomplaint.pdf>.

3. In the Matter of Evanston Northwestern Healthcare Corporation and ENH Medical Group, Inc., Initial Decision, p. 1.

merger cases over the last decade.”⁴ Second, and more notably for those outside the hospital field, the decision is a stark reminder that merging parties are not immune from antitrust scrutiny after their deal closes. Under Section 7 of the Clayton Act, the US antitrust agencies retain authority to investigate transactions after they close. Indeed, they retain this authority even when the agencies had previously cleared the transaction in the Hart-Scott-Rodino review process. And the agencies can seek divestiture of the acquired assets or other remedies if the merger is found to have resulted in anticompetitive effects.

I. Hospital Mergers

The government had previously challenged several hospital mergers based on arguments about probable anticompetitive effects, but had lost most of those cases. By contrast, here, the FTC presented evidence of actual price increases post-merger. The transaction combined ENH’s two hospitals in the northern Chicago suburbs (Evanston and Glenbrook) with Highland Park Hospital, the nearest hospital north of them. Judge McGuire found that as a result of ENH’s acquisition of Highland Park and elimination of it as a competitor, ENH increased its rate structures for managed care organizations above what any of the hospitals could have achieved themselves absent the acquisition.

Judge McGuire wrote, “[A]s soon as the merger was consummated, [ENH] began using its enhanced market power to impose significant price increases on managed care organizations, and ultimately consumers.”⁵ Further, he found that ENH continued unilaterally to raise its rates in 2002 and 2003, such that it “significantly increased the prices paid by managed care organizations for ENH services.”⁶ Judge McGuire concluded that the FTC’s evidence effectively ruled out factors other than the exercise of market power as explaining the price increases.⁷ The administrative law judge’s decision may encourage the FTC to bring pre-closing challenges to future hospital mergers, despite the Commission’s losing streak in the courts. The FTC now has a useful precedent where a decisionmaker found actual anticompetitive effects based on post-closing evidence. The Commission may determine that this precedent (and empirical evidence about competitive harm from completed hospital mergers) will make courts more willing to enjoin acquisitions than they had been based on the FTC’s traditional arguments about likely post-closing competitive effects.

II. A Broader Message

Although the US antitrust agencies conduct the vast majority of their reviews of large mergers and acquisitions prospectively through the Hart-Scott-

4. In the Matter of Evanston Northwestern Healthcare Corporation and ENH Medical Group, Inc., Initial Decision, p. 137. In many of those cases, courts found that the government had failed to prove a relevant geographic market within which the merger would harm competition. *Id.* at 137-8, citing *Tenet Health Care* 186 F.3d at 1053 (characterizing the FTC’s failure to produce sufficient evidence of a well-defined relevant geographic market as fatal to the government’s claim); *Freeman Hosp.* 69 F. 3d at 272 (describing the FTC’s failure to meet its burden of establishing the relevant geographic market as dispositive); *Mercy Health Serv.*, 902 F. Supp. at 987 (“The government has failed to establish the relevant geographic area and hence has failed to establish that the merger. . . will likely result in anticompetitive effects.”).

5. *Id.* at 166.

6. *Id.* at 1.

7. *Id.* at 2.



Rodino (HSR) Premerger Notification process,⁸ Judge McGuire's decision to force ENH to divest Highland Park Hospital serves as a reminder that they can also review transactions post-closing.

In another post-closing review, the FTC sued The Hearst Corporation in 2001 for disgorgement of monopoly profits from the acquisition by its subsidiary First Data Bank of Medi-Span. First Data Bank and Medi-Span owned the two commonly used drug information databases. Although the transaction had closed in 1988, evidence that the combined entity significantly raised prices after the transaction led the Commission staff to conduct a post-closing investigation. The FTC found that the deal created a monopoly in the sale of drug information databases, and that First DataBank used that monopoly power substantially to increase prices to all database customers. To settle charges, Hearst ultimately agreed to disgorge \$19 million in profits and divest the Medi-Span business.⁹

Hearst's troubles were compounded by the FTC's findings that Hearst had failed to include certain significant 4(c) documents in its HSR filing for the transaction.¹⁰ Indeed, this HSR violation likely contributed to the FTC's

decision to challenge the transaction over a decade after closing. The FTC's investigation of ENH, however, appears to be driven solely by the post-closing price increases that ENH instituted.

Other recent examples of post-closing reviews by the agencies include Chicago Bridge & Iron and Aspen Technologies. In October 2001, the FTC filed a complaint seeking to undo Chicago Bridge & Iron Company's February 2001 acquisition of Pitt-Des Moines, Inc. According to the FTC's complaint, the transaction resulted in a monopoly in markets for LNG tanks and thermal vacuum chambers. In addition, the complaint alleged that the combination created a dominant firm in the US markets for LPG tanks and LIN/LOX/LAR tanks.¹¹ An administrative law judge held the acquisition unlawful, and the full Commission upheld the decision in December 2004.¹²

The Aspen Technologies case involved a post-closing challenge to an acquisition that was not reportable under the HSR Act. In August 2003, the FTC filed an administrative complaint alleging that software developer Aspen Technologies's May 2002 acquisition of Hyprotech for \$106 million violated the Clayton Act. The FTC sought divestiture of

8. Pub. L. No. 94-435, 90 Stat. 1383 (1976). The premerger notification provisions are in Section 7A of the Clayton Act, 15 U.S.C. 18a.

9. FTC Press Release, Hearst Corp. To Disgorge \$19 Million and Divest Business to Facts and Comparisons to Settle FTC Complaint, Dec. 14, 2001. Available at <http://www.ftc.gov/opa/2001/12/hearst.htm>.

10. *Id.*

11. In the Matter of Chicago Bridge & Iron Company N.V., Chicago Bridge & Iron Company, and Pitt-Des Moines, Inc., Administrative Complaint, Oct. 25, 2001, FTC File No. 011 0015, Docket No. 9300 available at <http://www.ftc.gov/os/2001/10/chicagobridgeadmincmp.htm>.

12. FTC Press Release, Administrative Law Judge Upholds Allegations of Anticompetitive Acquisition by Chicago Bridge & Iron Company, June 27, 2003, available at <http://www.ftc.gov/opa/2003/06/cbi.htm>. The case is currently on appeal to the 5th Circuit. In re Chicago Bridge & Iron Co., Docket No. 9300, 2004 WL 3118878 (FTC Dec. 21, 2004), petition for review filed (5th Cir. Mar. 10, 2005).

Hyprotech to restore competition in the market for engineering simulation software.¹³ Aspen eventually agreed to a consent order requiring divestiture of certain Hyprotech assets.¹⁴

The agencies do not take lightly decisions to challenge transactions that have already closed.¹⁵ One of the most significant advantages of the HSR Premerger review process is to reduce the business and market uncertainties caused by post-closing challenges to transactions.¹⁶ It is both costly and disruptive to force a company to divest assets that have been integrated into the operations of another business. By contrast, under the HSR process, firms generally know before closing whether a particular transaction will be challenged. They can then make informed decisions whether to negotiate a settlement, abandon the transaction, or litigate.¹⁷ As importantly, the antitrust agencies have an opportunity to challenge transactions before closing, after which it will often be difficult or impossible to impose remedies that effectively restore competition.

Post-closing investigations generally begin when customers or competitors of the merged entity report potential anticompetitive behavior to one of the antitrust agencies. The agencies will

then investigate whether there have been significant price increases or other anticompetitive effects attributable to the transaction.¹⁸ To decide whether to issue a complaint, the agency determines whether any anticompetitive effects resulted from the transaction or whether they were caused by some exogenous factor (such as increases in input costs). In essence, the analysis is whether the merger, itself, harmed competition. Unlike with pre-closing investigations, the agencies have the benefit of hindsight.

Although the US antitrust agencies have challenged relatively few transactions post-closing, they have conducted many more investigations that did not lead to challenges. Even an investigation that does not lead the agency to file a complaint can be very costly. The agency typically issues a Confidential Information Demand (CID), which typically calls for a voluminous document production and formal responses to questions that can demand time and attention from key employees.

Finally, premerger HSR notification does not provide a safe-harbor against post-closing review. Although the agencies may be slightly more reticent to challenge a consummated merger that they have already reviewed through the HSR process, their clearance letters to

13. Aspen Technologies, Inc., Administrative Complaint, Dec. 20, 2004, Docket No. 9310 *available at* <http://www.ftc.gov/os/2003/08/aspencmp.pdf>.

14. FTC Press Release, FTC Orders Aspen Technology, Inc. to Divest Assets from its 2002 Purchase of Hyprotech, Jul. 15, 2004, *available at* <http://www.ftc.gov/opa/2004/07/aspen.htm>.

15. See, e.g., William J. Baer, "Reflections on 20 Years of Merger Enforcement under the Hart-Scott-Rodino Act," Prepared Remarks before The Conference Board, Oct. 29, 1996 at fn 58.

16. Congress intended the HSR Act to alleviate the inefficiency of post-merger review. See *FTC v. H.J. Heinz Co.*, 246 F.3d 708, 726 (D.C. Cir. 2001), citing 119 Cong. Rec. 36612 (1973).

17. *Id.*

18. See, e.g., In the Matter of Chicago Bridge & Iron Company, Administrative Complaint, *cited supra*; Aspen Technologies, Inc., Complaint, Dec. 20, 2004, Docket No. 9310, *available at* <http://www.ftc.gov/os/2003/08/aspencmp.pdf>; MSC Software Corp., Complaint, Aug. 14, 2002, Docket No. 9299 *available at* <http://www.ftc.gov/os/2002/11/mscdo.pdf>.



merging parties on completion of HSR review are only a statement of present intention not to challenge the proposed transaction. The agencies reserve the right to revisit the decision if post-merger evidence suggests that the combined firm has exercised market power as a result of the transaction.¹⁹ Whether they do so will generally turn on factors such as the quantum of anticompetitive effects from the transaction, the number and force of complaints, and whether there is an available remedy that is likely to restore lost competition.

In addition, it is possible for states to challenge closed transactions under their own or federal law and for private parties to bring suits post-closing under Section 7 or analogous state laws. Although challenges by state authorities have been rarer in recent years, private challenges to mergers

have been more common (but such challenges have rarely been successful).

The Evanston Northwestern Healthcare case stands as a reminder not to confuse the closing of a transaction with an exemption from further antitrust scrutiny. Merging parties should be cognizant that sharply raising prices or other post-closing conduct that may agitate consumers or other market participants can create risks of a burdensome and expensive antitrust investigation as well as unwinding of the transaction and other remedies.

James Lowe and Alexander Krulic authored this update.

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19. The Clayton Antitrust Act also permits private challenges mergers that violate Section 7, 15 U.S.C. §§ 12 et seq. (1914).