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Recent Enforcement Actions: Hospital Mergers [Ober|Kaler]

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Rockford Hospitals Abandon Merger After Preliminary Injunction Order

The proposed acquisition by OSF Healthcare System (OSF) of Rockford Health System (Rockford) is abandoned after the United States District Court for the Northern District of Illinois grants the FTC's request for a preliminary injunction. According to the opinion by Judge Kapala, the claimed efficiencies appeared too speculative at this point in the litigation to over come the FTC's strong prima facie case. *See Federal Trade Commission v. OSF Healthcare System and Rockford Health System*, No. 11C50344 (N.D. Ill. Apr. 5, 2012).

The administrative complaint in this matter identified concerns in both the hospital and physician services markets, and the FTC alleged that the merger is "presumptively unlawful by a wide margin." *See OSF Healthcare System and Rockford Health System*, 111 FTC 0102 (2011). According to the FTC, OSF/Rockford's post-merger market share in the market for general acute-care inpatient hospital services would be 64 percent, and the merger would increase the Herfindahl-Hirschman Index (HHI) by 2032. In addition, the FTC alleged that post-acquisition, OSF/Rockford and SwedishAmerican would be the only two competitors left in the market, controlling 99.5 percent of the Rockford hospital market, thus increasing the likelihood of, and incentive for, coordinated interaction. The FTC further alleged that the post-merger health system would control 37.4 percent of the primary care physician market; the HHI index would increase by 696. According to the FTC, the merger will reduce the number of hospital-employed physician groups from three to two in the Rockford region and leave the remainder of the market highly fragmented with small independent physician practices.

In its Complaint, and in papers seeking preliminary injunction, the FTC alleged that the parties' claimed efficiencies were unreliable, unfounded, and "made-for-litigation," and thus did not constitute the "extraordinary" efficiencies required to justify a merger with "vast potential" to harm competition. Ultimately, and after making it clear that the finding was for purposes of the FTC's request for preliminary injunction and not a ruling on the ultimate merits, the Court agreed.

ProMedica Ordered to Divest St. Luke's After Efficiencies and Flailing Firm Defenses are Rejected

In a 4–0 decision written by Commissioner Julie Brill and handed down on March 22, 2012, the FTC ordered Toledo-based ProMedica Health System (ProMedica) to divest St. Luke's within six months of its decision finding the transaction would harm competition. *In the Matter of ProMedica Health System, Inc.* Docket No. 9346. The Opinion of the Commission adopted in large measure the Findings of Fact and Conclusions of Law of the Initial Decision by the ALJ. See Administrative Law Judge's Initial Decision, *ProMedica Health System, Inc.*, 101 FTC 0167, at 114. (Dec. 12, 2011). Less than a week later, in a 115-page opinion containing its own findings of fact and conclusions of law, Judge Katz of the United States District Court for the Northern District of Ohio granted the FTC a preliminary injunction preventing ProMedica from further consolidating its operations with St. Luke's Hospital. *See* Judgment Entry, *Fed. Trade Comm. v. Promedica Health System, Inc.*, No. 3:11CV47 (N.D. Ohio Mar. 29, 2011).

In March 2010, ProMedica executed a joinder agreement with nearby St. Luke's Hospital. The parties' stated purpose for the merger was to adapt to health care reform by clinically integrating St. Luke's into the ProMedica system to achieve CMS's goals of higher-quality and lower-cost health care services.

The FTC filed an administrative complaint in opposition to the merger, alleging that ProMedica and St. Luke's joinder substantially would harm competition and lead to increased prices for general acute-care inpatient hospital services in the Toledo, Ohio area. Administrative Complaint, ProMedica Health System, Inc., 101 FTC 0167 (2011). Contemporaneously, the FTC filed a lawsuit in the United States District Court for the Northern District of Illinois seeking a court order to enjoin the merger pending the outcome of the administrative hearing.

To justify the merger, ProMedica argued both in the district court and in the administrative hearing that health care reform (specifically, the movement toward clinical integration) spurred the merger. ProMedica maintained that even if there was a presumption of anticompetitive effects, they would be outweighed by the resulting efficiencies. For example, ProMedica set aside $10 million for strategic capital for St. Luke's for the year 2011, part of ProMedica's commitment to invest $30 million in St. Luke's over three years. ProMedica committed to use its capital investment for projects at St. Luke's, including adding 17 additional private rooms, converting additional semi-private rooms to private rooms, updating St. Luke's IT systems to comply with "meaningful use" IT requirements, constructing an outpatient lobby, renovating the health center, moving administrative services, expanding surgical areas, and increasing the private postpartum area and well infant nursery.

ProMedica also argued that its acquisition of St. Luke's would not harm competition substantially because St. Luke's financial hardships made it a "flailing firm." In support of its position, ProMedica pointed to historical evidence of St. Luke's precarious financial position. ProMedica, on the other hand, was flush with cash and stood ready to inject capital into St. Luke's.

Despite recognizing certain benefits to the transaction, both the ALJ and the United States District Court held that ProMedica's proposed efficiencies were insufficient to legally justify the transaction, and that its flailing firm defense was insufficient to carry the day. Thus, ProMedica had not met its burden of showing "extraordinary" procompetitive benefits or that the asserted efficiencies would offset the likely anticompetitive effects of the increase in market power produced by the merger.

Observations

These decisions are consistent with the FTC's various public statements rejecting efforts by the industry to rely on health care reform as a defense to an otherwise unlawful transaction. They also highlight the FTC's continuing and fundamental reliance on market share and concentration measures as its primary method of assessing a merger's competitive effects. Reliance on efficiencies, and a flailing firm defense, also requires detailed, credible and concrete facts in order to overcome any rebuttable presumption that might be created by a transaction involving significant market shares and resulting increased market concentration. Similarly, to the extent the merging parties can prepare and document credible efficiencies intended to meet the goals of health care reform, this will increase the likelihood that the FTC will accept such efficiencies, and in turn, increase the likelihood that the merger will be cleared.