MERGER ANTITRUST LAW

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Tuesdays and Thursdays, 3:30-4:55 pm
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READING GUIDANCE

Class 13 (October 17): Sanford Health Mid Dakota Clinic (Unit 9)

In the first part of the course we examined antitrust institutions (the substantive statutes, the federal enforcement agencies and other potential plaintiffs, the DOJ/FTC merger review process under the HSR Act, merger antitrust litigation, and settlements of investigations and litigations), developed a model for predicting antitrust challenges and enforcement outcomes in the context of these institutions, used this model to assess the inquiry, substantive and relief risk in transactions, and then used this risk assessment to inform the negotiations on behalf of a buyer or seller on various provisions in the merger agreement in order to allocate this risk.

We are now shifting into the second part of the course: the formal analysis of mergers found in the DOJ/FTC Horizontal Merger Guidelines and in court opinions. We will focus primarily on horizontal mergers, which by far constitute the majority of merger antitrust investigations and challenges, although we will discuss the formal analysis of potential competition and vertical mergers in the last three classes.

As we have discussed, effective advocacy—either as a prosecutor or defense counsel—depends on capturing both the "heart" and "mind" of the decision-maker, whether that be the ultimate decision-makers in the DOJ or FTC or a federal court judge. Consider, for example, advocacy before a federal district court judge. Capturing the judge's heart means successfully appealing to the judge's judgment, experience and common sense that the position you are advocating is the one that best serves justice. This will make the judge look for ways to find in your favor. Capturing the judge's mind means providing the judge a way to justify the outcome that you are advocating that is consistent with the prevailing analytical paradigm and governing judicial precedent. More to the point, ideally you should provide the judge with legal arguments and supporting evidence that the judge can incorporate into her opinion that will make the judge look like a scholar to the bench and bar, is likely to be regarded as a model by other judges writing opinions in future cases, and (by no means least) will not be reversed on appeal. Prosecutors, of course, do not have to justify their decisions in formal written opinions, but they do have to be prepared to make their case before a judge, who in turn will have to write an opinion. The bottom line: even if you capture the "heart" of the decision-maker and convince them you have "right" on your side, you may still lose if you cannot provide the "mind" with an acceptable way to justify a decision in your favor. We will spend the rest of the course on the "mind" part of this equation by examining how modern judges in fact justify the outcomes they reach.

As a quite aside, when writing briefs, the fact section should be written not only to provide the factual predicates for the theory of the case but also to provide a compelling narrative to capture the "heart" of the judge. The argument section is more intended to speak to the "mind" of the judge. If the judge is not convinced that you have right on your side by the time the judge has finished reading the fact section, you have a problem.

This brings us to our first merger antitrust decision in the course. The transaction involves the proposed acquisition by Sanford Health of Mid Dakota Clinic, P.C. We will read only the Eight Circuit's opinion affirming the district court. The facts are easily understood and largely uncontested, and the appellate opinion is straightforward and short (which is why it is our first opinion). That said, I expect you to spend the time to develop a deep understanding of the structure and reasoning of the opinion.[1] I assure you that the time will be an investment that will pay significant returns as the course proceeds.

Sanford Health is an integrated healthcare system operating in North Dakota and several other states.[2] In the Bismarck-Mandan region of North Dakota, Sanford operates an acute care hospital, eight primary care clinics, and several specialty clinics. It employs approximately 160 physicians in the region, including 37 adult primary care physicians (PCPs), five pediatricians, eight OB/GYN physicians, and four general surgeons. Sanford's two main competitors in the Bismarck-Mandan region are Mid Dakota Clinic (MDC) and Catholic Health Initiatives St. Alexius Health (CHI).

MDC is a multispecialty for-profit physician group that has nine clinics and one ambulatory surgery center in the region. MDC has approximately 60 physicians, including 23 adult PCPs, six pediatricians, eight OB/GYN physicians, and five general surgeons.

CHI operates CHI St. Alexius, the only other acute care hospital in the Bismarck-Mandan area. CHI employs approximately 88 physicians, mostly hospitalists.[3] Its physicians include five adult PCPs but no pediatricians, OB/GYN physicians, or general surgeons.

Physicians in the Bismarck-Mandan region

	Sanford Bismarck	Mid Dakota	CHI St. Alexius	Others
Adult PCPs	37	23	5	10
Pediatricians	5	6	0	1
OB/GYNs	8	8	0	1
General surgeons	4	5	0	0

On June 23, 2017, the FTC filed a complaint under Section 13(b) of the FTC Act in the Federal District court of the District of North Dakota alleging that the transaction, if consummated, would violate Section 7 of the Clayton Act by threatening to lessen competition in the provision of adult primary care physician, pediatric, OB/GYN, and general surgery physician services (each a separate relevant product market) to commercial insurers in the Bismarck-Mandan area

[1] The homework assignment will help you develop this understanding.

[2] An integrated healthcare system is one comprised of both hospital services and physician services and which sometimes also includes insurance companies and research and education components.

[3] A hospitalist is a dedicated in-patient physician who works exclusively in a hospital.

of North Dakota.[4] For relief, the FTC sought a temporary restraining order and a preliminary injunction to enjoin the consummation of the Sanford Heath/MDC merger pending a resolution of the merits in an FTC administrative proceeding. The State of North Dakota joined the complaint as a plaintiff alleging a violation of Section 7 and seeking similar relief under Section 16 of the Clayton Act.

To get your bearings, read the FTC's press release announcing the action (pp. 5-7) and the complaint (pp. 8-39). The introduction and Section I give a good summary of the theory of the case and it worth some attention (pp. 1-5). Feel free to just skim Sections II-IV (pp.5-14), but read the reminder of the complaint with a little more care (pp. 14-31). The complaint is more fulsome than many of the complaints we have seen. That is because the FTC knew that the case would be going to litigation, and the complaint is the FTC's first opportunity to capture the "heart" of the judge with well-developed and compelling factual allegations.

The parties stipulated to a TRO restraining the closing of the transaction until the end of five business days after the court ruled on the preliminary injunction (pp. 41-44). After a four-day evidentiary hearing with 16 witnesses, the district court found that the plaintiffs were likely to succeed in proving each of the four relevant product markets and the relevant product market alleged in the complaint. The court also found that the transaction would result in the merged firm controlling an undue percentage share of each relevant market and would create a significant increase in concentration in each market, thus entitling the plaintiffs to a presumption of the requisite anticompetitive effect under *United States v. Philadelphia National Bank*.[5] After reviewing additional evidence presented by the plaintiffs on the likely competitive effect of the transaction and rejecting the various defenses advanced by the parties, the court concluded that the FTC was likely to succeed in ultimately proving on the merits that the proposed transaction may substantially lessen competition in each of the four relevant physician service lines sold to commercial insurers in the Bismarck-Mandan area and that the public equities favor preliminarily enjoining the proposed transaction. Consequently, the court entered a preliminary injunction blocking the closing (p. 48). The same day the merging parties filed a notice of appeal, terminating the jurisdiction of the district court and transferring it to the court of appeals (p. 49).

I am going to ask you to read the Eight Circuit's opinion twice (pp. 58-67).

On the first read, try to get a good sense of the opinion's analytical structure. It will be helpful if you outline the topics so that you can literally see the flow on a sheet of paper. On this read, you are looking only for the topics, not trying to analyze how Judge Colloton resolved each issue.

Understanding the detail is the purpose of the second read. Now that you know how the opinion is organized, go back and study the details under each topic. In additional to understanding the applicable statutes that govern the substantive offense and that provide the FTC and North Dakota a cause of action, the questions on appeal, and the standard of review, be sure to concentrate on the following topics.

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[4] The FTC, as is its practice, also alleged that the entry into the merger agreement violated Section 5 of the FTC Act.

[5] 374 U.S. 321 (1963).

Product market definition. There are two complementary judicial "tests" for whether a product grouping—a "candidate" or "provisional" market is a relevant product market for the purpose of merger antitrust analysis under Section 7: the "outer boundaries" and "practical indicia" criteria set forth by the Supreme Court in *Brown Shoe Co. v. United States*[6] and the hypothetical monopolist test under the Merger Guidelines.[7] The DOJ and FTC, not surprisingly, look primarily to the hypothetical monopolist test when making prosecutorial decisions, but it they have to prove their case in court they will also invoke the *Brown Shoe* criteria.

Under *Brown Shoe*, the "outer boundaries" of the relevant product market "are determined by the reasonable interchangeability of use or the cross-elasticity of demand between the product itself and substitutes for it." *Brown Shoe*, 370 U.S. at 325. Moreover, "within this broad market, well-defined submarkets may exist which, in themselves, constitute product markets for antitrust purposes. The boundaries of such a submarket may be determined by examining such practical indicia as industry or public recognition of the submarket as a separate economic entity, the product's peculiar characteristics and uses, unique production facilities, distinct customers, distinct prices, sensitivity to price changes, and specialized vendors." *Id*. (internal citations and footnotes omitted). The original purpose of the *Brown Shoe* "practical indicia" was to enable the finding of relevant (sub)markets within larger markets defined by the "outer boundaries" test. Modern courts, however, do not view submarkets as any different from markets and regard the *Brown Shoe* "practical indicia" as factors probative of reasonable interchangeability of use and high cross-elasticity of demand.

Second, the "hypothetical monopolist test," which was introduced by the 1982 Merger Guidelines and now adopted in one form or another by the courts, deems a product grouping as a relevant market if a hypothetical monopolist of all products in the product group could profitably raise the prices in the product grouping by a small but significant nontransitory increase in price (SSNIP), usually taken to be 5% for a period of one year. The current 2010 Merger Guidelines have modified the hypothetical monopolist test in two ways:

1. Originally, the hypothetical monopolist test only deemed the smallest product grouping that satisfied the test to be a relevant market (the "smallest market principle"). Under the 2010 Merger Guidelines, while the smallest market principle remains the preferred approach, where appropriate to reflect the economic realities a larger market can be used.
2. Originally, the hypothetical monopolist test required the hypothetical monopolist to increase the prices of all of the products in the candidate market. Under the 2010 Merger Guidelines, where the hypothetical monopolist could raise the prices of one or more products selectively while leaving the prices of the other products constant, the hypothetical monopolist test requires only that the hypothetical monopolist to be able to profitably raise the price of a single product in the product group for the product grouping to be a relevant market.

[6] 370 U.S. 294, 325 (1962).

[7] U.S. Dep't of Justice & Fed. Trade Comm'n, Horizontal Merger Guidelines § 4 (rev. Aug. 19, 2010).

These modifications are increasingly being adopted by the courts. In particular, the modern courts are using the one-product SSNIP test to define markets.[8]

Read the excerpt from *Brown Shoe* on the "outer boundaries" and "practical indicia" criteria (p. 67) and the portion of the 2010 Horizontal Merger Guidelines that deal with product market definition (pp. 68-75). Then reread the product market allegations in the FTC's complaint (pp. 17-19) to see how the FTC set up its product market definition, the excerpt from the district court's opinion in *Sanford Health* to see how the court analyzed product market definition (pp. 79-80), and the Eight Circuit's review of the district court's product market findings (pp. 57-59).

Geographic market definition. As in product markets, there are two complementary judicial "tests" for whether a geographic area is a relevant product market for the purpose of merger antitrust analysis under Section 7: a judicial "commercial realities" test developed in *Brown Shoe* and the Merger Guidelines hypothetical monopolist test.

Brown Shoe is the leading case on geographic market definition. The Court observed that the criteria for determining the relevant geographic market are essentially similar to those used to test the boundaries of a relevant product market.[9] The *Brown Shoe* Court also stated that the submarket concept applies equally to geographic markets and product markets.[10] In determining the boundaries of the relevant geographic market, the Court emphasized that a "pragmatic, factual approach," rather than a "formal, legalistic one," must be used and that the relevant geographic market must both "correspond to the commercial realities" of the industry and be "economically significant."[11] The Court, employing a level of generality similar to that it used in describing the outer boundaries of product markets, has defined the relevant geographic market to be "the area of effective competition . . . in which the seller operates, and to which the purchaser can practically turn for supplies."[12] The Court also observed that an element of

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[8] *See, e.g.*, *FTC v. Sanford Health*, 926 F.3d 959, 963 (8th Cir. 2019); *FTC v. Wilh. Wilhelmsen Holding ASA*, 341 F. Supp. 3d 27, 46 (D.D.C. 2018); *FTC v. Tronox Ltd*., 332 F. Supp. 3d 187, 203 (D.D.C. 2018); *United States v. Anthem, Inc.*, 236 F. Supp. 3d 171, 198 (D.D.C. 2017); *United States v. Aetna Inc.*, 240 F. Supp. 3d 1, 20 (D.D.C. 2017); *FTC v. Staples, Inc.*, 190 F. Supp. 3d 100, 121 (D.D.C. 2016); *FTC v. Sysco Corp.*, 113 F. Supp. 3d 1, 33 (D.D.C. 2015); *United States v. H&R Block, Inc.*, 833 F. Supp. 2d 36, 51-52 (D.D.C. 2011).

[9] Brown Shoe Co. v. United States, 370 U.S. 294, 336 (1962) (citing S Rep No 1775, 81st Cong, 2d Sess 5-6 (1950)); United States v. E. I. Du Pont de Nemours & Co., 353 U.S. 586, 593 (1957).

[10] Brown Shoe Co. v. United States, 370 U.S. 294, 336 (1962). *See, e.g.*, White & White, Inc. v. American Hosp. Supply Corp., 723 F.2d 495, 501 (6th Cir. 1983) (Sherman Act).

[11] Brown Shoe Co. v. United States, 370 U.S. 294, 336-37 (1962).

[12] United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 359 (1963) (emphasis removed) (quoting Tampa Elec. Co. v. Nashville Coal Co., 365 U.S. 320, 327 (1961) (Sherman Act § 2)). *See, e.g.*, FTC v. Tenet Health Care Corp., 186 F.3d 1045, 1052 (8th Cir. 1999); FTC v. Freeman Hosp., 69 F.3d 260, 268-69 (8th Cir. 1995); Morgenstern v. Wilson, 29 F.3d 1291, 1296 (8th Cir. 1994); White & White, Inc. v. American Hosp. Supply Corp., 723 F.2d 495, 501 (6th Cir. 1983) (Sherman Act); FTC v. OSF Healthcare Sys., 852 F. Supp. 2d 1069, 1076 (N.D. Ill. 2012); Malaney v. UAL Corp., 2010 WL 3790296, at *6 (N.D. Cal. 2010) (not for publication), aff'd, 434 F. App'x 620 (9th Cir. 2011) (unpublished); FTC v. Arch Coal, Inc., 329 F. Supp. 2d 109, 123 (D.D.C. 2004); FTC v. Libbey, Inc., 211 F. Supp. 2d 34, 45 (D.D.C. 2002); California v. Sutter Health Sys., 130 F. Supp. 2d 1109, 1120 (N.D. Cal. 2001); FTC v. Cardinal Health, Inc., 12 F. Supp. 2d 34, 49 (D.D.C. 1998); FTC v. Staples, Inc., 970 F. Supp. 1066, 1073 (D.D.C. 1997); United States v. Mercy Health Servs., 902 F. Supp. 968, 978 (N.D. Iowa 1995); FTC v. Butterworth Health Corp., 946 F. Supp. 1285, 1290, (W.D. Mich. 1996); United States v. Country Lake Foods, Inc., 754 F. Supp. 669, 675 (D. Minn. 1990); *see also* FTC v. CCC Holdings, Inc., 605 F. Supp. 2d 26, 37 (D.D.C. 2009)

"fuzziness would seem inherent in any attempt to delineate the relevant geographic market"[13] and that the market need not be defined by "metes and bounds as a surveyor would lay off a plot of ground."[14] Even so, to sustain a relevant geographic market there must be sufficient evidence to conclude that the market boundaries adequately capture the material competitive forces.

The hypothetical monopolist in geographic market definition is analytically identical to that used in product market definition: a candidate geographic market is a relevant market if a hypothetical monopolist controlling all firms in the area profitably raise the prices of the relevant product by a small but significant nontransitory increase in price (SSNIP), usually taken to be 5% for a period of one year.

Although plaintiffs cannot rely simply on political boundaries (such as towns, counties, or states) to establish the boundaries of a relevant geographic market without providing evidence of the competitive forces within these boundaries, if the operative competitive forces are roughly contained within a political boundary, courts will typically find the market to be the political boundary.

Read the portion of the 2010 Horizontal Merger Guidelines that deal with geographic market definition (pp. 75-77). Then reread the geographic market allegations in the FTC's complaint (pp. 19-20) to see how the FTC set up its geographic market definition and the excerpt from the district court's opinion in *Sanford Health* to see how the court analyzed the geographic market (pp. 81-82). It does not appear that the merging parties argued that the district court erred in finding the relevant geographic market to be the Bismarck, ND Metropolitan Statistical Area, which includes Burleigh, Morton, Oliver, and Sioux countries.

The *Philadelphia National Bank* presumption. In 1963, the Supreme Court in *United States v. Philadelphia National Bank*,[15] provided an approach to answering one of the fundamental questions of merger antitrust law. The Court held that the plaintiff can make a prima facie showing of the requisite anticompetitive effect under Section 7 of a horizontal merger through an evidentiary presumption where the combined share of the merging firms and the increase in market concentration due to the merger are sufficiently high:

> [A] merger which produces a firm controlling an undue percentage of the relevant market, and results in a significant increase in the concentration of firms in that market, is so inherently likely to lessen competition substantially that it must be enjoined in the absence of evidence clearly showing that the merger is not likely to have such anticompetitive effects.[16]

The *PNB* presumption, which was not suggested in the briefs of the parties, was based on the price-concentration hypothesis of the structure-conduct-performance paradigm, which at the time was the theory of dominant industrial organization. The idea was that the structure of the market

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("The 'relevant geographic market' identifies the geographic area in which the defendants compete in marketing their products or services."); *accord* United States v. H&R Block, Inc., 833 F. Supp. 2d 36, 50 n.7 (D.D.C. 2011).

13 United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 360 n.37 (1963), *see* United States v. Connecticut Nat'l Bank, 418 U.S. 656, 669 (1974) (geographic markets "need not-indeed cannot-be defined with scientific precision").

14 United States v. Pabst Brewing Co., 384 U.S. 546, 549 (1966).

15 374 U.S. 321 (1963).

16 *Id*. at 363.

determined the market's performance and that markets performed less efficiently and exhibited higher prices as they became more concentrated (at least past some threshold). In this light, the *PNB* presumption was (implicitly) an effort to stop mergers that would impair economic efficiency and result in higher prices.[17]

Read the notes on *Philadelphia National Bank* presumption and its subsequent history through the Supreme Court's opinion in *General Dynamics* in 1974 (pp. 84-92). You can skim through PNB's litigation history if you like, but pay particular attention to the discussion in the subsequent history on the *Von's*, *Pabst*, and *General Dynamics*. *General Dynamics*, in particular, is a foundational case of modern merger antitrust law. These four cases provide much of the core of Supreme Court precedent on horizontal mergers and you should be generally familiar with them. Next, read Section 5 of the 2010 Horizontal Merger Guidelines, which operationalizes the *PNB* presumption (pp. 93-98). While some think that the thresholds specified in the Merger Guidelines have some practical significance, the cases litigated by the DOJ and FTC do not bear this out. As you can see from the tables on the HHIs in successful litigated cases, the HHIs alleged by the government in litigation far exceeds the thresholds in the Merger Guidelines (pp. 101-102). That said, the DOJ and FTC consistently cited the Guidelines thresholds as sufficient to trigger the PNB presumption and some courts in dicta appear to agree. So the thresholds may have more significance in the future, especially in an administration that aggressively challenges mergers. Finally, read the portions of the complaint (pp. 20-18) and the district court's opinion (pp. 99-100) applying the *PNB* presumption to establish a prima facie anticompetitive effect in the relevant market. The merging parties did not appear to appeal the application of the presumption, and the Eight Circuit devoted all of one sentence to it (p. 59).

Allocation of the burdens of proof under Baker-Hughes. One of the most important questions in the wake of *General Dynamics* was the quantum of evidence the merging parties were required to adduce in order to defeat the plaintiff's prima facie case. *Philadelphia National Bank* stated once the plaintiff had made out its prima facie case the transaction "must be enjoined in the absence of evidence *clearly showing* that the merger is not likely to have such anticompetitive effects."[18] Notwithstanding some implicit skepticism of this standard by the Court in *General Dynamics*, the "clear showing" standard was invariably invoked by the DOJ and FTC in their merger antitrust litigations. As a general rule, courts did not push back too hard until the D.C. Circuit's 1990 opinion in *Baker Hughes*.[19] In that case, the court of appeals explicitly rejected the "clear showing" standard and adopted instead a three-step burden-shifting approach to the allocation of the burden of proof in a horizontal merger antitrust case:

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[17] Recall from Unit 1 that in 1962 the Supreme Court in *Brown Shoe* had interpreted Section 7 in light of the legislative history of the Celler-Kefauver Amendments to be a guard against "the rising tide of economic concentration in the American economy," the loss of opportunity for small business when competing with large enterprises, and the spread of multistate enterprises and the loss of local control over industry. These are somewhat different concerns than the loss of economic efficiency and higher prices that concentrative mergers may cause under the price-concentration hypothesis. On the other hand, since the *PNB* presumption was—at least at the time of its creation—only a sufficient but not necessary means of proving a prima facie case of anticompetitive effect under Section 7, the fact that the *PNB* presumption was more narrowly based may not have been significant.

[18] United States v. Philadelphia Nat'l Bank, 374 U.S. 321, 363 (1963); *accord* United States v. Phillipsburg Nat'l Bank & Tr. Co., 399 U.S. 350, 366 (1970).

[19] United States v. Baker Hughes Inc., 908 F.2d 981 (D.C. Cir. 1990).

1. The plaintiff bears burden of proof in market definition and in market shares and market concentration within the relevant market sufficient to trigger the *PNB* presumption and thereby prove a prima facie Section 7 violation.
2. If the plaintiff satisfies this burden, the burden of production shifts to defendants to adduce evidence sufficient to rebut *PNB* presumption.
3. The burden of persuasion then returns to plaintiff to prove in light of all of the evidence in the record that the merger is reasonably probable to have an anticompetitive effect in the relevant market.[20]

The court of appeals directly confronted the *Philadelphia National Bank* "clear showing" language and concluded that *General Dynamics* and other cases had implicitly changed the standard. The three-step burden-shifting approach became the law of the circuit in the District of Columbia where most merger antitrust cases are brought. It was also quickly adopted by other courts. The *Baker Hughes* approach now appears well-entrenched in law, especially since its author (Clarence Thomas) and another member of the panel (Ruth Bader Ginsburg) are now Supreme Court justices.

When you read the excerpt from *Baker Hughes* (pp. 104-107), pay attention both to the articulation of the three-step burden-shifting approach and to the panel's rejection of the *PNB* "clear showing" rule. The note on *Baker Hughes* (pp. 107-111) provides a deeper dive into burdens on the parties at each of the three steps. In my experience, most practitioners and even judges do not really understand the *Baker Hughes* approach, and a thorough understanding will enable you to make much better arguments and write much better briefs.[21]

Sanford Health has lots of other things going on, including additional evidence adduced by the FTC to support the prima facie case beyond the presumption and as the treatment of four defenses put forward by the merging parties in the second step of the *Baker Hughes* approach: (1) market concentration has no relationship to bargaining power in the North Dakota healthcare market, (2) Catholic Health was poised to enter the market to compete with Sanford after the merger, (3) merger efficiencies offset the potential to harm consumers, and (4) Mid Dakota's weakened condition justified the merger. The Eight Circuit agreed with the district court in rejecting these defenses as sufficient to raise a genuine issue of whether the merger would have the requisite antitrust effect, and therefore did not proceed to the Baker Hughes third step. We will discuss these elements of the case in class, but I will not burden you beyond the Eight Circuit's opinion on these issues. We will address each of these topics in detail in later case studies in the course.

Enjoy the reading! Email me if you have any questions.

[20] *Id.* at 982-83.

[21] As you will read, Thomas based his three-step burden-shifting approach on *Texas Dep't of Community Affairs v. Burdine*, 450 U.S. 248, 253-56 (1981), a civil rights case. Consequently, the *Baker Hughes* approach has application beyond antitrust cases.