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At Last, Some Judicial Guidance in Health Care Mergers

By Wiline Justilien and J. Mark Waxman

The health care industry is undergoing very rapid change. Health care entities everywhere are looking to clinically integrate, create a stronger capital base, and affiliate to address quality issues and marketplace challenges, as well as for a host of other reasons. They are routinely exploring mergers, strategic partnerships, and joint ventures. Consolidation often occurs when two or more actual or potential competitors come together to form a strategic alliance. In a landscape where growth and expansion are achieved through consolidation of competitors, antitrust concerns are surfacing with some regularity. A challenge is in ascertaining the limits to collaborative activity, particularly in two areas: activities between or among health care entities prior to their actual merger or consolidation as they explore the viability of the arrangement; and second, in the context of joint operating agreements (JOAs). Unfortunately, there is very little in the way of bright line rules to guide health care entities looking to avoid Sherman Act Section 1 scrutiny in these areas.

Three recent cases, as well as one not quite so recent case, however, provide some insight into what courts consider when examining alleged antitrust violations in the current consolidation environment. The first two, *Asahi Kasei Pharma Corp. v. CoTherix Inc.*[1] and *Omnicare Inc. v. United Healthcare Group Inc.*,[2] provide guidance on premerger activities that could be susceptible to antitrust scrutiny. The two cases support the notion that the premerger sharing of competitively sensitive information should be reasonable, and necessary to achieve legitimate business objectives. In that context, antitrust exposure may be limited. The last two, *Medical Center at Elizabeth Place LLC v. Premier Health Partners*[3] and *Healthamerica Pa. Inc., v. Susquehanna Health Sys.*,[4] explore postaffiliation challenges when merger was not the solution to the need to affiliate or consolidate, and the parties have pursued a JOA structure.

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Premerger Antitrust Scrutiny

Omnicare is one of the most recent federal case law precedents to provide antitrust counsel with judicial guidance on how to advise clients engaged in premerger activity in the health care field. This matter was before the U.S. Court of Appeals for the Seventh Circuit on appeal from the grant of summary judgment in favor of defendant United Healthcare Group (UHG). Plaintiff Omnicare, a large U.S. institutional pharmacy, brought suit against UHG alleging that UHG and health insurer PacifiCare Health Systems (PHS) formed a buyer's cartel against it to obtain below-market reimbursement rates for drugs covered under the then-new Medicare Part D program. Omnicare argued that while UHG and PHS engaged in a standard due diligence process prior to merging, the two insurance companies crossed the antitrust line when they exchanged competitively sensitive information in violation of Section 1, and coordinated their negotiations with Omnicare whereby PHS aggressively negotiated with Omnicare to obtain below-market reimbursement rates. Once the merger between UGH and PHS was completed, UGH allegedly aban-

[1] *Asahi Kasei Pharma Corp. v. CoTherix Inc.*, 138 Cal. Rptr. 3d 620 (Cal. Ct. App. 2012), *available at* http://op.bna.com/atr.nsf/r?Open=tmie-8s5ssg.

[2] *Omincare Inc. v. United Healthcare Group Inc.*, 629 F. 3d 697 (7th Cir. 2011), *available at* http://op.bna.com/pl.nsf/r?Open=byul-8zdr7p.

[3] *Medical Center at Elizabeth Place LLC v. Premier Health Partners*, No. 3:12-cv-26 (S.D. Ohio, Aug. 30, 2012), *available at* http://op.bna.com/pl.nsf/r?Open=byul-8zcuwb.

[4] *Healthamerica Pa. Inc., v. Susquehanna Health Sys.*, 278 F. Supp. 2d 423 (M.D. Pa. 2003), *available at* http://op.bna.com/pl.nsf/r?Open=byul-8zcver.

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doned its previous agreement with Omnicare and adopted the more favorable agreement between Omnicare and PHS.

In affirming the district court's grant of summary judgment in UGH's favor, the Seventh Circuit held that in order for Omnicare's claims to have survived summary judgment, it would have had to: ''show that the inference of conspiracy is reasonable in light of the competing inferences of independent action or collusive action,'' proffer evidence that tended to ''rule out the possibility that the defendants were acting independently,'' and prove that the pricing and strategic information exchanged between the parties did ''not tend to exclude the possibility that UnitedHealth and PacifiCare were acting to advance their own legitimate interests.'' In light of the evidence Omnicare proffered, the court found its conspiracy allegations lacking. Specifically, the court pointed to several precautions UGH and PHS took to avoid antitrust risk during the due diligence period:

- UGH and PHS had confidentiality agreements providing for how ''confidential'' and ''highly confidential'' information was to be exchanged;
- PHS had a ''clean team'' comprised of outside counsel who reviewed all PHS documents and determined the necessity of sharing the documents before providing them to UGH; and
- UGH and PHS never shared specific pricing information during the due diligence period. Instead, the two companies shared ''generalized and average high-level pricing data, policed by outside counsel.''

The district and appellate courts also acknowledged the sensitive balance involved in establishing restrictions that would not chill the business activity of companies that would merge ''but for a concern over potential litigation,'' and the need to prevent the sharing of competitively sensitive information that could lead to ''sham merger negotiations'' and concerted efforts that restrained trade.

The California Court of Appeal, in *Asahi* also faced this need for sensitive balancing of interests as it decided whether certain preacquisition behavior by the defendant constituted an unlawful ''combination'' in violation of California's Cartwright Act.[5] This matter was up on appeal from the lower court's grant of summary judgment in the defendant's favor. At issue was whether the activities of two companies in anticipation of a merger constituted a violation of the Cartwright Act's prohibition against conspiracies in restraint of trade. Plaintiff Asahi, a Japanese pharmaceutical products developer and marketer, contracted with defendant CoTherix, a California-based biopharmaceutical company, to commercialize Asahi's drug, Fasudil, in the United States. Approximately six months after Asahi entered into a licensing agreement with CoTherix, Actelion, a Swiss pharmaceutical company with a U.S.-based operational subsidiary, acquired CoTherix and discontinued development of Asahi's drug.

Asahi filed suit against CoTherix, alleging it violated the Cartwright Act by conspiring with Actelion preacquisition to mislead Asahi about Actelion's intentions to discontinue marketing Fasudil, which Actelion viewed as a potential competitor to its own drug, Tracleer. According to Asahi, Actelion conspired with CoTherix to delay development of Fasudil, thereby delaying the entry of a competitor in a relevant market. Moreover, Actelion allegedly directed CoTherix to falsely reassure Asahi that it would continue developing the drug, which deprived Asahi the opportunity to avail itself of injunctive relief under the licensing agreement. Asahi alleged Actelion acted with anticompetitive intent, but it did not challenge the merger itself nor plead a premerger meeting of the minds. CoTherix countered that the Cartwright Act was inapplicable to corporate acquisition transactions, there were no triable issues of material fact as to whether CoTherix and Actelion conspired to interrupt Fasudil's development, and that Asahi lacked antitrust standing.

In deciding the matter, the court of appeal extended to premerger activity the holding in a prior seminal decision, *State of California ex rel. Van de Kamp v. Texaco*,[6] that the Cartwright Act did not reach mergers where one or more of the entities ceases to exist. As the *Texaco* decision stated, the Cartwright Act applied only to those entities that ''continue as separate, independent, competing entities during and after their collusive action.'' Where two or more entities have unity in economic interest and purpose, they are incapable of conspiring for Cartwright Act purposes. Here, the court found that once CoTherix and Actelion formally agreed to merge, as evidenced by the acquisition agreement, their independent economic decisionmaking was compromised.[7] The court went on to state that, even if it found CoTherix and Actelion were capable of conspiring during the premerger period, Asahi failed to present a viable Cartwright claim, as it did not ''produce evidence of any premerger meeting of the minds specifically to restrain the trade of Fasudil.'' Finding so, the court affirmed the grant of summary judgment in CoTherix's favor. Thus, the court emphasized that it was the ''meeting of the minds'' that was critical, and not the sharing of the information.

Postaffiliation Challenges Against JOAs

One of the ways in which parties, particularly hospitals, have considered working together without actually merging is through a JOA.[8] A JOA is a contract that two or more entities enter to facilitate the management of a certain aspect of the entities. JOAs also have been used in the health care industry to create hospital system parents that have oversight authority over the participating hospitals. It was behind a JOA that the defendants in *Medical Center at Elizabeth Place* were alleged to have hidden to allow their conduct to escape Section 1 scrutiny.

In *Medical Center at Elizabeth Place*, the court examined whether a group of hospitals operating under a

[5] The Cartwright Act is California's analogue to Section 1. However, it does not reach single-firm monopolization as does Section 2.

[6] *State of California ex rel. Van de Kamp v. Texaco*, 46 Cal. 3d 1147 (Cal. 1988).

[7] The court noted that under the acquisition agreement, CoTherix obligated itself to ''numerous contractual covenants and conditions, including limitations on its pre-closing ability to incur indebtedness, make certain capital expenditures, and engage in certain dealings with its employees.''

[8] *See generally* J. Mark Waxman and Janice A. Anderson, *Hospital Systems Today—Valuable Integration or Is It Time to Cut the Cord?* Health Lawyers News, October 2008, at 24.

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JOA constituted a single entity and was, therefore, incapable of a group boycott in violation of Section 1. Plaintiff Medical Center at Elizabeth Place (MCEP) filed suit against Premier Health Partners (Premier) and its hospital affiliates (collectively, the defendants) alleging that the defendants, who function under a JOA, conspired through managing agent Premier to facilitate a *per se* illegal boycott against MCEP. Specifically, the defendants allegedly ''coerced, compelled, co-opted or financially induc[ed]'' managed care plan providers to refuse MCEP full access to their networks. MCEP also alleged that the defendants offered physicians financial incentives for not working with MCEP and threatened financial consequences for physicians who did.

The defendants argued that MCEP's group boycott claim did not qualify for *per se* treatment, that MCEP did not allege antitrust injury, and that the defendants were incapable of conspiring under Section 1 because their conduct under the JOA was that of a single entity that was sufficiently integrated. In rejecting the defendants' latter argument, the court stated that as pleaded in MCEP's complaint, the defendants were subject to Section 1's prohibition against joint conduct between multiple entities. Entities that remain separate and distinct, and that remain both ''actual and potential competitors in the relevant markets,'' are not single entities whose conduct is exempt from Section 1 scrutiny. The court pointed to these MCEP allegations, among others, to reach its conclusion that the JOA did not integrate the defendants' hospitals in such a way that they operated as a single entity: 1) the hospitals were independently owned and operated; 2) the JOA was a ''consolidation of revenue streams''; 3) Premier had never reported any assets, liabilities, revenue, income, or expenses; and 4) each hospital made material independent decisions concerning their respective operations that were not managed by Premier. The court denied the defendants' motion, holding that the plaintiff's case could not be resolved on a motion to dismiss.

As part of its analysis, the court examined *Healthamerica Pa. Inc., v. Susquehanna Health Sys.*, which involved a JOA similar to the one MCEP challenged, a case that many health care practitioners have looked to for guidance in the context of looking at sole-member based health care systems. Unlike *Medical Center at Elizabeth Center*, *Healthamerica* was decided on a motion for summary judgment after extensive discovery on the structure of the entity that was created by the JOA, Susquehanna Alliance (Alliance). Accordingly, the matter yielded a detailed decision with important guidance on how to structure a JOA that will withstand Section 1 scrutiny. The *Healthamerica* court granted the hospital defendants' motion for summary judgment, holding that the defendant hospitals and their JOA structure, Alliance, constituted ''a single entity legally incapable of'' concerted action.

To reach its decision, the court applied the *Copperweld* doctrine and examined whether the hospitals were a single entity ''in substance, not form.'' The court noted that the ''Defendants' composition is akin to a corporate parent (Susquehanna Alliance) and its subsidiaries (the hospitals and Affiliates).'' Moreover, their actions were guided (quoting *Copperweld*) ''not by two separate corporate consciousnesses, but one.'' Specifically, the hospitals integrated their internal operations, including risk management, facilities management, human resources, administrative policies, compliance, operating budget, and health insurance program. The Alliance also centralized marketing, shifted cash between the hospitals, set charges for the hospitals, and purchased singular insurance policies for the hospitals. Consequently, the court found the hospitals' conduct was not concerted action between unintegrated competitors, and Section 1 was inapplicable because the hospitals were not capable of conspiring.

Practical Application

What lessons can health care practitioners learn from *Omnicare*, *Asahi, Medical Center at Elizabeth Place, and Healthamerica*? Entities that remain independent units, even during a premerger period or after a strategic alliance, may be exposed to antitrust liability under Section 1 when engaging in concerted acts that potentially affect competition. Independence will be tested by looking at the unity of economic interest, purpose, and functioning, as well as by determining if the entities remain actual and potential competitors in the marketplace. Accordingly, health care entities addressing a consolidation effort should take special precautions to ensure independent decision-making when engaging in premerger/affiliation or postclosing activity that will impact the competitive marketplace. Thus, here are some general do's and don't's to guide the process in avoiding scrutiny under Section 1 or under state statutes that prohibit the same behavior. Until or unless the two entities become one functioning unit with the same economic interests and purpose:

- **It is important to** consult with antitrust counsel.
- Remember that two independent entities providing similar goods and/or services in a relevant market are competitors.
- **IF THERE IS A LEGITIMATE BUSINESS NEED TO** exchange competitively sensitive information, **DO** respond to pricing questions in general terms, and disclose only the information needed for legitimate business reasons. Use a ''clean team''—an external third party—to communicate highly sensitive information during the due diligence period. Share information on a redacted or historical, aggregate basis.
- A systemized method of tracking the competitively sensitive information exchanged between or among entities will be valuable.
- **The merging parties should** only undertake the due diligence that is reasonably necessary at any given time to properly analyze and effect the contemplated merger.
- It is best not to share or discuss information unrelated to the business that is subject of the strategic alliance.
- Premerger agreements or understandings with competitors regarding the division of markets or pricing may well lead to antitrust exposure.

With respect to operations under a JOA:

- **To create a unity of interest from an economic standpoint for antitrust purposes will require some degree of centralized authority and sharing**

of risks. A fully decentralized model may face real antitrust scrutiny.

- **One element likely to reduce antitrust risk is an** integration of management and operations across the system.

The current merger and consolidation effort continues to evolve. Given the number of open issues and lack of bright lines, any case law that addresses the current structures and approaches is welcome. The recent decisions we have discussed help provide some guidance with respect to premerger discussions, albeit under a state antitrust law, and the use of a joint operating agreement. The underlying message, of course, remains that these types of issues are very fact specific, and counsel should be involved in not just the documentation of a transaction, but in understanding the nature of its risks and proactively providing appropriate counsel to mitigate them.

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