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ANTITRUST

Expert Analysis

Merger Challenges Large and Small

By **Elai Katz**

Antitrust authorities have been busy litigating mergers in 2016: The Federal Trade Commission's challenge to a hospital merger in Pennsylvania was revived on appeal, and the Department of Justice (DOJ) filed two lawsuits to block a pair of health insurance mergers. The antitrust agencies also brought enforcement actions directed at corporate entanglements, alleging violations of premerger notification and interlocking directorate statutes.

Hospital Merger

The U.S. Court of Appeals for the Third Circuit endorsed the FTC's challenge to the proposed merger of two Pennsylvania hospitals, PinnacleHealth System and Penn State Hershey Medical Center. The court reversed the district court's denial of the FTC's request for an injunction, stating that the lower court erred in defining the relevant market for evaluating the competitive effects of the potential merger. *FTC v. Penn State Hershey Med. Ctr.*, No. 16-cv-2365, 2016 WL 5389289 (3d Cir. Sept. 27, 2016).

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The FTC, joined by Pennsylvania, defined the geographic market to include the four counties surrounding Harrisburg, where both hospitals are located, excluding other hospitals in surrounding counties. The district court rejected this territorial boundary as too narrowly drawn because "patient flow data" showed that over 40 percent of Hershey Medical Center's patients traveled from outside the four-county area and nearly 20 hospitals within about an hour's drive of Harrisburg could offer patients an alternative if the merging hospitals increased prices.

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The Third Circuit disagreed, explaining that the lower court's analysis was "particularly unhelpful in hospital merger cases," as it does not reflect the commercial reality of the health-care market, where patients largely select hospitals based on non-price criteria and health insurers play a critical role in negotiating with hospitals. Relying in part on an amicus brief submitted by economists, the appellate court observed that the district court's analysis closely resembled a "discredited" economic theory now disavowed by its inventor. The Third Circuit reversed and remanded, directing the district court to preliminarily enjoin the proposed merger so that the FTC could review the transaction. The parties subsequently abandoned the deal.

Health Insurance Mergers

The DOJ filed parallel lawsuits on the same day, challenging what the department characterized as two "unprecedented" mergers of major health insurance companies. (See DOJ Press Release July 21, 2016). The first challenge, to Aetna's $37 billion acquisition of Humana, concerns the market for Medicare Advantage, a market-based alternative to traditional Medicare that provides lower out-of-pocket costs and additional

coverage in exchange for using a network of doctors and hospitals. *U.S. v. Aetna*, No. 16-cv-01494 (D.D.C. July 21, 2016).

Traditional Medicare does not limit services to a particular network, but can result in higher out-of-pocket expenses. The DOJ alleged that the merger would substantially reduce competition in the market for Medicare Advantage plans by eliminating Humana, the nation's second-largest Medicare Advantage insurer, and by dampening the increased competition created by Aetna's "aggressive expansion" into the Medicare Advantage market over the last four years.

In support of limiting the relevant market to Medicare Advantage plans, DOJ asserted that if Medicare Advantage providers imposed a small but significant price increase, an insufficient number of seniors would switch to alternatives to make that price increase unprofitable. Aetna and Humana, however, contended that traditional Medicare products should have been included in the DOJ's relevant product market definition as they compete for customers with Medicare Advantage plans and, when considering the available alternatives in public and private markets together, the elimination of Humana would have little impact on competition. The DOJ also alleged that the merger will substantially reduce competition to sell commercial health insurance to individuals and families on the public exchanges in 17 local markets in Florida, Georgia and Missouri.

In a second complaint, the DOJ alleged that Anthem's proposed $54 billion acquisition of Cigna would substantially reduce competition in the sale of health insurance to national accounts, large groups, and on the public exchanges, and would lessen competition for the purchase of health-care services from doctors, hospitals and other health-care providers. *U.S. v. Anthem*, No. 16-cv-01493 (D.D.C. July 21, 2016). Both cases are expected to proceed to trial in the next two months.

The mergers are challenged in separate complaints, involve distinct product and geographical markets, and were ultimately assigned to different judges. Yet the DOJ painted the same picture, with identical allegations, at the beginning of both complaints: that the proposed mergers of four of "the big five" insurers was done "in a scramble to become even bigger," "will reshape the industry, eliminating two innovative competitors—Cigna and Humana—at a time when the industry is experimenting with new ways to lower healthcare costs." While each case must be analyzed independently, merger review necessarily involves predictions about the state of the market in the future, making it difficult to disregard consideration of other proposed transactions.

> The Justice Department conditionally approved the merger of the world's two largest brewing companies, Anheuser-Busch InBev (ABI) and SABMiller. Together they accounted for 74 percent of national beer sales and owned the top three brands, including Bud Light, Coors Light and Miller Lite.

Premerger Notification

ValueAct, an investment manager, agreed to pay $11 million to settle a government lawsuit charging that it violated premerger notification regulations. (See DOJ Press Release, July 12, 2016). The enforcement action arises under the Hart Scott Rodino (HSR) Act, which requires purchasers of voting securities exceeding certain thresholds to notify the DOJ and FTC and observe waiting periods before completing the acquisitions to give the antitrust agencies an opportunity to review the transactions.

Acquisitions of not more than 10 percent of outstanding voting securities may be exempt from notification as long as they are made solely for the purpose of investment. DOJ claimed that when ValueAct purchased over $2.5 billion in stock without submitting HSR notifications, it improperly relied on the investment-only exemption because it planned to take an active role in the investments.

ValueAct began purchasing shares of two of the three largest providers of oilfield services, Halliburton and Baker Hughes, shortly after the two companies announced their merger plans, which have since been abandoned. The DOJ alleged that ValueAct intended from the outset to influence business decisions of the companies and to improve the chances that the merger would close. *U.S. v. VA Partners I*, No. 16-cv-01672 (N.D. Cal. April 4, 2016). DOJ alleged that ValueAct reached out to both companies almost immediately after it began purchasing shares, and frequently

communicated with senior management at both companies. DOJ also noted that, unlike passive funds, ValueAct promotes itself as having an active investment strategy.

The DOJ explained that a substantial penalty was warranted in this case because ValueAct previously violated the HSR Act and should have recognized its filing obligation, or at least known to consult the FTC. (See Competitive Impact Statement). Lastly, DOJ considered it an "aggravating factor that the transactions at issue raised substantive competitive concerns," observing that ValueAct established these positions as the Halliburton and Baker Hughes merger was under antitrust review and "planned to intervene to influence the probability that the merger would be completed or to determine the companies' courses if it was not."

Interlocking Directorates

Tullett Prebon and ICAP, providers of brokerage services, restructured a transaction to resolve the DOJ's concerns that the parties would violate Section 8 of the Clayton Act by creating an "interlocking directorate," whereby a person sits on the board of directors of two competitors. (See DOJ Press Release, July 14, 2016). In November 2015, Tullett Prebon announced its plan to purchase ICAP's voice brokerage business. ICAP would remain in the electronic brokerage market, and would continue competing against Tullett Prebon for electronic brokerage business after the acquisition.

The initial structure of the transaction involved ICAP shareholders receiving a 36.1 percent stake in Tullett Prebon and ICAP receiving a 19.9 percent stake along with the right to appoint a director on Tullett Prebon's board. In response to DOJ's concerns, the parties restructured the deal to give ICAP shareholders the entire 56 percent stake in Tullett Prebon. ICAP will not own any part of Tullett Prebon and will not have a right to nominate a director to the board.

The DOJ stated that ICAP's nomination right would have created "a cozy relationship among competitors," adding that interlocking directorates may present "opportunities and temptations" to violate antitrust laws.

The two cases reported immediately above stand apart from acquisitions of controlling positions and come at a time when some scholars and popular publications have voiced concerns about harm to competition when a common set of investors holds significant minority stakes in rival firms. (Einer Elhauge, "Horizontal Shareholding," 129 Harv. L. Rev. 1267 (2016); "Stealth socialism: Passive investment funds create headaches for antitrust authorities," The Economist (Sept. 17, 2016)).

Green Light for Beer Merger

The Justice Department conditionally approved the merger of the world's two largest brewing companies, Anheuser-Busch InBev (ABI) and SABMiller. (See DOJ Press Release, July 20, 2016). Together they accounted for 74 percent of national beer sales and owned the top three brands, including Bud Light, Coors Light and Miller Lite. See DOJ Complaint, *U.S. v. Anheuser-Busch InBev*, No. 16-cv-01483 (D.D.C. July 20, 2016).

The DOJ settled charges that the proposed merger would substantially lessen competition in the U.S. beer industry in violation of Section 7 of the Clayton Act by requiring a divestiture of SABMiller's ownership stake in MillerCoors LLC, to the minority owner, Molson Coors LLC, maintaining MillerCoors as an independent competitor. (See Competitive Impact Statement).

This transaction received antitrust scrutiny from many foreign regulators as well, including the European Commission, which required ABI to divest some brands to a Japanese brewer. The DOJ's settlement requires that even for brands sold to the Japanese company, ABI must divest its rights to import those brands into the U.S. to Molson Coors.

The DOJ also asserted that the proposed merger threatened competition by increasing ABI's "incentive and ability" to restrict access to distribution channels. The proposed settlement includes provisions designed to ensure ABI's distributors can continue to carry rival brands, especially high-end import and craft beers that constrain ABI's ability to raise prices.

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