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ANTITRUST

Expert Analysis

Acquisition With Steep Price Hike Survives FTC Challenge

By **Elai Katz**

A district court rejected a challenge to the acquisition of a newly developed drug by a company that owned a well-established drug used to treat the same condition because it found that the two drugs were not in the same relevant market. The U.S. Court of Appeals for the Ninth Circuit ruled that a profit-sharing agreement among Southern California supermarkets to counteract targeted strikes during a labor dispute was not shielded from antitrust scrutiny by the labor exemption. The U.S. Court of Appeals for the Federal Circuit decided that an agreement between participants in a standard-setting collaboration not to license competitive technology did not give rise to a patent misuse defense in an infringement action.

Other recent antitrust developments of note included the Department of Justice's enforcement action challenging a leading health insurance company's Most-Favored Nation (MFN) clauses requiring hospitals to charge rival insurers the same or higher rates.

Drug Acquisition

In 2005, a drug company acquired an off-patent drug that has been used for many years to treat patent ductus arteriosus, a heart condition in premature babies, and in early 2006 the company acquired a soon-to-be approved, newly developed drug used to treat the same condition. Very shortly after acquiring the newly developed drug, the company raised the price of its off-patent product from around $100 to $1,500 per three-vial course.

The Federal Trade Commission (FTC) and the State of Minnesota commenced an action asserting that the company's 2006 acquisition and swift 1,300 percent price increase violated federal and state antitrust laws prohibiting monopolization and acquisitions that substantially lessen competition. Following a bench trial, the district court entered judgment in favor of the company and dismissed the lawsuit.

In its recitation of the facts, the court noted that the company had decided to substantially raise the price of the off-patent drug before it agreed to acquire the newly developed drug, after conducting detailed analysis concluding that the prior owner of the off-patent drug had significantly under-priced it. The court also noted that although the newly developed drug and the off-patent drug were not bioequivalent, they were both correspondingly effective in treating the same premature-baby heart condition. The company's internal studies forecast that the newly developed drug would "capture a significant portion" of the off-patent drug's sales. Furthermore, the company planned to promote switching away from the off-patent drug—which attracted generic competition at its elevated price—to the newly developed drug.

> The appellate court in 'California v. Safeway, Inc.' stated that not all employer conduct during labor negotiations is insulated from antitrust review.

The court acknowledged that the government enforcers' case was "superficially appealing" because of the sharp post-acquisition price increase, but ultimately found no antitrust violations. The court determined that FTC and Minnesota failed to prove that the relevant product market was drugs used to treat the premature heart condition. The court stated that the relevant consumers were neonatologists, not hospitals, because even though the hospitals purchase the drugs, the neonatologists ultimately determine which drugs to use. The evidence showed that neonatologists do not consider price in their selection of one drug over another, but rather differences between the drug's side effects, safety and track record. The court was persuaded by the defense expert's testimony that the cross-price elasticity of demand between the two drugs was very low—in other words, an increase in the price of one of the drugs was not likely to lead many customers to switch to the other drug.

FTC v. Lundbeck Inc., 2010-2 CCH Trade Cases ¶77,160 (D. Minn.), notice of appeal filed (Oct. 28, 2010)

Comment: The decision reported immediately above invites more detailed consideration of how one should go about defining the contours of a relevant market where products serve as substitutes yet consumer purchasing decisions are not driven principally by price. This problem arises often in markets with third-party payors, such as the health care industry. The formalistic application of the price elasticity test may at times lead to especially narrow relevant markets, which may benefit plaintiffs or defendants depending on the circumstances.

Labor Exemption

In anticipation of a strike during multi-employer contract negotiations with unions, several of the leading Southern California supermarkets entered into a mutual strike assistance agreement whereby if the unions decided to picket only one of the supermarkets, all of the supermarkets would lock out their union employees and share revenues during the strike. The revenue sharing provision was intended to counteract an expected union "whipsaw" tactic of picketing only one or some of the employees, which would exert economic pressure on the picketed employers as their sales drop significantly.

The Attorney General of California brought an antitrust suit alleging that the profit sharing provisions unreasonably restrained trade in violation of §1 of the Sherman Act. The defendant supermarkets argued that their agreement was immune from antitrust challenge by operation of the non-statutory labor exemption, which allows rival employees to coordinate their collective bargaining activities in certain circumstances without risk of antitrust liability. The judicially created exemption was crafted because courts recognized that it would be difficult to require collective bargaining by groups of employers and employees under federal labor laws while at the same time prohibiting coordination by multiemployer bargaining groups under the antitrust laws.

The Ninth Circuit affirmed the district court's denial of summary judgment to defendants, rejected the supermarkets' immunity defense

ELAI KATZ *is a partner at Cahill Gordon & Reindel.* LAUREN RACKOW, *an associate at the firm, assisted in the preparation of this article.*

and stated that profit sharing is not a traditional or necessary part of multiemployer bargaining. The appellate court added that not all employer conduct during labor negotiations is insulated from antitrust review and that by eliminating incentives to compete, the profit-sharing agreement had a direct effect on the product market.

In evaluating the legality of the profit-sharing agreement under the Sherman Act, the Ninth Circuit stated that it applied a hybrid "per se-plus or quick look-minus analysis." Under this approach, the appellate panel determined that there was a "great likelihood of competitive effects" by examining prior cases, the circumstances of the agreement, logic and rudimentary principles of economics, without requiring empirical evidence of anticompetitive effects.

California v. Safeway Inc., 615 F.3d 1171, 2010-2 CCH Trade Cases ¶77,134

Patent Misuse

The Federal Circuit, sitting en banc, ruled that an agreement not to license technology that might arguably compete with an industry standard covered by a patent pool could not support a misuse defense in a patent infringement suit.

The owner of patents for manufacturing recordable and re-writable compact discs participated in developing the industry standard and put together a patent pool covering the technology. The patent owner brought infringement claims against a manufacturer and importer of compact discs before the International Trade Commission. The alleged infringer argued that the patent misuse doctrine rendered the patents unenforceable because the patent owner included a non-essential patent covering competing technology in the required package of pooled patents and had contracted to prevent independent licensing of the competing technology.

A panel of the Federal Circuit had stated that an agreement not to license the alternative technology could constitute patent misuse, *Princo Corp. v. ITC*, 563 F.3d 1301 (Fed. Cir. 2009) (vacated), but a majority of the full appellate court, sitting en banc, disagreed. The majority opinion observed that the patent misuse doctrine—a shield against an infringement action but not a sword to attack a licensing arrangement—should be construed narrowly and that the antitrust laws are sufficiently broad and flexible to regulate restraints of trade related to patent licenses.

The majority stated that patent misuse should be cabined to situations where the license is conditioned upon purchase of an unpatented product, extends the term of the patent or otherwise seeks to extend the patentee's rights beyond the scope of the patent. The en banc majority added that the patent misuse defense is not available whenever a patent holder engages in wrongful, even anticompetitive, conduct. Rather, the key question, according to the court, is whether the patent owner has "impermissibly broadened the physical or temporal scope of the patent grant."

In addition, invoking patent misuse as a defense to an infringement action requires a showing of anticompetitive effects, according to the appellate court. In this case, evidence did not show that the alternative technology included in the patent pool had real potential for technical or commercial success and therefore any agreement not to separately license that technology did not harm competition.

Princo Corp. v. International Trade Commission, 616 F.3d 1318, 2010-2 CCH Trade Cases ¶77,147

Comment: The dissenting judges in the decision reported immediately above expressed a concern that in the absence of a patent misuse defense, agreements to suppress technology in the standard-setting context may evade private challenge under the Sherman Act.

Most-Favored Nation Clauses

The U.S. Department of Justice and the State of Michigan brought an action asserting that Michigan's largest health insurer unreasonably restrained trade in violation of federal and Michigan antitrust law by including MFN and "MFN-plus" clauses in its contracts with hospitals. The complaint alleges that when hospitals negotiated to increase the fees the insurer paid for medical services, the insurer insisted that the hospitals agree to charge other insurers at least as much as it paid. Many of the major hospitals in the state agreed to charge rival insurers a specified percentage more—in some cases as high as 40 percent—than the leading insurer.

The FTC circulated proposed changes to the premerger notification form that must be submitted to facilitate antitrust review of mergers and acquisitions under the Hart-Scott-Rodino Act.

The government enforcers claim that these provisions diminished rival insurers' ability to compete with the leading insurer, which accounted for over 60 percent of the market for the sale of commercial health insurance to groups and individuals in Michigan, and raised the prices for medical services as well as health insurance premiums. The complaint asserted that the insurer did not use MFNs to lower its costs and that these terms have caused hospitals to raise prices charged to other insurers rather than reduce prices for the leading insurer. The complaint also alleges that the MFNs have deterred entry by insurers that could not compete if they had to pay more than the leading insurer for medical services.

United States v. Blue Cross Blue Shield of Michigan, Civ. Action No. 2:10-cv-15155-DPH-MKM, CCH Trade Reg. Rep. ¶45,110, No. 5128 (E.D. Mich. Oct. 18, 2010)

Comment: Courts have declared that MFNs are standard devices used by buyers to bargain for lower prices and should not be presumed to be unlawful, but the antitrust agencies have brought enforcement actions challenging certain MFNs from time to time, particularly in the health care context as in the development reported immediately above.

Outlet Center Acquisition

The FTC announced the settlement of charges that the completed acquisition of an operator of retail mall outlet centers by the largest retail mall company in the United States substantially lessened competition in violation of §7 of the Clayton Act. The settlement requires the company to divest one of two outlet centers in Ohio and eliminate territorial restrictions preventing the company's tenants from opening stores in competing outlet centers in the Chicago and Orlando regions, which should enable rival outlet centers and developers to enter these markets.

Simon Property Group, FTC Docket No. C-4307, File No. 101-0061, CCH Trade Reg. Rep. ¶16,519 (Nov. 10, 2010), available at www.ftc.gov

Premerger Filings

The FTC circulated proposed changes to the premerger notification form that must be submitted to facilitate antitrust review of mergers and acquisitions under the Hart-Scott-Rodino Act. The proposed new form would no longer require companies to report older revenues, substantially lessening the financial reporting burden imposed on companies. However, it would expand the categories of documents that must be submitted by requiring the inclusion of offering memoranda, studies, evaluations and analyses that reference the acquired entity or assets. Notably, these documents would not be limited to the notified transaction, and they would encompass materials prepared by lower-level employees and third parties, such as investment bankers. The new form would also require reporting of holdings and operations of entities under common management with the filer.

Premerger Notification; Reporting and Waiting Period Requirements, 75 Fed. Reg. 57,110 (Sept. 17, 2010), available at http://www.ftc.gov/os/2010/08/100812hsrfrn.pdf and CCH Trade Reg. Rep. ¶50,255

Comment: By not restricting the submission of materials to documents about the notified transaction, the FTC may inadvertently cause the search for documents to require contacting employees and outside advisers not involved with the proposed transaction, possibly implicating confidentiality concerns.

Successor Liability

A district court found that a company that acquired the assets of a sulfuric acid producer was not liable for price fixing and output restriction claims asserted against the producer. The court observed that in most states, a purchaser of assets does not assume the seller's liabilities even if an entire business was transferred in the sale. Although the acquiring company assumed the sulfuric acid producer's agreement with a joint venture at the center of the conspiracy allegations, the court stated that the plaintiff did not show that the asset purchaser knowingly joined in a seller's antitrust conspiracy.

In re: Sulfuric Acid Antitrust Litigation, 2010-2 CCH Trade Cases ¶77,194 (N.D. Ill. Sept. 24, 2010)

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