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FTC Attempt to Block Chicago Hospital Merger Rejected by Federal Court

For the second time in as many months, a federal judge has rejected the Federal Trade Commission's (the "FTC") attempt to block a merger between hospital systems. In an opinion issued June 20, 2016, Illinois U.S. District Judge Jorge Alonso denied the motion of the FTC and the State of Illinois (collectively, the "Plaintiffs") for a preliminary injunction prohibiting the merger of Advocate Health Care ("Advocate") and NorthShore University HealthSystem ("NorthShore") in suburban Cook and Lake Counties north of Chicago. The court reasoned that the Plaintiffs had failed to prove a relevant geographic market, and thus had not shown a likelihood of success on its claim that the Advocate-NorthShore merger would substantially lessen competition or create a monopoly in violation of the Clayton Act.

The Advocate-NorthShore decision comes just one month after a Pennsylvania federal judge—for similar reasons—denied the FTC's effort to enjoin the merger of Harrisburg-area Penn State Hershey Medical Center and PinnacleHealth System.[1] In denying the request for an injunction in the *Hershey* case, U.S. District Judge John E. Jones III also held that the FTC had failed to set forth a relevant geographic market, but then went on to conclude that anticompetitive effects would not arise through the merger. In particular, the court in *Hershey* found that the defendants presented a "compelling efficiencies argument in support of the merger," highlighting evidence that the merger would alleviate Hershey's capacity constraints by enabling it to transfer lower-acuity patients to Pinnacle and avoid an outpouring of capital on expansion, thereby serving more patients and keeping costs down. For more detail on the *Hershey* decision, see "FTC's Attempt to Block Hershey-Pinnacle Merger Rejected by Federal Court."

Background

Advocate is a health care system with eleven hospitals providing general acute care services, while the NorthShore system includes four hospitals. Both operate in the North Chicagoland area of northern Cook County and southern Lake County. The two signed an affiliation agreement in September 2014. The Plaintiffs took action to block the proposed merger late last year, including their request for a preliminary injunction to halt the merger pending an administrative trial on the Plaintiffs' antitrust claims.

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The Plaintiffs argued that the consolidation of the Advocate and NorthShore systems would create a 15-hospital system that would control more than 50% of general acute care services in a geographic market it referred to as the "North Shore Area," threatening competition and potentially harming consumers. The court, however, concluded that the Plaintiffs had not met their burden of showing a likelihood of success on the merits of its claim and denied the injunction, but granted a request for a temporary injunction while the case is pending before the U.S. Court of Appeals for the Seventh Circuit.

Decision

The determinative issue for the court—just as it was in the *Hershey* decision—was the Plaintiffs' failure to establish a relevant geographic market in which competition is allegedly threatened. But unlike the *Hershey* decision, the court's opinion in the Advocate-NorthShore case rested solely on the geographic market determination. While his decision described Advocate and NorthShore's plans to create a new, low-cost, high-performing network insurance product for the Chicago area, Judge Alonso did not comment on whether the defendants had established an efficiency defense, nor did he directly address the anticompetitive or procompetitive implications of the merger.

The Plaintiffs and their expert argued for a geographic market that included eleven hospitals in northern Cook County and southern Lake County—six of which were part of the proposed merged Advocate-NorthShore system. The Plaintiffs arrived at this market construction by including local hospitals and excluding so-called "destination" hospitals located in Chicago proper, and by including only those hospitals with at least a 2% share of patients from the areas in which Advocate and NorthShore attract patients, and which overlap in area with both Advocate *and* NorthShore. The Plaintiffs' expert concluded that the geographic market passed the "hypothetical monopolist" test, meaning that a hypothetical owner of *all* hospitals in the proposed market could profitably raise prices by a small but significant amount because the hospitals in the market are sufficiently close substitutes.

Advocate and NorthShore argued that the Plaintiffs' proposed geographic market was too narrow and its exclusion of the "destination hospitals" was arbitrary, noting that one such hospital—Northwestern Memorial Hospital—was the second or third choice for patients using many of the North Shore Area hospitals.

The court—which did not directly address the Plaintiffs' hypothetical monopolist

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conclusions—sided with the defendants, finding that the exclusion of destination hospitals from the Plaintiffs' asserted geographic market on the basis that patients preferred to receive general acute care services near home ignored "commercial realities" of the industry. The decision notes that with inpatient services on the decline, outpatient services and physician relationships play a large role in where a patient goes for inpatient care. Evidence that patients prefer to receive general acute care services near home was, in the court's words, "equivocal," with some testimony indicating that individuals in the Chicago area may work as far as 40 miles from where they live, and seek care at either location.

Because it found that the Plaintiffs had failed to meet their burden of proving a relevant geographic market, and thus had not established a likelihood of success on the merits, the court did not tackle the anticompetitive effects alleged by the Plaintiffs or consider whether enjoining the merger was in the public's best interest.

Conclusions and Additional Questions

The Plaintiffs have filed a notice of appeal of the *Advocate* decision to the U.S. Court of Appeals for the Seventh Circuit and the merger is temporarily enjoined pending that appeal. Likewise, the U.S. Court of Appeals for the Third Circuit granted the FTC's request for a stay in the *Hershey* case which prevents Hershey and Pinnacle from moving forward on the merger while the FTC's appeal of the lower court's decision is pending. Both the appellate court decisions likely will address how the FTC constructed the geographic market and whether the lower courts were correct in rejecting those constructions and both decisions will have substantial implications for FTC challenges to health care mergers going forward.

Legal counsel should be involved in the earliest stages of any considered merger in order to minimize the risk of an FTC challenge and to proactively develop defenses to any such challenge. If you would like to discuss a proposed merger or other contemplated transaction, or have questions about recent developments in antitrust challenges to health care mergers, please contact Larri Broomfield, Guy Temple or your Reinhart attorney.

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[1] *See FTC v. Penn State Hershey Med. Ctr.*, No. 1:15-cv-2362, 2016 WL 2622372 (M.D. Pa. May 9, 2016).

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